

GAO

Report to the Chairman, Subcommittee
on Government Efficiency, Financial
Management and Intergovernmental
Relations, Committee on Government
Reform, House of Representatives

March 2002

DEBT COLLECTION IMPROVEMENT ACT OF 1996

Department of
Agriculture's Farm
Service Agency Has
Not Yet Fully
Implemented Certain
Key Provisions



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Abbreviations	
CNC	currently not collectible
DCIA	Debt Collection Improvement Act of 1996
DOJ	Department of Justice
FSA	Farm Service Agency
FMS	Financial Management Service
TOP	Treasury Offset Program
TROR	Treasury Report on Receivables Due from the Public



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

March 29, 2002

The Honorable Stephen Horn
Chairman, Subcommittee on Government Efficiency,
Financial Management and Intergovernmental Relations
Committee on Government Reform
House of Representatives

Dear Mr. Chairman:

On October 10, 2001, we testified before your subcommittee on selected federal agencies' implementation of certain key provisions of the Debt Collection Improvement Act (DCIA) of 1996.¹ That testimony addressed requirements to refer older delinquent debts to the Department of the Treasury for offset against amounts the government might owe the debtors and for additional collection action at Treasury's central debt collection facility, operated by the Financial Management Service (FMS). Our more recent testimony, on December 5, 2001, focused on progress in this area by two Department of Agriculture agencies—the Rural Housing Service and the Farm Service Agency (FSA).²

One of the major purposes of DCIA is to maximize collection of billions of dollars of nontax delinquent debt owed to the federal government. Toward this end, DCIA requires that agencies refer eligible debts delinquent more than 180 days that they have been unable to collect to Treasury for payment offset and to Treasury or a Treasury-designated debt collection center for cross-servicing. Treasury performs payment offset through its Treasury Offset Program (TOP), which includes the offset of certain benefit payments, vendor payments, and tax refunds. Cross-servicing involves such actions as locating debtors, issuing demand letters, and referring debts to private collection agencies.

¹U.S. General Accounting Office, *Debt Collection Improvement Act of 1996: Agencies Face Challenges Implementing Certain Key Provisions*, GAO-02-61T (Washington, D.C.: Oct. 10, 2001).

²U.S. General Accounting Office, *Debt Collection Improvement Act of 1996: Department of Agriculture Faces Challenges Implementing Certain Key Provisions*, GAO-02-277T (Washington, D.C.: Dec. 5, 2001).

The purpose of this report is to expand on the information provided in our December 2001 testimony regarding FSA's progress and to offer our recommendations for improving the agency's implementation of the debt-referral provisions of DCIA. As you know, our prior reports have shown that agencies have been slow to implement the referral requirements of DCIA.³ Our testimonies referred to above offered an overview of agencies' progress during fiscal years 2000 and 2001 to the extent that data were available and addressed your request for information. For this report, we looked at whether (1) FSA was promptly referring eligible farm loan program loans to Treasury's FMS for collection action, (2) any obstacles were hampering FSA from referring eligible farm loan program loans to FMS, and (3) FSA was appropriately using exclusions from referral requirements.

Results in Brief

FSA has ongoing initiatives to enhance its capacity to timely refer all eligible delinquent debt. However, the agency's failure to make DCIA a priority since its enactment in 1996 has hindered implementation of key provisions of the act and severely reduced opportunities for collection as contemplated by DCIA. As of September 30, 2000, FSA reported that it had referred about \$934 million of delinquent direct farm loan program loans to TOP for offset and that it had excluded approximately \$732 million of delinquent direct farm loan program loans from referral to TOP. However, FSA reported that it had referred only \$38 million of the approximately \$114 million of debt it reported as eligible for referral to FMS for cross-servicing.

FSA lacks effective procedures and controls to identify and promptly refer eligible delinquent debts to Treasury for collection action. We identified the following obstacles to FSA's establishment and implementation of an effective and complete debt-referral process:

- The agency's automated system lacked the capacity to distinguish deficiency judgment debts, which are eligible for referral to TOP, from types of judgment debts that are not eligible for referral. The agency therefore excluded all judgment debts from referral and missed

³U.S. General Accounting Office, *Debt Collection: Treasury Faces Challenges in Implementing Its Cross-Servicing Initiative*, GAO/AIMD-00-234 (Washington, D.C.: Aug. 4, 2000), and *Medicare: HCFA Could Do More to Identify and Collect Overpayments*, GAO/HEHS/AIMD-00-304 (Washington, D.C.: Sept. 7, 2000).

opportunities to collect delinquent deficiency judgment debts through TOP.

- Although the vast majority of farm loan program loans have codebtors, FSA's automated system could not accommodate information on codebtors. Because of this limitation, which the agency has recognized since 1986, FSA did not pursue collection from codebtors or report their names and taxpayer identification numbers to FMS for collection action and consequently missed opportunities to collect eligible delinquent debts through TOP.
- Staff in FSA field offices did not routinely update the eligibility status of delinquent debts in the agency's loan-accounting system. As a result, the system could not accurately identify loans eligible for referral, and FSA could not provide accurate debt information to Treasury, which not only distorts the Treasury Report on Receivables Due from the Public (TROR) for debt management and credit purposes, but also distorts key financial indicators such as receivables, total delinquencies, and loan loss data. In addition, failure to process closed-out debts delays the agency's reporting of those amounts to the Internal Revenue Service as income to the debtor.
- FSA temporarily suspended referral of delinquent debts to FMS for cross-servicing while developing guidelines to implement a new agency policy that limited cross-servicing referrals to debts delinquent less than 6 years.
- Even though loans became delinquent relatively evenly throughout the year, FSA referred delinquent debts to FMS for TOP only once annually, which delayed some referrals and may have reduced FMS's ability to collect on delinquent farm loan program debts.
- FSA did not have policies and procedures in place to recognize its losses on guaranteed farm loan program loans as federal debt and therefore did not apply DCIA debt collection remedies to those losses.

Regarding the appropriateness of FSA's use of exclusions from referral requirements, we reviewed the exclusions from referral to TOP because of bankruptcy, forbearance/appeals, foreclosure, and Department of Justice (DOJ) litigation made by a sample of field offices in the four states with the highest dollar amounts of debt excluded from referral to TOP. Based on our review, we estimated that approximately half of the exclusions in these four states were inconsistent with established criteria for excluding debts in bankruptcy, forbearance/appeals, foreclosure, and DOJ litigation.

We are recommending that FSA take several actions to enhance the scope and improve the timeliness of referrals of delinquent debt under DCIA.

The administrator of FSA stated in comments on this report that FSA generally agreed with our findings and recommendations but took issue with our portrayal of FSA's efforts to collect delinquent debts and our estimate of the percentage of loans that FSA inappropriately excluded from referral requirements. We continue to maintain that FSA did not make compliance with DCIA a priority and therefore missed collection opportunities. We also affirm the validity of the estimated error rate for exclusions from referral requirements included in our report. FSA stated that it has developed an action plan to implement the remaining DCIA provisions referred to in our report by December 31, 2002. Additional details on FSA's comments and our evaluation are included in the Agency Comments and Our Evaluation section of this report.

Background

FSA was established in 1994 during the reorganization of the Department of Agriculture and operates through a network of field offices located across the United States. The agency provides a variety of services, including providing financial assistance to new or disadvantaged farmers and ranchers who are unable to obtain commercial credit at reasonable rates and terms.

FSA loans available to farmers and ranchers include direct or guaranteed ownership loans and direct or guaranteed operating loans. Direct ownership loans are for buying farm real estate and making capital improvements. Direct operating loans, which are made to beginning farmers and ranchers who are unable to qualify for guaranteed operating loans, are for the purchase of items to help daily farm operations. Guaranteed farm loan program loans are for the same purposes as direct farm loan program loans, but they are made by private third-party lenders and are guaranteed by FSA for up to 95 percent of the principal loan amount.

Objectives, Scope, and Methodology

Our objectives were to determine whether (1) FSA was promptly referring eligible farm loan program loans to FMS for collection action, (2) any obstacles were hampering FSA from referring farm loan program loans to FMS, and (3) FSA was appropriately using exclusions from referral requirements.

To address these objectives, we interviewed officials from FSA to obtain an understanding of the FSA referral process and any obstacles that were hampering the referral of eligible debts. We reviewed FSA's policies and procedures on debt referrals and examined the agency's current and planned efforts to refer eligible delinquent debts. We obtained and analyzed the TROR for the fourth quarter of fiscal year 2000, which was the most recent year-end report available at the completion of our fieldwork,⁴ and other financial reports prepared by FSA, and held discussions with FSA officials to determine whether the agency was appropriately using exclusions from referral requirements. In addition, we reviewed responses to questions about FSA's debt collection practices that you submitted to the deputy secretary of agriculture in October 2001 and used information from the responses to clarify or augment our report, where appropriate.

To determine whether FSA's use of exclusions from referral requirements was appropriate, we used statistical sampling techniques to select 15 FSA field offices from the four states with the highest dollar amounts of reported debt excluded from TOP as of September 30, 2000. Using electronic and hard-copy files obtained from Agriculture, we reviewed all 263 loans from the 15 selected offices that were more than 180 days delinquent and had been reported as excluded from referral to FMS as of September 30, 2000, for bankruptcy, forbearance/appeals, foreclosure, and DOJ litigation. (Appendix I contains additional information on the sampling method and the results.) Based on the results of our review, we estimated the percentage of loans inappropriately excluded as of September 30, 2000, in the four states from which the sample offices were drawn. Because we found numerous errors in the exclusion categories we tested, we did not test other reported exclusions from referral to FMS for cross-servicing, such as internal offset.⁵

We did not review FSA's process for identifying and referring debts to Treasury for cross-servicing because the agency had suspended all such referrals in April 2000 pending development of guidelines to implement a

⁴The most recent year-end TROR should contain the most reliable information available because Treasury requires that agency chief financial officers (or their designees) certify year-end data as accurate.

⁵Loans eligible for referral to FMS for TOP may not be eligible for referral to FMS for cross-servicing. Additional exclusion categories apply to referrals for cross-servicing. Loans being offset internally and certain loans with collateral, for example, are eligible for referral to TOP but not for cross-servicing.

new referral policy. FSA issued the new guidelines in July 2001 and, according to an Agriculture official, the first referral to FMS under this new policy was made in September 2001. We did not review implementation of FSA's new guidelines, since the procedures were implemented near the completion of our fieldwork.

We conducted our review from November 2000 through October 2001 in accordance with U.S. generally accepted government auditing standards. We did not independently verify the reliability of certain information that FSA provided to us, such as debts more than 180 days delinquent and debts classified as currently not collectible (CNC)⁶ and information in FSA's loan-accounting and loan-servicing systems.

We requested written comments on a draft of this report from the secretary of agriculture or her designated representative. The written response from the administrator of FSA is reprinted in appendix II.

FSA Referred a Significant Amount of Direct Farm Loan Program Loan Debt to Treasury for TOP, but Not for Cross-Servicing

As of September 30, 2000, FSA reported having about \$8.7 billion in direct farm loan program loans. As shown in table 1, the agency reported about \$1.7 billion of direct farm loan program loans more than 180 days delinquent, including debts classified as CNC, as of September 30, 2000. Of this amount, FSA reported referring about \$934 million to TOP and excluding about \$732 million from referral to TOP. FSA reported that it had referred only \$38 million of loans to FMS for cross-servicing as of September 30, 2000. It is FSA's policy to refer delinquent loans for cross-servicing only if collateral has been liquidated and a deficiency remains. In addition, as discussed in more detail later in this report, FSA suspended cross-servicing referrals from April 2000 until September 2001 while it developed and implemented a new cross-servicing referral policy.

⁶CNC debts are debts the agency has written off for accounting purposes but has not discharged. Collection action can still be taken on such debts.

Table 1: Direct FSA Farm Loan Program Loans Delinquent as of September 30, 2000

	Loan amounts (in millions of dollars)
Loans more than 180 days delinquent, including loans classified as CNC	\$1,666
Less: exclusions allowed by DCIA ^a	732
Loans eligible for TOP ^b	934
Loans referred to FMS for TOP	934
Loans referred to FMS for cross-servicing	38

^aThe vast majority of the reported exclusions, \$694 million, were for bankruptcy, forbearance/appeals, foreclosure, and DOJ litigation.

^bIn addition to loans excluded from referral to TOP, FSA reported other exclusions from referral to FMS for cross-servicing, including loans eligible for internal offset, as of September 30, 2000.

Source: Treasury Report on Receivables Due from the Public for fourth quarter 2000 (September 30, 2000).

Several Obstacles Have Impeded FSA's Implementation of DCIA Referral Requirements

Since DCIA's enactment, several obstacles have impeded FSA's implementation of the act's referral requirements. Loan system limitations have resulted in the automatic exclusion of certain types of debts without any review for eligibility and the inability to pursue collection from codebtors through TOP. FSA's failure to ensure that field offices routinely updated the status of delinquent loans has led to inappropriate exclusions from referral and inaccurate reporting of delinquent and eligible debt amounts to Treasury. A change in referral policy led to a suspension of all delinquent loan referrals to FMS for cross-servicing. FSA's policy of referring delinquent debt to FMS only once a year resulted in delayed referrals and may have reduced collections. Finally, FSA did not take action until recently to recognize losses on guaranteed farm loan program loans as nontax federal debt. According to FSA, until certain steps, such as software implementation, are completed, FSA cannot use the collection tools provided under DCIA to pursue collection directly from debtors on guaranteed farm loan program loans.

FSA Excluded Deficiency Judgment Debts from Referral Because of System Limitations

Of the \$694 million of debt reported by FSA as excluded from referral for bankruptcy, forbearance/appeals, foreclosure, and DOJ litigation, about \$295 million consists of judgment debts, including deficiency judgments, which are court judgments requiring payment of a sum certain to the United States.⁷ According to FSA officials, deficiency judgments—unlike some other types of judgment debts—are eligible for TOP and should be referred to FMS. However, FSA's Finance Office in St. Louis automatically excluded all judgment debts for direct farm loan program loans from referral to FMS because of automated system limitations. Although the system does contain information indicating which debts are judgment debts, it cannot currently accommodate information on subcategories of judgment debts. Therefore, FSA staff cannot use the agency's automated system to identify deficiency judgments for referral. On account of our inquiries, FSA officials initiated a special project in May 2001 to manually identify all deficiency judgment debts for direct farm loan program loans so that such debts could be referred to FMS.

FSA Cannot Report Codebtor Information to FMS Because of System Limitations

Even though FSA reported having referred \$934 million of direct farm loan program loans to FMS for TOP as of September 30, 2000, the agency has lost and continues to lose opportunities to maximize collections on these loans because it does not report information on codebtors to FMS. According to FSA officials, the vast majority of direct farm loan program loans have codebtors, who are also liable for loan repayment, but FSA's automated loan system cannot record more than one taxpayer identification number for each loan. Because taxpayer identification numbers are required for referrals to FMS for TOP, FSA cannot refer codebtors on farm loan program loans to FMS. An FSA official said that the agency first recognized the need to have codebtor information in the system in 1986 to facilitate debt collection but that higher-priority systems projects have precluded FSA from completing the necessary enhancements to allow the system to accept more than one taxpayer identification number per debt. FSA was planning to incorporate this modification in the new Farm Loan Program Information System scheduled for implementation in fiscal year 2005, but during the December 5, 2001, testimony before your subcommittee, the agency committed to make the change by December 2002.

⁷A deficiency is the remaining indebtedness after foreclosure and after all collateral has been sold.

FSA Did Not Routinely Update Referral Eligibility Status of Direct Farm Loan Program Loans

FSA field offices across the country make determinations as to whether direct farm loan program loans are in bankruptcy, forbearance/appeals, or foreclosure and therefore should be excluded from referral to FMS. The status of these loans changes over time, and information on the loans must be updated as changes occur if exclusion determinations are to be continuously accurate. Our review of selected excluded loans indicated that personnel in the FSA field offices we visited did not routinely update the eligibility status of farm loan program loans in FSA's Program Loan Accounting System. Without up-to-date information on loan status, the system cannot accurately identify which loans are eligible for referral.

One of the most frequently identified inappropriate exclusions pertained to amounts that had been discharged in bankruptcy, which should not have been included in delinquent debt. Farm loan managers in some of the FSA field offices we visited said they had not closed out many direct farm loan program loans discharged in bankruptcy because making new loans has been a higher-priority use of their resources. In addition, FSA did not provide sufficient oversight to help ensure that field office personnel adequately tracked the status of discharged bankruptcies and updated the loan files and debt records in the Program Loan Accounting System.

Delays in promptly closing out discharged bankruptcy debts not only distort the TROR for debt management and credit policy purposes, but also distort key financial indicators such as receivables, total delinquencies, and loan loss data. The information is therefore misleading for budget and management decisions and oversight. Aside from erroneously inflating reported loans receivable and delinquent loan amounts, failure to process closed-out debts delays the agency's reporting of those amounts to the Internal Revenue Service as income to the debtor.⁸

FSA Temporarily Suspended Cross-Servicing Referrals

FSA suspended cross-servicing referrals in April 2000 pending development of guidelines implementing a new policy to refer only debts less than 6 years delinquent to FMS for cross-servicing. According to agency officials, FSA adopted the new policy in response to discussions they had with Agriculture's Office of the General Counsel that addressed a conflict

⁸The Federal Claims Collection Standards, which were last updated in November 2000, and Office of Management and Budget Circular A-129 both require agencies, in most cases, to report closed-out debt amounts to the Internal Revenue Service as income to the debtor.

between Farm Loan Program regulations and FMS policy. These officials stated that the Office of the General Counsel decided that FSA must adhere to Farm Loan Program regulations, which specify a 6-year delinquency limit for cross-servicing referrals, despite the fact that, according to FMS officials, FMS accepts debts for cross-servicing that are more than 6 years delinquent.

In July 2001, FSA issued revised guidelines to implement the new policy and is now reviewing loans at more than a thousand FSA field offices to determine the loans' eligibility for referral under the new policy. According to an Agriculture official, FSA made the first referral under the new policy in September 2001. Agency officials told us they eventually plan to make cross-servicing referrals quarterly but will refer delinquent loans more frequently until the backlog resulting from the referral suspension is cleared.

Some Delinquent Loans Were Not Referred Promptly Because FSA Refers Debts to TOP Only Once a Year

According to data provided by FSA officials, about \$400 million of new delinquent debt became eligible for TOP during calendar year 2000. FSA officials stated that the debts became eligible relatively evenly throughout the year, but the agency refers debts eligible for TOP only once annually, during December. Consequently, a large portion of the \$400 million of debt likely was not promptly referred when it became eligible. As we have previously testified, industry statistics have shown that the likelihood of recovering amounts owed on delinquent debt decreases dramatically as the age of the debt increases.⁹ Thus, the old adage that "time is money" is very relevant for referrals of debts to FMS for collection action. FSA officials told us that the agency agrees that quarterly referrals could enhance collection of delinquent debts and is working on automated system modifications to refer debts quarterly to TOP. FSA plans to have a quarterly referral process ready for implementation in August 2002.

⁹U.S. General Accounting Office, *Debt Collection: Treasury Faces Challenges in Implementing Its Cross-Servicing Initiative*, GAO/T-AIMD-00-213 (Washington, D.C.: June 8, 2000).

FSA Did Not Refer Losses on Guaranteed Farm Loan Program Loans to Treasury for Collection Action

Guaranteed farm loan program loans—as well as related losses—have been significant since the enactment of DCIA in 1996. The outstanding principal due on guaranteed farm loan program loans was about \$8 billion as of September 30, 2000; as of that date, FSA had paid out about \$293 million in losses on guaranteed farm loan program loans since fiscal year 1996.

Since DCIA's enactment, FSA has referred none of its losses on guaranteed farm loan program loans to FMS for collection action. According to FSA officials, the agency could not pursue recovery from guaranteed farm loan program debtors or use DCIA debt collection tools because under the guaranteed farm loan program, no contract existed between these debtors and FSA. As a result, the agency did not recognize the losses that it paid to guaranteed lenders as federal debt and did not apply DCIA debt collection remedies to them.

In June 2000, Agriculture's Office of Inspector General reported that FSA was not referring its losses on guaranteed farm loan program loans to FMS for collection and identified the need for FSA to recognize the losses as federal debts and begin referring them to FMS for collection action. However, as of September 30, 2000, FSA still had no policies and procedures to recognize losses on guaranteed farm loan program loans as federal debts and to refer such debts to FMS for TOP and cross-servicing. As a result, FSA has missed opportunities to collect millions of dollars that the agency has paid to lenders to cover guaranteed losses.

FSA officials told us that the agency has revised the loan application forms applicable to guaranteed loans made after July 20, 2001, to include a section specifying that amounts FSA pays to a lender as a result of a loss on a guaranteed loan constitute a federal debt. FSA expects that software needed to implement the revisions to the Guaranteed Loan Accounting System should be completed around mid-2002 and in place before any loss claims are paid on guaranteed loans made after July 20, 2001.

FSA Did Not Appropriately Use Exclusions from Referral Requirements

As of September 30, 2000, FSA had excluded \$732 million of delinquent loans from referral to FMS for TOP. FSA cited bankruptcy, forbearance/appeals, foreclosure, and DOJ litigation as the reasons for about \$694 million, or 95 percent, of these exclusions. About \$295 million of the exclusions were judgment debts. As we noted earlier, FSA excluded all judgment debts from referral because of automated system limitations, despite the fact that deficiency judgment debts are eligible for referral. We

also noted that we found exclusion errors caused by FSA's failure to ensure that loan status was routinely updated. As a result of inappropriate exclusions and exclusion errors, FSA failed to maximize its collection of delinquent loans and provided inaccurate TROR data to federal agencies that rely on such information for policy and oversight purposes.

Using statistical sampling, we selected 15 FSA field offices in California, Louisiana, Oklahoma, and Texas—the four states with the highest dollar amounts of debt excluded from TOP. We reviewed supporting documents for all 263 loans from these offices that were more than 180 days delinquent and had been excluded from referral to FMS as of September 30, 2000, to determine the extent to which exclusions in the four states were consistent with established criteria for excluding loans in bankruptcy, forbearance/appeals, foreclosure, and DOJ litigation.¹⁰ Based on the results of our review, we estimate that as of September 30, 2000, FSA had inappropriately placed about 575 loans, or approximately half the excluded loans in the four selected states, in exclusion categories.¹¹ As part of our sample, we reviewed supporting documents for 52 bankruptcies that had been discharged before September 30, 2000. In fact, many had been discharged several years before that date. For example, one loan with a balance due of about \$325,000 was reported as more than 180 days delinquent and had been excluded from referral because of bankruptcy. Our review of the loan file at the FSA field office showed that a bankruptcy court had discharged the debt in 1986. Therefore, the debt should not have been included in either the delinquent debt amount or exclusion amount reported to Treasury as of September 30, 2000.

Because of the large number of errors we found in the bankruptcy, forbearance/appeals, foreclosure, and DOJ litigation exclusion categories, we did not test other reported exclusions from referral to FMS for cross-servicing, such as loans being internally offset.

¹⁰Field offices in these four states serviced about \$272 million, or about 39 percent, of the total debts excluded by FSA from referral to FMS as of September 30, 2000, for bankruptcy, forbearance/appeals, foreclosure, or DOJ litigation.

¹¹We estimate that 48.5 percent \pm 15.7 percent of the population were inappropriately reported as exclusions from referral to TOP. Projecting the errors in the sample to the population of 1,187 loans, we are 95 percent confident that the errors in the population are from 389 to 761 loans.

Conclusions

Although DCIA was enacted in 1996, FSA continues to face major obstacles to complying fully with the act. FSA lacks sufficient processes and controls to adequately identify and promptly refer all direct farm loan program loans eligible for referral to FMS. Automated system limitations, which have existed for years and have delayed FSA's compliance with the act, have still not been corrected, even though they have prevented referral and potential collection of substantial amounts of eligible delinquent debt. The failure of FSA field offices to routinely update delinquent loan information has led to erroneous exclusions from referral and inaccurate reporting of debt to Treasury. FSA's policy of referring debts to TOP only once a year has allowed debts to age unnecessarily and has likely reduced their collectibility. FSA has only recently taken action to establish procedures to refer losses on guaranteed loans to FMS; therefore, opportunities to collect on losses of about \$300 million since DCIA was enacted may have already been lost. If FSA is to make significant progress in collecting on millions of dollars of delinquent farm loan program loans, the agency must give higher priority to fully complying with the debt collection provisions of DCIA.

Recommendations for Executive Action

To improve FSA's compliance with DCIA, we recommend that the secretary of agriculture direct the administrator of FSA to take the following actions:

- Develop and implement automated system enhancements to make the Program Loan Accounting System capable of identifying all judgment debts eligible for referral to FMS for collection action. In the interim, continue with the manual project to identify judgment debts eligible for referral to FMS.
- Monitor planned system enhancements to the Program Loan Accounting System to ensure that capacity to record and use codebtor information is available and implemented by December 2002.
- Develop and implement oversight procedures to ensure that FSA field offices timely and routinely update the Program Loan Accounting System to accurately reflect the status of delinquent debts. Aside from requirements for database integrity, this is critical to determining allowable collection action, including whether debts are eligible for referral to FMS for collection action.
- Develop and implement oversight procedures to ensure that all debts discharged through bankruptcy are promptly closed out and reported to the Internal Revenue Service as income to the debtor in accordance

with the Federal Claims Collection Standards and Office of Management and Budget Circular A-129.

- Monitor effective completion of the planned automated system modifications to refer eligible debt to TOP on a quarterly, rather than annual, basis by August 2002.
- Monitor planned system enhancements to the Guaranteed Loan Accounting System to ensure that the software is completed that is needed to implement the revisions to the loan application forms to establish guaranteed loan losses as federal debt.
- Once guaranteed loan losses are established as federal debt and are deemed eligible for referral to FMS, timely refer such debt to FMS for collection action in accordance with DCIA.

Agency Comments and Our Evaluation

In written comments on a draft of this report, the administrator of FSA generally agreed with our findings and recommendations. The administrator stated that FSA has developed an aggressive action plan to implement the remaining DCIA provisions mentioned in our report by December 31, 2002. FSA's letter is reprinted in appendix II.

While FSA agreed with our finding that it had inappropriately placed several loans in various exclusion categories allowed by DCIA, it disagreed with our estimated error rate of about 50 percent in the sample population of 1,187 loans. FSA stated that its own internal review of 967 loans in the four states that were included in our review resulted in an error rate of 35.7 percent.

Our sample was statistically selected and resulted in a valid projected error rate of about 50 percent for the states covered by our test work. To substantiate our work for each error identified during our testing, we asked FSA farm loan managers to sign a statement as to whether they agreed with the GAO sample results and conclusion that the exclusion was inappropriate. In all but 3 of the 113 errors we identified, the managers agreed with our conclusions and, as a result, said they planned to take action to correct the errors.

Since the FSA review was performed subsequent to our tests, we cannot comment on the validity of FSA's internal assessment of the reported results. In addition, since many of the loans in our sample had been inappropriately excluded for years, corrections made subsequent to our testing but prior to FSA's review would likely have resulted in a lower error rate at the time of FSA's work. In any case, it is important to note that the

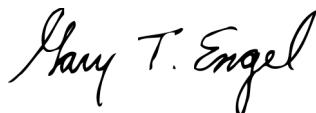
35.7 percent error rate cited by FSA from its internal assessment is still unacceptable, and we remain firm in our recommendation that FSA develop and implement oversight procedures to ensure that FSA field offices timely and routinely update the Program Loan Accounting System to accurately reflect the status of delinquent debts.

FSA also took issue with our report's reference to possible missed collection opportunities. It stated we had not given FSA sufficient credit for collections totaling millions of dollars of delinquent debt using various collection tools. Our point is that FSA's mentioned successes could have been much greater had it made DCIA a higher priority and thus implemented certain key provisions much sooner. Our position remains unchanged. The details in the body of our report demonstrate lack of adequate progress. Most important, 5 years after the passage of DCIA, FSA had not yet established an adequate framework or systems capacity to effectively carry out its responsibilities for collecting large sums of delinquent debt.

As agreed with your office, unless you announce its contents earlier, we plan no further distribution of this report until 30 days after its issuance date. At that time, we will send copies to the chairmen and ranking minority members of the Senate Committee on Governmental Affairs and the House Committee on Government Reform and to the ranking minority member of your subcommittee. We will also provide copies to the secretary of agriculture, the inspector general of the Department of Agriculture, the administrator of the Farm Service Agency, and the secretary of the treasury. We will then make copies available to others upon request.

If you have any questions about this report, please contact me at (202) 512-3406 or Kenneth R. Rupa, assistant director, at (214) 777-5714. Key contributors to this report are listed in appendix III.

Sincerely yours,

A handwritten signature in black ink that reads "Gary T. Engel". The signature is written in a cursive, flowing style.

Gary T. Engel
Director
Financial Management and Assurance

Sampling Method and Results

We first identified the four states (Texas, California, Louisiana, and Oklahoma) with the highest dollar amounts of debt excluded from TOP. From the four states, we drew a multistage cluster sample of 15 field offices (population 123) using probability proportionate to size, a sampling method in which larger clusters (in this case, offices) have a higher probability of being selected than smaller clusters. Our debt population consisted of all FSA debt more than 180 days delinquent that had been excluded from referral to Treasury as of September 30, 2000. We reviewed all excluded debt (263) at the 15 sample offices.

Table 2 identifies the four states selected, the number of offices selected in each state, the number of excluded debts at the selected offices in each state, and the number of errors found at the selected offices in each state.

Table 2: Summary of Sample Results for FSA’s Excluded Farm Loan Program Debt			
State	Number of offices selected	Number of excluded debts	Number of exclusion errors found
California	3	103	17
Texas	6	85	59
Oklahoma	3	34	16
Louisiana	3	41	21
Total	15	263	113

Based on our review, we estimate that 48.5 percent ± 15.7 percent of the population were inappropriately excluded from Treasury referral. When projecting these errors to the population of 1,187, we are 95 percent confident that the errors in the population are from 389 to 761 debts.

Table 3 shows the two-stage probability proportionate to size cluster sample results.

Table 3: Two-Stage Probability Proportionate to Size Cluster Sample Results

Sample plan

Stage 1

Total items in the population (for all field offices in the four states with the highest dollar amounts of debt excluded from TOP)	1,187
Total number of primary sample units (county/field offices with debtors in the four states)	123
Number of secondary sample units selected	15

Stage 2

Total number of items sampled in all clusters (county) ^a	263
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^aOne hundred percent of the debtors in each office selected were reviewed.

Comments from the Farm Service Agency



United States
Department of
Agriculture

Farm and Foreign
Agricultural
Services

Farm Service
Agency

Operations Review
and Analysis Staff

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State and County
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TO: Gary T. Engel, Director
Financial Management and Assurance

FROM: James R. Little *James R. Little* MAR 19 2002
Administrator

SUBJECT: U. S. General Accounting Office (GAO) Draft Report No. GAO-02-463,
"DEBT COLLECTION IMPROVEMENT ACT (DCIA) OF 1996:
Department of Agriculture's Farm Service Agency Has Not Yet Fully
Implemented Certain Key Provisions"

The Farm Service Agency (Agency) would like to thank you for the opportunity to review and comment on your draft report. In general, the Agency agrees with your findings and recommendations. However, the Agency takes issue with several points. Although your report makes reference of possible missed collection opportunities as a result of annual referral to Treasury Offset Program, it does not mention any of the positive actions that the Agency has taken to reduce delinquent debt. We believe the GAO report does not portray a balanced picture of what this Agency is doing to collect the delinquent debts it is owed. Since the implementation of the Debt Collection Improvement Act in 1996, the Agency has collected millions of dollars on delinquent debt. Below is a break down of some of the collections:

- **Internal Administrative Offset Program:** - Collections totaled \$104 million.
- **Voluntary Payments
(From FLP due process letter):** - Collections totaled \$210.5 million.
- **Treasury Offset Program:** - Collections totaled \$11.6 million.
- **Cross-Servicing Program:** - Collections totaled \$185,000.
- **Salary offset (pilot):** - Collections totaled \$15,775.

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Gary T. Engel
Page 2

The Agency also recovered \$6.5 million on guaranteed loans after the final loss payments were paid to the lenders. This is because the private lenders continue collection action after final liquidation. After the Agency implemented the above programs, the delinquent Farm Loan debt decreased from \$3.3 billion to \$1.6 billion, a reduction of \$1.7 billion, in just 5 years. As a result of this improvement in the Farm Loan Program's portfolio, the GAO, in their report dated May 16, 2001, removed the Farm Loan Program from the high-risk list.

The Agency agrees that there were some improperly flagged cases, and appreciates GAO's bringing this to our attention. However, the Agency disagrees with GAO's findings on the error rate for Exclusions from the Referral Requirements. GAO concluded that half the excluded loans were inappropriately coded. Based on the Agency's review of the cases in the four States sampled by GAO, 35.7 percent of the cases were not flagged properly. There were 967 accounts flagged in those States as cases involved in bankruptcy, forbearance/appeals, and foreclosure. The flags needed to be corrected on 345 cases. It is important to note that only 35 of those cases were eligible for referral to Department of Treasury (Treasury); the others fell into other excluded categories. Therefore, only 10 percent of the incorrectly flagged cases, and only 3.6 percent of the flagged cases in those States were eligible to be referred to Treasury. The Agency continues to monitor the proper flagging of cases to ensure that all eligible debts are timely referred to Treasury for collection.

Implementation of the DCIA is a complex and lengthy process. The approach that the Agency took to implement DCIA was to implement those phases that would provide the greatest impact on reducing delinquencies first. While we agree that the Agency has not completely implemented all the provisions of DCIA, we believe that we have taken aggressive action as evidenced by the above information. The Agency has also developed an aggressive action plan to implement the remaining provisions mentioned in your report by December 31, 2002.

GAO Contact and Staff Acknowledgments

GAO Contact

Kenneth R. Rupar, (214) 777-5714

Acknowledgments

Other key contributors to this report were Arthur W. Brouk, Sharon O. Byrd, Richard T. Cambosos, Michael D. Chambless, Michael S. LaForge, and Gladys E. Toro.

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