

GAO

Report to the Chairman, Subcommittee
on Government Management, Finance,
and Accountability, Committee on
Government Reform, House of
Representatives

March 2005

FINANCIAL MANAGEMENT

Challenges in Meeting Requirements of the Improper Payments Information Act





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Highlights of [GAO-05-417](#), a report to the Chairman, Subcommittee on Government Management, Finance, and Accountability, Committee on Government Reform, House of Representatives

Why GAO Did This Study

Fiscal year 2004 marked the first year that federal agencies governmentwide were required to report improper payment information under the Improper Payments Information Act of 2002 (IPIA). The increasing scope of reporting over the past several years has demonstrated that improper payments are a significant and widespread problem in federal agencies, and in the past a limited number of agencies reported in their Performance and Accountability Reports (PAR) annual payment accuracy rates and estimated improper payment amounts.

Because of your continued interest in addressing the governmentwide improper payments issue, you asked GAO to report on (1) the extent to which agencies have performed the required assessments to identify programs and activities that are susceptible to significant improper payments and (2) the annual amount estimated for improper payments by the agencies.

What GAO Recommends

GAO is making three recommendations to the Office of Management and Budget (OMB) to help ensure successful implementation of the IPIA requirements. OMB commented that its management emphasis and inspector general oversight offer sufficient incentives to ensure agencies meet IPIA requirements.

www.gao.gov/cgi-bin/getrpt?GAO-05-417.

To view the full product, including the scope and methodology, click on the link above. For more information, contact McCoy Williams at (202) 512-6906 or williamsm1@gao.gov.

What GAO Found

The federal government made progress in identifying programs susceptible to the risk of improper payments in response to the new IPIA requirements. The fiscal year 2004 PARs for 29 of 35 federal agencies that are significant to the U.S. government's consolidated financial statements show that even with the enhanced emphasis on improper payment reporting fueled by the new legislation, 6 agencies reported that they did not perform risk assessments of all their programs.

The magnitude of the governmentwide improper payment problem is still unknown, because agencies have not yet prepared estimates of improper payments for all of their programs. In the 29 agency PARs included in GAO's fiscal year 2004 review, 17 agencies reported over \$45 billion of improper payments in 41 programs governmentwide. This represented almost a \$10 billion, or 27 percent, increase in the amount of improper payments reported by agencies in fiscal year 2003. This increase was primarily attributable to changes in the method for estimating and reporting improper payment amounts in one major program. Looking forward, future estimates are likely to trend higher because the governmentwide estimate did not include 12 programs with outlays of \$248.7 billion in fiscal year 2004 that were required to annually report improper payments under OMB Circular No. A-11 during the past 3 years. This included some of the largest risk-susceptible federal programs, such as the Department of Health and Human Services' Medicaid Program, with outlays exceeding \$175 billion annually, or the Department of Education's Title I Program, with outlays of over \$10 billion annually.

Number of Agencies and Amounts of Improper Payments Reported (Fiscal Years 1999-2004)

Fiscal year	Number of agencies reporting improper payments ^a	Reported amounts of improper payments (in billions)
1999	8	\$20.7
2000	8	\$19.6
2001	8	\$20.9
2002	7	\$19.5
2003	13	\$35.7
2004	17	\$45.4

Source: GAO.

^a Other agencies acknowledged making improper payments in their PARs but did not disclose dollar amounts.

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Abbreviations

CFO	Chief Financial Officer
IPIA	Improper Payments Information Act of 2002
MD&A	Management Discussion and Analysis
OMB	Office of Management and Budget
PAR	Performance and Accountability Report
PMA	President's Management Agenda

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United States Government Accountability Office
Washington, D.C. 20548

March 31, 2005

The Honorable Todd R. Platts
Chairman
Subcommittee on Government Management,
Finance, and Accountability
Committee on Government Reform
House of Representatives

Dear Mr. Chairman:

Federal agencies expended a record \$2.3 trillion through thousands of programs and activities to address the needs of the American people in fiscal year 2004. As the steward of taxpayer dollars, the federal government is accountable for how its agencies and grantees spent this money, including the safeguarding of federal funds from improper payments. Our work over the past several years has demonstrated that improper payments are a significant and widespread problem in the federal government, with only a limited number of agencies reporting in their Performance and Accountability Reports (PAR) the annual payment accuracy rates and estimated improper payment amounts. Fiscal year 2004 marked the first year that federal agencies governmentwide were required to report improper payment information under the Improper Payments Information Act of 2002 (IPIA).¹ The IPIA raised improper payments to a new level of importance by requiring agency heads, based on guidance from the Office of Management and Budget (OMB),² to identify programs and activities susceptible to improper payments, estimate the amount of their improper payments, and report on the amount of and their actions to reduce their improper payments.

An improper payment is defined by the IPIA as an amount that should not have been paid or was paid for an incorrect amount. Specifically, improper payments include inadvertent errors, such as duplicate payments and calculation errors; payments for unsupported or inadequately supported claims; payments for services not rendered or rendered to ineligible beneficiaries; and payments resulting from fraud and abuse. The OMB

¹Pub. L. No. 107-300, 116 Stat. 2350 (Nov. 26, 2002).

²OMB Memorandum M-03-13, "Improper Payments Information Act of 2002 (Public Law 107-300)," May 21, 2003.

implementation guidance requires that estimates, and if applicable, a corrective action report, be included in federal agencies' PARs beginning with fiscal year 2004.

Prior to the IPIA, OMB Circular No. A-11, *Preparation and Submission of Budget Estimates*, Section 57, "Information on Erroneous Payments,"³ required 46 programs in 15 agencies to annually report improper payment information. Last year we testified on the federal agencies that reported under OMB Circular No. A-11.⁴ We noted that federal agency fiscal year 2003 PARs typically contained limited amounts of improper payment information. Historically, relatively few federal agencies and their components have publicly reported improper payment information. Estimates reported for fiscal year 2003 were about \$36 billion annually for major federal benefit programs required to report under OMB Circular No. A-11. These programs managed payments in excess of \$1.2 trillion annually. Importantly, this estimate did not account for payments made by all federal programs and activities, which totaled over \$2.1 trillion in fiscal year 2003. Not only did the enactment of the IPIA expand the range of agencies, it also expanded the programs agencies are required to assess for improper payments to include all federal programs and payments.

Because of your continued interest in addressing the governmentwide improper payments issue, you asked us to report on the progress being made by agencies in complying with certain requirements of the IPIA. This report summarizes (1) the extent to which agencies have performed the required assessments to identify programs and activities that are susceptible to significant improper payments and (2) the annual amount estimated for improper payments by the agencies.

To respond to your request, we conducted a review of improper payment information reported by agencies in their fiscal year 2004 PARs. We further reviewed OMB guidance on implementation of the IPIA and its report on the results of agency-specific reports, significant findings, agency accomplishments, and remaining challenges. We did not assess the

³Section 57 was eliminated from OMB Circular No. A-11. See OMB Circular No. A-11, *Transmittal Memorandum #77*, July 25, 2003. App. I lists the 15 agencies and 46 programs previously cited in Section 57.

⁴GAO, *Financial Management: Fiscal Year 2003 Performance and Accountability Reports Provide Limited Information on Governmentwide Improper Payments*, [GAO-04-631T](#) (Washington, D.C.: Apr. 15, 2004).

effectiveness of the agencies' efforts or independently validate the data that they or OMB reported. The results of our review are detailed in this report. We conducted our work from November 2004 through February 2005 in accordance with U.S. generally accepted government auditing standards. Appendix I contains further details on our scope and methodology. OMB provided written comments on a draft of this report that are reprinted in appendix V.

Results in Brief

In response to the new IPIA requirements, agencies overall made progress in identifying programs susceptible to the risk of improper payments. At the same time, our reviews of the fiscal year 2004 PARs for 29 of 35 federal agencies⁵ that are significant to the U.S. government's consolidated financial statements show that even with the enhanced emphasis on improper payment reporting fueled by the new legislation, certain agencies did not perform risk assessments of all their programs. Specifically, 23 of the 29 agencies we reviewed reported that they had completed risk assessments for all programs and activities.

The magnitude of the governmentwide improper payment problem is still unknown because, in addition to not assessing all programs, the agencies had not yet prepared estimates of significant improper payments for all of the programs that they determined were susceptible to the risk of improper payments. In the 29 agency PARs included in our fiscal year 2004 review, 17 agencies reported over \$45 billion of improper payments in 41 programs. This represented almost a \$10 billion, or 27 percent, increase in the dollar amount of improper payments reported by agencies in fiscal year 2003. However, we determined that this increase was primarily attributable to changes in the method for estimating and reporting improper payment amounts in one program. Further, the governmentwide estimate did not include 12 programs with total outlays of \$248.7 billion in fiscal year 2004 that were required to annually report improper payments under OMB Circular No. A-11 during the past 3 years. This included some of the largest risk-susceptible federal programs, such as the Department of Health and Human Services' Medicaid Program, with outlays exceeding \$175 billion annually, or the Department of Education's Title I Program, with outlays of

⁵See *Treasury Financial Manual*, vol. 1, part 2, ch. 4700, for a list of the 35 agencies. Six of the 35 agencies had not issued PARs as of our fiscal year 2004 audit report on the U.S. government's consolidated financial statements, dated December 14, 2004; therefore, these agencies were not included in our review.

over \$10 billion annually. Eight of these 12 programs reported that they would be able to estimate and report on improper payments sometime within the next 4 years, but the remaining 4 were silent as to when they would report estimates in the future.

We are making three recommendations to OMB to help ensure successful implementation of IPIA requirements. In its comments, OMB emphasized that in fiscal year 2004, federal agencies established a strong foundation for measuring improper payments, identifying and implementing the necessary corrective actions, and tracking success over time. OMB also pointed out that there are already procedures in place for the 15 federal agencies under the new President's Management Agenda (PMA) initiative to meet the objectives of our recommendations and sufficient incentives and disincentives for ensuring that agencies meet the necessary IPIA requirements. However, our recommendations focus on all federal agencies meeting the IPIA requirements and are directed at any agency that does not do so or agencies that may benefit from incentives such as gain sharing to fund efforts to reduce improper payments.

Background

The PMA issued in 2001 targeted improper payments as an area with opportunities for improvement. The PMA included five governmentwide initiatives—one of which is improved financial management, which expressly addresses improper payments as a priority. This initiative called for the administration to establish a baseline on the extent of erroneous payments. Under it, agencies were to include in their 2003 budget submissions to OMB information on improper payment rates, including actual and target rates where available, for benefit and assistance programs over \$2 billion. The PMA also noted that using this information, OMB will work with agencies to establish goals to reduce improper payments identified in their programs.

In July 2001, as part of its efforts to advance the PMA initiative, OMB revised Circular No. A-11 to require 16 federal agencies (15 of the then 24 Chief Financial Officer's (CFO) Act agencies and the Railroad Retirement Board) to submit improper⁶ payment data, assessments, and action plans for about 50 programs to OMB with their initial budget submissions. Specifically, the circular required that agencies submit information

⁶OMB's guidance uses the term erroneous payments rather than improper payments. We consider the terms synonymous.

including estimated improper payment rates, target rates for future reductions in these payments, the types and causes of these payments, and variances from targets or goals established. In addition, agencies were to provide a description and assessment of the current methods for measuring the rate of improper payments and the quality of data resulting from these methods. Agencies were to first include this improper payment information in their initial fiscal year 2003 budget submissions. A June 2002 revision to the circular removed the Agency for International Development from the list and reduced the number of programs for which improper payment information was required to 46. (App. II lists the agencies and programs.)

In November 2002, the Congress passed the IPIA. The law requires agency heads to annually review all programs and activities that they administer and identify those that may be susceptible to significant improper payments.⁷ Once agencies identify their susceptible programs, the act requires them to estimate and report on the annual amount of improper payments in those programs and activities. For programs for which estimated improper payments exceed \$10 million, agencies are to report annually to the Congress on the actions they are taking to reduce those payments. The report is also to include a discussion of the causes of the improper payments identified, actions taken to correct those causes, and the results of the actions taken to address those causes.

The act further requires OMB to prescribe guidance for federal agencies to use in implementing the act. OMB issued this guidance in Memorandum M-03-13 in May 2003. It requires use of a systematic method to annually review and identify those programs and activities that are susceptible to significant improper payments. OMB guidance defines significant improper payments as annual improper payments in any particular program exceeding both 2.5 percent of program payments and \$10 million. The OMB guidance then requires agencies to estimate the annual amount of improper payments using statistically valid techniques for each susceptible program

⁷The law defines “payment” as any payment (including a commitment for future payment, such as a loan guarantee) that is (1) made by a federal agency, a federal contractor, or a governmental or other organization administering a federal program or activity and (2) derived from federal funds or other federal resources or that will be reimbursed from federal funds or other federal resources. The law defines an “improper payment” as (1) any payment that should not have been made or that was made in an incorrect amount (including overpayments and underpayments) under statutory, contractual, administrative, or other legally applicable requirements and (2) any payment to an ineligible recipient, any payment for an ineligible service, any duplicate payment, payment for services not received, and any payment that does not account for credit for applicable discounts.

or activity. For those agency programs determined to be susceptible to significant improper payments and with estimated annual improper payments greater than \$10 million, the IPIA and related OMB guidance require each agency to report the results of its improper payment efforts in the Management Discussion and Analysis (MD&A) section of its PAR for fiscal years ending on or after September 30, 2004. The IPIA requires the following information in their reports:

- a discussion of the causes of the improper payments identified, actions taken to correct those causes, and results of the actions taken to address those causes;
- a statement of whether the agency has the information systems and other infrastructure it needs in order to reduce improper payments to the agency's targeted levels;
- if the agency does not have such systems and infrastructure, a description of the resources the agency has requested in its most recent budget submission to obtain the necessary information systems and infrastructure; and
- a description of the steps the agency has taken and plans to take to ensure that agency managers (including the agency head) are held accountable for reducing improper payments.

OMB's guidance in M-03-13 requires that three additional things be included in the report:

- a discussion of the amount of actual erroneous payments that the agency expects to recover and how it will go about recovering them;
- a description of any statutory or regulatory barriers that may limit the agency's corrective actions in reducing erroneous payments; and
- provided the agency has estimated a baseline erroneous payment rate for the program, a target for the program's future erroneous payment rate that is lower than the agency's most recent estimated error rate.

On July 22, 2004, OMB, working with the CFO Council's Improper Payments Committee, issued a standardized reporting format, or framework, for reporting IPIA information. This framework was included as Attachments 2 and 3 to OMB Memorandum M-04-20, "Fiscal Year 2004

Performance and Accountability (PAR) and Reporting Requirements for the Financial Report of the United States Government.” To satisfy the reporting requirements of the IPIA for fiscal year 2004, the framework instructed agencies to provide a brief summary of both what they have accomplished and what they plan to accomplish in the MD&A portion of the fiscal year 2004 PAR. All other required reporting details are to be included in an appendix to the PAR. The framework for the information reported in the appendix incorporates the requirements set forth in the law and further illustrates the reporting format required in OMB’s implementation guidance. Under accelerated financial reporting requirements of the PMA, agency fiscal year 2004 PARs were due November 15, 2004. Accordingly, the first set of reports representing the results of agencies’ assessing improper payments for all federal programs in accordance with the IPIA and OMB guidance were due in November 2004.

In August 2004, OMB established Eliminate Improper Payments as a new program-specific initiative.⁸ With this new program initiative, agencies are to measure their improper payments annually, develop improvement targets and corrective actions, and track the results annually to ensure the corrective actions are effective. This initiative is also to have its own scorecard requirements and rating beginning with fiscal year 2005. With the establishment of this new program-specific initiative, agency efforts to address improper payment issues will no longer be tracked under the governmentwide initiative, Improved Financial Performance.

In our December 2004 report on the U.S. government’s consolidated financial statements for the fiscal years ended September 30, 2004 and 2003, which includes our associated opinion on internal control, we reported that while most agencies acknowledged the IPIA reporting requirements in their PARs, they did not always indicate whether they had

⁸The PMA issued in 2001 included nine program initiatives, including reform of food aid programs. When OMB issued this August 2004 report to federal employees, the reform of food aid program initiative was the only initiative not carried forward from the 2001 PMA. OMB also added two new program initiatives—(1) Strengthen Real Property Management and Optimize the Use of Federal Property and (2) Eliminate Improper Payments. As a result to these changes, 10 program-specific initiatives are currently in place under the PMA.

completed agencywide assessments, and they did not estimate improper payments for all of their susceptible⁹ programs.

Progress Made but Challenges Remain in Assessing Programs for Risk of Significant Improper Payments

In response to the new requirements of the IPIA, agencies overall made progress in identifying programs susceptible to the risk of improper payments. At the same time, our reviews of the fiscal year 2004 PARs for 29 of 35 federal agencies¹⁰ that are significant to the U.S. government's consolidated financial statements suggest that even with the enhanced emphasis on improper payment reporting fueled by the new legislation, certain agencies have not yet performed risk assessments of all their programs. Appendix III lists the agencies included in this review.

In its guidance on implementing the IPIA, OMB required agencies to institute a systematic method of inventorying all programs and activities and identifying those the agency believes are susceptible to the risk of significant error. OMB further instructed agencies to describe, in their PARs, the risk assessments performed.

We determined that 23 of the 29 agencies reviewed reported that they had completed risk assessments for all programs and activities. Of the 15 agencies with prior reporting requirements under OMB Circular No. A-11, 12 reported that they had performed comprehensive inventories and assessed the risk of improper payments for all their programs and activities. Three of the 15 agencies stated that their risk assessments were not complete for all programs and activities. Of those 14 agencies without prior reporting requirements, 11 agencies reported that they had completed risk assessments for all programs and activities, whereas 3 agencies reported that they had not.

Recognizing weaknesses in agency risk assessments, three agency auditors cited noncompliance with the IPIA in their annual auditor's reports included in the agency PARs. For example, two agency auditors each reported that their agency's risk assessment did not consider all payment types or programs. Another auditor reported the agency did not institute a

⁹In determining which programs are susceptible to significant improper payments, OMB defines significant erroneous payments as those annual erroneous payments in a program exceeding both 2.5 percent of program payments and \$10 million.

¹⁰See *Treasury Financial Manual*, vol. 1, part 2, ch. 4700, for a list of the 35 agencies.

systematic method of reviewing all programs and identifying those it believed were susceptible to significant erroneous payments.

Magnitude of Improper Payments Is Still Unknown

Once agencies have identified programs that may be susceptible to significant improper payments, developing statistically valid estimates of the amounts of improper payments for their programs and activities has been a further challenge. Appendix IV lists the 29 agencies and 70 programs for which we reviewed fiscal year 2004 PARs for improper payment reporting. In the 29 agency PARs included in our review, 17 agencies reported over \$45 billion of improper payments in 41 programs. This represented almost a \$10 billion, or 27 percent, increase in the dollar amount of improper payments reported by agencies in fiscal year 2003. However, we determined that this increase was primarily attributable to changes in the method for estimating and reporting improper payment amounts in the Department of Health and Human Services' Medicare Program. The 24 agency programs with no prior reporting requirements reported improper payment estimates that did not significantly increase the governmentwide total.

As discussed earlier, OMB Circular No. A-11 has required certain agencies to report selected improper payment information on 46 programs to OMB beginning 3 years ago with their fiscal year 2003 budget submissions. We found that for 34 of the programs, agencies reported estimates in their fiscal year 2004 PARs or stated that improper payment amounts were insignificant.

As shown in table 1, the governmentwide estimate did not include the remaining 12 programs with total outlays of \$248.7 billion in 2004. This included some of the largest risk-susceptible federal programs, such as the Department of Health and Human Services' Medicaid Program, with outlays exceeding \$175 billion annually, or the Department of Education's Title I Program, with outlays of over \$10 billion annually.

Table 1: Programs Required to Report under A-11 and Projected Year of Improper Payment Estimates

Program	Fiscal year 2004 outlays (in billions)	Target fiscal year for estimate				Did not report
		2005	2006	2007	2008	
Department of Agriculture – Agriculture Marketing and Assistance	\$8.8	X				
Department of Health and Human Services – Foster Care – Title IV-E	4.7	X				
Department of Health and Human Services – State Children’s Insurance Program	4.6	X				
Department of Health and Human Services – Child Care and Development Fund	4.8	X				
Small Business Administration – 7(a) Business Loan Program	.7	X				
Department of Health and Human Services – Medicaid	175.3		X			
Department of Agriculture – School Programs	8.4			X		
Department of Agriculture – Women, Infants, and Children Program	4.8				X	
Department of Labor – Workforce Investment Act	3.1					X
Department of Education – Title I	10.3					X
Department of Health and Human Services – Temporary Assistance for Needy Families	17.7					X
Department of Housing and Urban Development – Community Development Block Grant	5.5					X
Total	\$248.7	5	1	1	1	4

Sources: Cited agencies’ fiscal year 2004 PARs and OMB.

The table further shows that of these 12 programs, 8 reported that they would be able to estimate and report on improper payments sometime within the next 4 years, but could not do so now. The other 4 programs in 4 agencies did not estimate improper payment amounts for their programs and were silent as to whether they would report estimates in future reports. As a result, improper payments for several large risk-susceptible programs will not become transparent for several or an undetermined number of years, although these agencies were required to report such information since their fiscal year 2003 budget submissions. Moreover, by only looking at those agencies significant to the U.S. consolidated financial statements, this estimate does not include all of the agencies subject to the IPIA.

OMB reported that in certain risk-susceptible programs, agencies were unable to determine the rate or amount of improper payments due to measurement challenges as well as time and resource constraints, which OMB expects to be resolved in the future. Although OMB reported that the

\$45 billion in improper payments will be used as a baseline on which short- and long-term program improvements and strategies will be based, it recognizes that fiscal year 2005 reductions in improper payments will be affected by outlay changes as well as the identification of new improper payments as additional programs are measured and methodologies for currently measured programs are enhanced.

Conclusions

Measuring improper payments and designing and implementing actions to reduce or eliminate them are not simple tasks. The ultimate success of the governmentwide effort to reduce improper payments depends, in part, on each federal agency's continuing diligence and commitment to comply fully with the requirements of the act and the related OMB guidance. The level of importance each agency, the administration, and the Congress place on the efforts to implement the act will determine its overall effectiveness and the level to which agencies reduce improper payments and ensure that federal funds are used efficiently and for their intended purposes. Without such efforts, the likelihood of designing and implementing actions governmentwide to reduce or eliminate improper payments is doubtful. Fulfilling the requirements of the IPIA will require sustained attention to implementation and oversight to monitor whether desired results are being achieved.

Recommendations for Executive Action

We are making three recommendations to help ensure the successful implementation of the Improper Payments Information Act of 2002 and its goal of enhancing the accuracy and integrity of federal payments. Specifically, we recommend that the Director of OMB:

- Require those agencies that did not address the IPIA requirements or did not perform risk assessments of all of their programs and activities to establish time frames and identify resources needed to perform risk assessments and satisfy reporting requirements.
- Develop a plan to address the resource needs of those agencies that did not perform risk assessments or satisfy reporting requirements.
- Consider as part of the budget process, for any agency that OMB deems to have not taken the IPIA requirements seriously or that has lagged behind, the feasibility of disincentives for poor performance, such as

reductions in funds for the program involved or adding incentives such as gain sharing for making substantive progress.

Agency Comments and Our Evaluation

In its written comments on a draft of this report, which are enclosed in appendix V, OMB emphasized that in fiscal year 2004, federal agencies established a strong foundation for measuring improper payments, identifying and implementing the necessary corrective actions, and tracking success over time. OMB's response further discussed key findings included in its report, *Improving the Accuracy and Integrity of Federal Payments*, which was issued on January 25, 2005.

With regard to our first recommendation that agencies establish time frames and identify resources needed to perform risk assessments and satisfy reporting requirements, OMB stated that pursuant to the PMA initiative called Eliminate Improper Payments, federal agencies are already required to submit relevant time frames and account for the resources necessary to complete planned actions. Further, OMB stated that the remaining risk assessments to be completed correlate to programs with relatively small outlays. While we view the PMA initiative as a positive action, it applies to 15 agencies, 3 of which we found had not yet assessed all their programs. Three other agencies—the Farm Credit System Insurance Corporation, the National Credit Union Administration, and the Pension Benefit Guaranty Corporation—which are not included in the PMA initiative and therefore are not required to establish time frames and account for needed resources, have outlays that are significant to the U.S. government's consolidated financial statements and were silent with respect to IPIA requirements in their fiscal year 2004 PARs. In addition to these three agencies, the PMA initiative would also not cover those agencies that while not significant to the U.S. government's consolidated financial statements, are subject to the IPIA. Our recommendation is directed to the broader range of agencies.

Regarding our second recommendation that OMB develop a plan to address resource needs of agencies that did not perform risk assessments or satisfy reporting requirements, OMB stated that agency plans for addressing IPIA reporting requirements are closely considered in identifying agency resource needs and preparing the President's Budget. While we agree with OMB on that point, as discussed in our response to OMB's comments on the first recommendation, certain agencies are not required to submit plans that include time frames and resource needs to

OMB. As a result, resource needs may not be addressed in the budget process.

With respect to our third recommendation that it consider using incentives and disincentives, as applicable, for quick and timely action for meeting the IPIA requirements, OMB offered the view that the requirements of the PMA and inspector general reviews of agency IPIA activities provide sufficient incentive for ensuring that agencies meet the necessary requirements. We agree that these requirements will help ensure that agencies take the IPIA seriously. Our recommendation is directed at any agency that does not do so or agencies that may benefit from incentives such as gain sharing to fund efforts to reduce improper payments. Again, as discussed above, while the major 15 agencies are covered by the PMA, 3 of these had not yet assessed all their programs and a number of agencies not covered under the PMA initiative, but significant to the U.S. government's consolidated financial statements, were silent with respect to the IPIA requirements.

OMB's written comments and our evaluation of one comment not addressed above are presented in appendix V.

As agreed with your office, unless you publicly announce its contents earlier, we plan no further distribution of this report until 30 days from its date. At that time, we will send copies of the report to interested congressional committees. We will also be sending copies to the Director of the Office of Management and Budget and the heads of the agencies included in our scope of review. We will make copies available to others upon request. In addition, the report will be available at no charge on the GAO Web site at <http://www.gao.gov>.

Should you or your staff have any questions on matters discussed in this report, please contact me at (202) 512-6906 or williamsm1@gao.gov.

Additional contacts and major contributors to this report are provided in appendix VI.

Sincerely yours,

A handwritten signature in black ink that reads "McCoy Williams". The signature is written in a cursive style with a large, prominent "M" and "W".

McCoy Williams
Director, Financial Management and Assurance

Scope and Methodology

This report is based on our review of agency fiscal year 2004 Performance and Accountability Reports (PAR). We reviewed the fiscal year 2004 PARs of 29 of 35 agencies¹ that are significant to the U.S. government's consolidated financial statements to obtain information on the status of their implementation of the Improper Payments Information Act of 2002 (IPIA) and the related Office of Management and Budget (OMB) implementation guidance. We paid particular attention to the 15 agencies with prior improper payment reporting requirements for 46 of their programs under OMB Circular No. A-11, Section 57. A list of the agencies with prior reporting requirements is presented in appendix II. In addition, we reviewed relevant agency documents, including strategic plans, agency performance plans and reports, agency audit reports, and reports from agency program partners.²

We completed reviews of fiscal year 2004 PARs for 29 agencies identifying 70 key programs. Appendix III lists the agencies and programs included in this review. To supplement our review and analysis, we contacted agencies to clarify responses, requested additional information, and updated the initial responses. We did not determine the validity of representations made or the documentation provided.

We performed our work in Washington, D.C., from November 2004 through February 2005 in accordance with U.S. generally accepted government auditing standards.

¹See *Treasury Financial Manual*, vol. 1, part 2, ch. 4700, for a list of the 35 agencies. Six of the 35 agencies had not issued PARs as of our fiscal year 2004 audit report on the U.S. government's consolidated financial statements, dated December 14, 2004; therefore, these agencies were not included in our review.

²Program partners can include other agencies or intermediaries responsible for carrying out different aspects of the program and might include federal agencies, states or localities, grant recipients, participating financial institutions, regulated bodies, and contractors.

Agencies and Related Programs for Which OMB Circular No. A-11 Required Erroneous Payment Information

Agency	Program or activity
1. Department of Agriculture	1. Food Stamp Program
	2. Commodity Loan Program
	3. National School Lunch and Breakfast
	4. Women, Infants, and Children
2. Department of Defense	5. Military Retirement Fund
	6. Military Health Benefits
3. Department of Education	7. Student Financial Assistance
	8. Title I
4. Department of Health and Human Services	9. Head Start
	10. Medicare
	11. Medicaid
	12. Temporary Assistance for Needy Families
	13. Foster Care – Title IV-E
	14. State Children's Insurance Program
	15. Child Care and Development Fund
5. Department of Housing and Urban Development	16. Low Income Public Housing
	17. Section 8 Tenant Based
	18. Section 8 Project Based
	19. Community Development Block Grants
6. Department of Labor	20. Unemployment Insurance
	21. Federal Employee Compensation Act
	22. Workforce Investment Act
7. Department of the Treasury	23. Earned Income Tax Credit
8. Department of Transportation	24. Airport Improvement Program
	25. Highway Planning and Construction
	26. Federal Transit – Capital Investment Grants
	27. Federal Transit – Formula Grants
	28. Compensation
9. Department of Veterans Affairs	29. Dependency and Indemnity Compensation
	30. Pension
	31. Insurance Programs
10. Environmental Protection Agency	32. Clean Water State Revolving Funds
	33. Drinking Water State Revolving Funds

Appendix II
Agencies and Related Programs for Which
OMB Circular No. A-11 Required Erroneous
Payment Information

(Continued From Previous Page)

Agency	Program or activity
11. National Science Foundation	34. Research and Education Grants and Cooperative Agreements
12. Office of Personnel Management	35. Retirement Program (Civil Service Retirement Systems and Federal Employees Retirement System)
	36. Federal Employees Health Benefits Program
	37. Federal Employees' Group Life Insurance
13. Railroad Retirement Board	38. Retirement and Survivors Benefits
	39. Railroad Unemployment Insurance Benefits
14. Small Business Administration	40. 7(a) Business Loan Program
	41. 504 Certified Development Companies
	42. Disaster Assistance
	43. Small Business Investment Companies
15. Social Security Administration	44. Old Age and Survivors' Insurance
	45. Disability Insurance
	46. Supplemental Security Income Program

Source: GAO.

Agencies and Related Programs Included in Our Review of Fiscal Year 2004 PARs

Agency	Program or activity
1. Agency for International Development	1. All programs and activities
2. Department of Agriculture	2. Marketing Assistance Loan Program (previously Commodity Loan Program)
	3. Food Stamp Program
	4. School Programs
	5. Women, Infants, and Children
	6. Child and Adult Care Food Program
	7. Wildland Fire Suppression Management
	8. Rental Assistance Program
	9. Federal Crop Insurance Corporation
	10. Farm Security and Rural Investment
3. Department of Commerce	11. All programs and activities
4. Department of Defense	12. Military Retirement Fund
	13. Military Health Benefits
5. Department of Education	14. Student Financial Assistance
	15. Title I
6. Department of Energy	16. All programs and activities
7. Environmental Protection Agency	17. Clean Water State Revolving Funds
	18. Drinking Water State Revolving Funds
8. Farm Credit System Insurance Corporation	19. All programs and activities
9. Federal Communications Commission	20. Universal Service Fund's Schools and Libraries
	21. High Cost Support Programs
10. General Services Administration	22. All programs and activities
11. Department of Health and Human Services	23. Medicaid
	24. Medicare
	25. Head Start
	26. Temporary Assistance for Needy Families
	27. Foster Care—Title IV-E
	28. State Children's Insurance Program
	29. Child Care and Development Fund
12. Department of Homeland Security	30. All programs and activities

**Appendix III
Agencies and Related Programs Included in
Our Review of Fiscal Year 2004 PARs**

(Continued From Previous Page)

Agency	Program or activity
13. Department of Housing and Urban Development	31. Low Income Public Housing
	32. Section 8 Tenant Based
	33. Section 8 Project Based
	34. Community Development Block Grant (Entitlement Grants, States/Small Cities)
	35. Federal Housing Administration's Single Family Acquired Asset Management System
14. Department of the Interior	36. All programs and activities
15. Department of Justice	37. All programs and activities
16. Department of Labor	38. Unemployment Insurance
	39. Federal Employees' Compensation Act
	40. Workforce Investment Act
17. National Aeronautics and Space Administration	41. All programs and activities
18. National Credit Union Administration	42. All programs and activities
19. National Science Foundation	43. Research and Education Grants and Cooperative Agreements
20. Nuclear Regulatory Commission	44. All programs and activities
21. Office of Personnel Management	45. Retirement Program (Civil Service Retirement System and Federal Employees Retirement System)
	46. Federal Employees Health Benefits Program
	47. Federal Employees Group Life Insurance
22. Pension Benefit Guaranty Corporation	48. All programs and activities
23. Railroad Retirement Board	49. Retirement and Survivors Benefits
	50. Railroad Unemployment Insurance Benefits
24. Small Business Administration	51. 7(a) Business Loan Program
	52. 504 Certified Development Companies
	53. Disaster Assistance
	54. Small Business Investment Companies
25. Social Security Administration	55. Old Age and Survivors' Insurance
	56. Disability Insurance
	57. Supplemental Security Income Program

Appendix III
Agencies and Related Programs Included in
Our Review of Fiscal Year 2004 PARs

(Continued From Previous Page)

Agency	Program or activity
26. Department of State	58. International Narcotic and Law Enforcement Affairs-Narcotics Program
	59. International Information Program-U.S. Speaker and Specialist Program
	60. Vendor Payments
27. Department of Transportation	61. Airport Improvement Program
	62. Highway Planning and Construction
	63. Federal Transit—Capital Investment Grants
	64. Federal Transit—Formula Grants
28. Department of the Treasury	65. Earned Income Tax Credit
29. Department of Veterans Affairs	66. Compensation
	67. Dependency and Indemnity Compensation
	68. Education Programs
	69. Pension
	70. Insurance Programs

Source: GAO.

Improper Payment Estimates Reported in Agency Fiscal Years 2003 and 2004 PARs

Agency	Program or activity	Improper payments reported		A-11	Agency reported it had assessed all programs	Programs that the agency reported were not susceptible to significant improper payments	Will estimate within the next 6 years
		2003 (in millions)	2004 (in millions)				
1. Agency for International Development	1. All programs and activities	0.0	0.0		X	X	
2. Department of Agriculture	2. Marketing Assistance Loan Program (previously Commodity Loan Program)	\$153.0	0.0	X			X
	3. Food Stamp Program	1,419.0 ^a	\$1,613.4	X			
	4. School Programs	0.0	0.0	X			X
	5. Women, Infants, and Children	0.0	0.0	X			X
	6. Child and Adult Care Food Program	0.0	0.0				X
	7. Wildland Fire Suppression Management	0.0	0.0				X
	8. Rental Assistance Program	0.0	0.0 ^b				Unknown
	9. Federal Crop Insurance Corporation	0.0	125.0				
	10. Farm Security and Rural Investment	0.0	0.0 ^b				Unknown
3. Department of Commerce	11. All programs and activities	0.0	0.0		X	X	
4. Department of Defense	All programs and activities				X		
	12. Military Retirement Fund	33.1	34.1	X			
	13. Military Health Benefits	33.2 ^a	100.1	X			

**Appendix IV
Improper Payment Estimates Reported in
Agency Fiscal Years 2003 and 2004 PARs**

(Continued From Previous Page)

Agency	Program or activity	Improper payments reported		A-11	Agency reported it had assessed all programs	Programs that the agency reported were not susceptible to significant improper payments	Will estimate within the next 6 years
		2003 (in millions)	2004 (in millions)				
5. Department of Education	All programs and activities				X		
	14. Student Financial Assistance	482.5	797.0	X			
	15. Title I	0.0	0.0 ^b	X			Unknown
6. Department of Energy	16. All programs and activities	13.7 ^a	20.3		X		
7. Environmental Protection Agency	17. Clean Water State Revolving Funds	0.0	10.3	X			
	18. Drinking Water State Revolving Funds	0.0	0.0 ^c	X			
8. Farm Credit System Insurance Corporation ^d	19. All programs and activities	0.0	0.0				Unknown
9. Federal Communications Commission	All programs and activities				X		
	20. Universal Service Fund's Schools and Libraries	0.0	0.0				X
	21. High Cost Support Programs	0.0	0.0				X
10. General Services Administration	22. All programs and activities	0.0	0.0		X	X	

**Appendix IV
Improper Payment Estimates Reported in
Agency Fiscal Years 2003 and 2004 PARs**

(Continued From Previous Page)

Agency	Program or activity	Improper payments reported			Agency reported it had assessed all programs	Programs that the agency reported were not susceptible to significant improper payments	Will estimate within the next 6 years
		2003 (in millions)	2004 (in millions)	A-11			
11. Department of Health and Human Services	All programs and activities				X		
	23. Medicaid	0.0	0.0	X			X
	24. Medicare	11,600.0	21,700.0	X			
	25. Head Start	0.0	255.0	X			
	26. Temporary Assistance for Needy Families	0.0	0.0 ^b	X			Unknown
	27. Foster Care—Title IV-E	0.0	0.0	X			X
	28. State Children's Insurance Program	0.0	0.0	X			X
	29. Child Care and Development Fund	0.0	0.0	X			X
12. Department of Homeland Security	30. All programs and activities	0.0	0.0		X	X	
13. Department of Housing and Urban Development	All programs and activities				X		
	31. Low Income Public Housing	650.0	356.0	X			
	32. Section 8 Tenant Based	1,215.0	840.0	X			
	33. Section 8 Project Based	662.0	511.0	X			
	34. Community Development Block Grant (Entitlement Grants, States/Small Cities)	0.0	0.0 ^b	X			Unknown
	35. Federal Housing Administration's Single Family Acquired Asset Management System	0.0	26.1				
14. Department of the Interior	36. All programs and activities	0.0	0.0		X	X	

**Appendix IV
Improper Payment Estimates Reported in
Agency Fiscal Years 2003 and 2004 PARs**

(Continued From Previous Page)

Agency	Program or activity	Improper payments reported		A-11	Agency reported it had assessed all programs	Programs that the agency reported were not susceptible to significant improper payments	Will estimate within the next 6 years
		2003 (in millions)	2004 (in millions)				
15. Department of Justice	37. All programs and activities	0.0	0.0		X	X	
16. Department of Labor	All programs and activities				X		
	38. Unemployment Insurance	4,225.0	3,861.0	X			
	39. Federal Employees' Compensation Act	9.1	6.4	X			
	40. Workforce Investment Act	3.1	0.0 ^b	X			Unknown
17. National Aeronautics and Space Administration	41. All programs and activities	0.0	0.0		X	X	
18. National Credit Union Administration ^d	42. All programs and activities	0.0	0.0				Unknown
19. National Science Foundation	43. Research and Education Grants and Cooperative Agreements	0.0	4.4	X			
20. Nuclear Regulatory Commission	44. All programs and activities	0.0	0.0		X	X	
21. Office of Personnel Management	All programs and activities				X		
	45. Retirement Program (Civil Service Retirement System and Federal Employees Retirement System)	177.3	197.7	X			
	46. Federal Employees Health Benefits Program	28.2	86.1	X			
	47. Federal Employees Group Life Insurance	0.4	2.1	X			

**Appendix IV
Improper Payment Estimates Reported in
Agency Fiscal Years 2003 and 2004 PARs**

(Continued From Previous Page)

Agency	Program or activity	Improper payments reported		A-11	Agency reported it had assessed all programs	Programs that the agency reported were not susceptible to significant improper payments	Will estimate within the next 6 years
		2003 (in millions)	2004 (in millions)				
22. Pension Benefit Guaranty Corporation ^d	48. All programs and activities	0.0	0.0				Unknown
23. Railroad Retirement Board	All programs and activities				X		
	49. Retirement and Survivors Benefits	168.3	172.8	X			
	50. Railroad Unemployment Insurance Benefits	2.8	3.3	X			
24. Small Business Administration	All programs and activities				X		
	51. 7(a) Business Loan Program	13.0	0.0 ^b	X			X
	52. 504 Certified Development Companies	0.0	0.0 ^e	X			
	53. Disaster Assistance	0.0	1.1	X			
	54. Small Business Investment Companies	0.0	129.0	X			
25. Social Security Administration	All programs and activities				X		
	55. Old Age and Survivors' Insurance	600.0	1,707.0	X			
	56. Disability Insurance	340.0	0.0 ^c	X			
	57. Supplemental Security Income Program	2,740.0	2,639.0	X			

**Appendix IV
Improper Payment Estimates Reported in
Agency Fiscal Years 2003 and 2004 PARs**

(Continued From Previous Page)

Agency	Program or activity	Improper payments reported			Agency reported it had assessed all programs	Programs that the agency reported were not susceptible to significant improper payments	Will estimate within the next 6 years
		2003 (in millions)	2004 (in millions)	A-11			
26. Department of State	All programs and activities				X		
	58. International Narcotic and Law Enforcement Affairs-Narcotics Program	0.0	1.7				
	59. International Information Program-U.S. Speaker and Specialist Program	0.0	1.4				
	60. Vendor Payments	0.0	0.8				
27. Department of Transportation	All programs and activities				X		
	61. Airport Improvement Program	14.0	0.0 ^f	X			
	62. Highway Planning and Construction	1.4	0.0 ^e	X			
	63. Federal Transit—Capital Investment Grants	32.0	0.0 ^e	X			
	64. Federal Transit—Formula Grants	64.0	0.0 ^e	X			
28. Department of the Treasury	All programs and activities				X		
	65. Earned Income Tax Credit	10,500.0	9,650.0	X			
29. Department of Veterans Affairs	All programs and activities				X		
	66. Compensation	256.0 ^a	238.0	X			
	67. Dependency and Indemnity Compensation	0.0 ^c	0.0 ^c	X			
	68. Education Programs	52.0 ^a	55.0				
	69. Pension	284.0	262.0	X			
	70. Insurance Programs	0.3	0.4	X			
	Totals		\$35,772.4	\$45,407.5	46	23	10

Source: GAO's analysis of cited agencies' fiscal year 2004 PARs.

Appendix IV
Improper Payment Estimates Reported in
Agency Fiscal Years 2003 and 2004 PARs

^aFiscal year 2003 estimates were updated to the revised estimates reported in the fiscal year 2004 PARs.

^bAgency did not report an annual improper payment estimate.

^cAgency combined with the above program.

^dAgency did not address improper payments or the IPIA requirements for this program in its fiscal year 2004 PAR.

^eAgency reported that its annual improper payment estimate was zero.

^fAgency reported an annual improper payment estimate, but it was an insignificant amount that rounded to zero for purposes of this table.

Comments from the Office of Management and Budget

Note: GAO comment supplementing those in the report text appears at the end of this appendix.



EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF MANAGEMENT AND BUDGET
WASHINGTON, D. C. 20503

MAR 25 2005

DEPUTY DIRECTOR
FOR MANAGEMENT

Mr. McCoy Williams
Director
Financial Management and Assurance
Government Accountability Office
441 G Street, NW
Washington, DC 20548

Dear Mr. Williams:

Thank you for the opportunity to comment on the GAO draft report entitled, "Financial Management: Challenges in Meeting Requirements of the Improper Payments Information Act" (GAO-05-417).

Eliminating improper payments in the Federal Government continues to be a central focus of this Administration. Through the government-wide efforts to improve financial management under the President's Management Agenda (PMA), as well as the new PMA Eliminating Improper Payments initiative in particular, we are striving to eliminate improper payments within all agency programs and activities. GAO remains an integral partner in this endeavor, and we appreciate the ongoing feedback and guidance that you have provided.

In Fiscal Year (FY) 2004, Federal agencies established a strong foundation for measuring improper payments, identifying and implementing the necessary corrective actions, and tracking success over time. These agency efforts are detailed in the OMB report, *Improving the Accuracy and Integrity of Federal Payments*, which was issued on January 25, 2005. The report on improper payments represents a critical step in meeting the goals of the Improper Payments Information Act (IPIA) of 2002, as it establishes a baseline from which short- and long-term program improvement strategies and priorities will be based.

Several of the key findings of the OMB report include the following:

- Federal agencies determined that 60% of all Federal outlays in FY 2004 (\$1.4 trillion out of \$2.3 trillion) were risk susceptible for a significant level of improper payments;
- Federal agencies were able to establish improper payment rates (and amounts) for programs that account for more than 80% of risk susceptible dollars;
- Seven programs alone account for approximately 95% of the improper payments reported in FY 2004; and

Appendix V
Comments from the Office of Management
and Budget

- The improper payments total reported in FY 2004 is expected to decline when reported in FY 2005, based on agency established reduction targets supported by process and control improvements to the payment process.

This OMB report may be found at http://www.whitehouse.gov/omb/financial/fia/ipia_gov-wide_report.pdf.

With regard to the GAO draft report, OMB has the following comments:

- OMB recognizes that a small number of risk assessments are not complete and that improper payment measurements are needed for certain programs. However, it is important to note that the remaining risk assessments to be completed correlate to programs with relatively small outlay amounts that, if found to be risk susceptible, are not expected to add significantly to the government-wide total. Moreover, Federal agencies reported an improper payment amount for 80% of risk susceptible dollars. Once an improper payment amount is reported for Medicaid – which is expected to begin with the FY 2005 reporting cycle – Federal agencies will then be reporting an improper payment amount for 94% of risk susceptible dollars.
- While improved detection methods may raise the government-wide improper payments estimate in future years, OMB notes that Federal agencies are actively implementing control and process improvements. It is expected that these actions will result in corresponding reductions for those improper payments already identified.
- Pursuant to the PMA Eliminating Improper Payments initiative, Federal agencies are currently required to submit completed risk assessments and error measurement plans for OMB review and approval. Such deliverables must include relevant timeframes and account for the resources necessary to complete planned actions. Agency plans for addressing IPIA reporting requirements are closely considered in identifying agency resource needs and preparing the President's Budget.
- While it is recommended that OMB consider using disincentives (such as reduced program funding) in cases where agencies fail to meet IPIA reporting requirements, the requirements of the PMA, in addition to the Inspector General review of agency IPIA activities, currently provide sufficient incentive for ensuring that agencies meet the necessary requirements.
- OMB notes that the Environmental Protection Agency and the National Science Foundation completed risk assessments in FY 2004.

See comment 1.

Appendix V
Comments from the Office of Management
and Budget

OMB will continue to work with Federal agencies, as well as the Chief Financial Officer's Council, to direct the necessary attention and resources toward efforts to eliminate improper payments.

Thank you for the opportunity to review and comment on your draft report on this important issue.

Sincerely,



Clay Johnson III

The following is GAO's comment on OMB's letter dated March 25, 2005.

GAO Comment

1. In our review of these agencies' fiscal year 2004 PARs, we determined that assessments were not completed for all programs and activities.

GAO Contacts and Staff Acknowledgments

GAO Contacts

Carla Lewis, (202) 512-6915
Alana Stanfield, (202) 512-3197

Acknowledgments

In addition to those named above, Lisa Crye, Bonnie McEwan, and Donell Ries made important contributions to this report.

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