



United States
General Accounting Office
Washington, D.C. 20548

Accounting and Information
Management Division

B-271911

June 26, 1996

The Honorable William V. Roth, Jr.
Chairman, Permanent Subcommittee on
Investigations
Committee on Governmental Affairs
United States Senate

Dear Mr. Chairman:

This letter responds to your request for a review of disbursements made from 1993 through 1995 from the U.S. Marshals Service's seized asset deposit fund (SADF) for the Central District of California. Specifically, we assessed whether a sample of the total \$21.4 million of disbursements and \$93.3 million of transfers made during that period from the Central District's SADF were appropriate, including whether they were properly supported and authorized. For the sample of disbursements related to seized real property, we also determined whether the subject property appeared to be properly managed.

The U.S. Marshals Service (USMS) is responsible for managing property, such as financial instruments or personal or real property, seized by investigative agencies primarily within the Department of Justice. Currency that is seized and income received from seized rental properties are deposited into the SADF. As of December 31, 1995, the balance in the SADF for the Central District was \$59.1 million. According to USMS policy, authorized disbursements from this fund primarily include (1) remittances back to owners, (2) payments to innocent third parties, and (3) mortgage payments to the extent of rental income received on property. Disbursements for other purposes also may be made in response to court orders authorizing such disbursements. Funds may also be transferred from the SADF to the asset forfeiture fund¹ upon forfeiture of the seized property to the government.

¹The asset forfeiture fund is administered by USMS and is used to hold proceeds of forfeitures and to finance program-related expenses, as well as certain law enforcement activities directly related to the asset forfeiture program.

To perform our review, we selected a sample of 110 disbursements and 58 transfers made from 1993 through 1995 from the Central District's SADF as recorded in USMS' Financial Management System. In addition, we gained an understanding of the disbursement process in place at the time of our fieldwork.

RESULTS IN BRIEF

Concerning the propriety of the disbursements we reviewed, we identified part of one disbursement which was not paid consistent with the related court order. The court order stipulated that certain expenses be paid from sales proceeds; however, such expenses were paid from rental collections. In addition, we were unable to determine the appropriateness of three other disbursements in our sample due to lack of supporting documentation. We also found internal control weaknesses, some of which were due to a lack of adherence to written policies and procedures, that could result in unauthorized transactions being processed and not detected. These weaknesses consisted of (1) disbursements and transfers that were not properly authorized or that were authorized after the transaction occurred and (2) a lack of adequate segregation of duties over the disbursement process. Further, we also found inadequate management of seized real property, including instances where property deteriorated because of inadequate maintenance and mortgages were paid late. Because of these property management problems, the federal government has incurred unnecessary losses.

INTERNAL CONTROLS OVER PROCESSING DISBURSEMENTS AND TRANSFERS

Proper authorizations, supporting documentation, and segregation of duties are key to ensuring that disbursements and transfers are appropriate. As part of our review, we reviewed written procedures and tested selected transactions to determine if such processes and internal controls were in place for disbursements and transfers from the SADF.

Authorizations provide assurance that designated staff have reviewed transactions for accuracy and approved them prior to payment. In accordance with USMS procedures, certifying officers review the supporting documentation for a disbursement and sign the voucher. Prior to signing a check, disbursing officers ensure that the voucher has been certified. Both certifying and disbursing officers are required to be approved by USMS headquarters before they can authorize disbursements. We found the following instances in which disbursements and transfers were not properly authorized or were authorized after the transaction occurred:

- A disbursement made from rent collections to a lienholder included \$5,037 for hazard insurance, legal fees, and appraisal fees. However, based on a court order, only principal and interest should have been paid from rents collected. Advances for unpaid hazard insurance, legal fees, and appraisal fees were to be paid from proceeds of the future sale of the property.
- Eight vouchers totaling \$761,319 from our sample of disbursements were certified by an individual who was not approved by USMS headquarters to certify vouchers. Two other vouchers totaling \$55,710 were certified and one check for \$572,644 was signed by an individual prior to receiving USMS headquarters approval to function as a certifying or disbursing officer.
- All certifications for the transfers we reviewed were signed after the transaction occurred. Fifteen were certified more than 1 week after the transactions occurred, and there was no certification for three transfers made in 1994 and 1995.

Maintaining proper supporting documentation, such as vouchers and court orders authorizing transactions, is essential for ensuring validity and for audit trail purposes. We found the following instances in which adequate supporting documentation was not provided:

- We were unable to review the original case files for 13 of the 110 disbursements and 11 of the 58 transfers. According to the Central District, these case files had been microfilmed and sent to archives; however, it was unable to locate the original files and did not have a usable microfilm reader available to review the copied files. We subsequently requested that support be provided for 9 of the 13 disbursements that we judgmentally selected due primarily to the nature of the check payee (e.g., checks issued to individuals or private companies as opposed to other government agencies). USMS was unable to provide support for two disbursements totaling \$38,867.
- USMS could not provide adequate supporting documentation for a \$17,456 disbursement. The case file included instructions from the U.S. Attorney to "comply with the attached order"; however, the attached order and other supporting documentation within the file did not identify the vendor that was paid.

Proper segregation of duties ensures that no individual controls all key duties of a transaction and reduces the risk that unauthorized checks could be written and diverted. In the Central District, we found inadequate segregation of duties, because the same individual (1) manually types payee information on the check,

(2) enters the check information into the accounting system, (3) presents the check for signature, and (4) is typically also responsible for the distribution of those checks.

In connection with gaining an understanding of the disbursement process in place at the time of our review, we found the following two additional problems:

- In 13 instances, USMS was not timely in issuing checks or transferring funds. Timely disbursements are equitable for recipients and timely transfers are important so that funds do not remain in the SADF unnecessarily. In addition, USMS policy requires that funds be transferred to the asset forfeiture fund within 30 days upon receipt of instructions to do so. In 2 instances, it took USMS over 5 months to issue a check, and in 11 instances it took USMS over 30 days to transfer funds from the SADF to the asset forfeiture fund. In one of these instances, it took USMS over 2 years to transfer the funds.
- Transfers within the SADF (e.g., when there is a change in case numbers) do not involve actual disbursements, however such transactions are recorded in the accounting system and reported as both a disbursement and a collection. As a result, reported disbursement and collection activity is often significantly overstated. For example, our sample included 16 transfers, totaling approximately \$3.5 million, which represented appropriate transactions within SADF, but not actual disbursements.

REAL PROPERTY MANAGEMENT IS INADEQUATE

Our review of disbursements involving payments to maintain or manage real property revealed instances of inadequate property management during the period covered by our review. USMS' Central District of California contracts with a property management company to perform the day-to-day management of seized real property and is responsible for overseeing the contractor. The property management objective is to provide efficient and effective management and disposal of seized and forfeited property as well as to maintain the value and condition of the property. We found similar property management problems as those previously reported in our high-risk series reports² and by the Department of Justice's Office of Inspector General. Examples of poor property management found during our review include:

- A 78-acre horse ranch, race track, and training facility with one main residence, a heated pool, one apartment, and other structures was seized in

²High-Risk Series: Asset Forfeiture Programs (GAO/HR-95-7, February 1995).

November 1989 and appraised for \$4.69 million in March 1990. Subsequent appraisals indicated a trend in declining values with one dated August 1995 showing a value of \$523,000. Over these 5 years, the property remained idle and deteriorated as evidenced by photographs in the file which showed significant deterioration and vandalism. In addition, inspection reports prepared by USMS and the property manager state that the property is "trashed," "demolished," "a fire hazard," "in a dangerous condition," and that the "buildings are near collapse." An inspection report dated May 1992 stated that a 500-foot fence had been installed, and that "many tons of trash had been dumped."

Despite the significant original appraised value of and vandalism to this property, USMS had only paid approximately \$25,000 through April 1996 to manage and maintain this property, including about \$130 a month in management fees. Due to the significant deterioration of this property and a stipulation in a 1993 court order which guarantees the owner \$1.25 million once the property is sold, a significant loss could be incurred by the federal government.

- An 18-unit apartment building was seized in February 1991. While in USMS' possession, the property's roof suffered serious maintenance problems, thereby exposing the government to potential liabilities. In January 1993, one of the tenants reported that her entire bedroom ceiling had collapsed and by February 1993, eight of the eighteen units could not be rented due to the condition of the roof. In addition, mortgage payments on this property were paid late. The property was eventually turned over to the lienholder in April 1994 at a loss to the federal government of approximately \$105,000.
- A five-unit rental property was seized in January 1991. Each month, the property management company collected rents from the tenants, deducted the mortgage amount, and submitted the remainder to USMS to be deposited into SADF. In April 1995, USMS received a letter from the lienholder informing them that the mortgage was overdue by over a year's worth of mortgage payments. USMS paid the lienholder over \$25,000 in June 1995, which included principal, interest, late fees, appraisal fees, legal fees, and hazard insurance from the SADF. As of the completion of our fieldwork, USMS had not reconciled with the property management company the deficiency in the mortgage payments.

AGENCY COMMENTS

We provided a draft of this report to officials of the U.S. Marshals Service for their comment. In general, they agreed with our findings and acknowledged that

significant problems existed in the management of seized assets in the Central District of California during the time period covered by our review. They told us that the senior district management team, established in late 1994, and headquarters have undertaken a concerted and continual effort to rebuild the district's seized asset unit including taking the following key actions:

- Headquarters provided staffing, training, and automated data processing resources to assist in the district's ongoing efforts to reconstruct and reconcile old case files.
- The district was allocated additional personnel and is recruiting for experts in real estate and property management.
- In May 1995, the district and headquarters reconciled their records to ensure that the documentation of authorized certifying and disbursing officers was consistent.
- Headquarters recently engaged independent public accountants to (1) audit the past and present performance of the district's real property management contractor and (2) review the district's real property inventory and assist the district in expediting appropriate disposition of properties held.

Our sample of 110 disbursements included all disbursements of \$100,000 or more, a random sample of disbursements less than \$5,000, and a judgmental sample of the remaining unselected disbursements. The sample of 58 transfers included all transfers of at least \$500,000, a judgmental sample of transfers less than \$500,000, and a random sample of the remaining unselected transfers. These samples represented about 74 percent and 38 percent of the Central District's total disbursements and transfers, respectively, made from 1993 through 1995. We selected our samples from the Central District's Financial Management System and relied on those records as being complete. Due to time constraints, the scope of our work did not include performing reconciliations of bank accounts or other audit procedures to verify the completeness of our population. We performed our work from April through May 1996 in accordance with generally accepted government auditing standards.

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We are sending copies of this letter to the Director of the U.S. Marshals Service and U.S. Marshal for the USMS Central District of California. If you need further information, please contact me at (202) 512-9510, or Gary Engel, Assistant Director, at (202) 512-8815.

Sincerely yours,



Gregory M. Holloway
Director, Governmentwide Audits

(901700)

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