

# FEDERAL TRADE COMMISSION

## OFFICE OF INSPECTOR GENERAL



### SEMIANNUAL REPORT TO CONGRESS

October 1, 2007 - March 31, 2008

Report #38



Office of Inspector General

UNITED STATES OF AMERICA  
FEDERAL TRADE COMMISSION  
WASHINGTON, D.C. 20580

April 29, 2008

The Honorable William E. Kovacic  
Chairman  
Federal Trade Commission  
600 Pennsylvania Avenue, N.W.  
Washington, D.C. 20580

Dear Chairman Kovacic:

I am pleased to present the attached report that covers the Office of Inspector General's (OIG) activities for the first half of fiscal year 2008 and is submitted according to Section 5 of the Inspector General Act of 1978, as amended.

During the six-month reporting period ending March 31, 2008, the OIG issued an audit of the FTC's FY 2007 financial statements and a companion report to management containing financial-related findings and recommendations resulting from the audit. The OIG also received the final report on its *External Peer Review* of the OIG's audit program.

The OIG processed 32 consumer inquiries and complaints/allegations of possible wrongdoing during the reporting period. Three new investigations of misconduct were conducted, and three investigations were closed. We consulted with the Department of Justice on one of the closed matters and obtained a declination from prosecution. We referred the two remaining closed investigations to agency management for further action.

As in the past, management has been responsive in working with the OIG to implement all proposed recommendations. I appreciate management's support and I look forward to working with you in our ongoing efforts to promote economy and efficiency in agency programs.

Sincerely,

John M. Seeba  
Inspector General

## INTRODUCTION

The Federal Trade Commission (FTC) seeks to ensure that the nation's markets are competitive, efficient and free from undue restrictions. The FTC also seeks to improve the operation of the marketplace by ending unfair and deceptive practices with emphasis on those practices that might unreasonably restrict or inhibit the free exercise of informed choice by consumers. The FTC relies on economic analysis to support its law enforcement efforts and to contribute to the economic policy deliberations of Congress, the Executive Branch and the public.

To aid the FTC in accomplishing its consumer protection and antitrust missions, the Office of Inspector General (OIG) was provided five work years and a budget of \$905,000 for fiscal year 2008.

## AUDIT ACTIVITIES

During the six month reporting period ending March 31, 2008, the OIG issued an audit of FTC's FY 2007 financial statements and a companion report to management containing financial related findings and recommendations resulting from the audit. The OIG also received its final External Peer Review report which was conducted by the Smithsonian Institution OIG.

### Completed Audits

The OIG completed the following activities during the first half of FY 2008:

- *AR 08-001 -Audit of the Federal Trade Commission's Financial Statements for FY 2007*
- *AR 08-001A- Management Letter for FY 2007 Financial Statements*
- *N/A- External Peer Review of the Office of Inspector General*

### Summary Information on Completed Audits

*AR 08-001- Audit of the Federal Trade Commission's Financial Statements for the Fiscal Year Ending September 30, 2007*

The objective of this audit was to determine whether the agency's financial statements fairly present the financial position of the agency. The statements audited were the Balance Sheets as of September 30, 2007 and 2006 and the related Statements of Net Cost, Statements of Changes in Net Position, Statements of Budgetary Resources, and Statements of Custodial Activity for the years then ended. This was the eleventh consecutive year that the FTC received an unqualified opinion, the highest opinion given by independent auditors.

The FY 2007 audited statements provide insight into the mission and operations of the Federal Trade Commission. The FTC had total assets of \$346 million and \$322 million as of September 30, 2007 and 2006, respectively. Approximately \$248 million and \$238 million of the 2007 and 2006 assets, respectively, were funds collected or to be collected and distributed through the consumer redress program under the agency's Consumer Protection mission.

Revenue and financing sources received in fiscal years 2007 and 2006 totaled \$231 and \$214 million, respectively. Exchange revenue, classified as earned revenue on the financial statements, was received from three sources: the collection of premerger notification filing fees, Do Not Call (DNC) registry fees, and reimbursements received for services provided to other government agencies. Financing was received through direct appropriations and imputed costs absorbed by others.

Exchange revenue totaled \$167 million and \$133 million for fiscal years 2007 and 2006, respectively. The primary source of exchange revenue collected, \$145 million in fiscal year 2007 and \$111 million in fiscal year 2006, was premerger filing fees. The FTC collects a filing fee from each business entity that files a Notification and Report transaction form, as required by the Hart-Scott-Rodino (HSR) Antitrust Improvement Act. Qualifying mergers with a transaction amount over \$50 million in total assets are charged a filing fee. The fee is based on a three-tiered structure: \$45,000, \$125,000, and \$280,000, depending upon the combined total of assets of the merger transaction. The fee is divided equally between the FTC and the Antitrust Division of the Department of Justice (DOJ).

The second largest source of exchange revenue was Do Not Call fees. The FTC collects fees associated with the implementation and enforcement of the national Do Not Call Registry sufficient to cover registry costs. The Registry operates under Section 5 of the FTC Act, which enforces the Telemarketing Sales Rule (TSR). Telemarketers under the FTC's jurisdiction are required to pay a user fee and download from the DNC database a list of consumer telephone numbers listed on the Registry. Fees are based on the number of area codes downloaded. In fiscal years 2007 and 2006, respectively, the FTC collected \$22 million in each year in DNC fees.

In addition to exchange revenue, other financing sources were realized through a direct appropriation from the General Fund of the Treasury, and other non-expenditure transfers, in the amount of \$75 million in fiscal year 2007 and \$78 million in fiscal year 2006. Direct appropriation and transfers represent 32 percent and 36 percent of total funding sources received for fiscal years 2007 and 2006, respectively.

The gross cost of operations for 2007 fiscal year was \$224 million and represents an increase of 8.1 percent over the fiscal year 2006 gross cost of operations. These costs supported 1,059 staff employed in fulfilling the FTC's missions.

The statement of Custodial Activity details the monetary results of the agency's law enforcement mission. Fighting consumer fraud is one of the FTC's highest priorities, as consumers lose billions of dollars every year to perpetrators of traditional and internet fraud. In FY 2006 and FY 2005, the agency obtained monetary judgments against defendants in consumer fraud cases totaling \$250 million and \$315 million, respectively. Collections against judgments

are generally returned to the fraud victims through the redress program.

*AR 08-001A- Financial Statement Audit Management Letter*

During the financial statement audit, the OIG identified deficiencies in internal controls that were not significant deficiencies or material weaknesses (that is, they did not rise to a level of seriousness to be reported in the auditor's opinion). The OIG communicated these findings to management in a letter (*Management Letter to the FY 2007 Financial Statements* (AR 08-001A)).

The objective of the management letter is to bring to management's attention financial and/or internal control weaknesses and to make recommendations for corrective action. The current management letter also follows up on past recommendations made in the prior year's management letter. This year's management letter contains one new finding and the status (follow-up) of eight prior year findings. FTC Management has taken action to close 6 of the 8 open recommendations from our audit of the agency's 2006 financial statement. The one new finding recommended improving procedures for recording year-end journal entries.

*External Peer Review of Office of Inspector General Audit Program*

In accordance with Government Auditing Standards, we are required to have an external quality control review conducted of our audit operations and quality control system at least once every three years. The purpose of the peer review is to determine whether the audit organization has a quality control system in place to provide reasonable assurance that it is following all applicable auditing standards. During this reporting period, the Smithsonian Institution (SI) OIG conducted an external quality control review of our audit operations. We are pleased to report that the SI OIG found that our audit quality control system provides reasonable assurance of conforming to professional auditing standards in the conduct of our audits. In the report, the SI OIG made three suggestions regarding our internal quality assurance program and enhancing our internal audit policies and procedures.

The OIG will complete implementation of all three suggestions in FY 2008. The SI OIG agreed that our planned actions meet the intent of the recommendations and considers them resolved.

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**Planned Audits**

The OIG plans the following activities during the second half of FY 2008:

- *AR 09-001- Audit of the FTC's Financial Statements for Fiscal Year 2008*
- *AR-09-XXX- Annual review for the Federal Information Security Management Act (FISMA)*
- *AR-09-XXX- Audit of employee leave*

- *AR-09-XXX - Follow-up review of Redress Administration Office (RAO) database for tracking judgments and collections*

*AR 09-001- Audit of the FTC's Financial Statements for Fiscal Year 2008*

This audit is required annually under the Accountability of Tax Dollars Act of 2002. The purpose of the audit is to express an opinion on the financial statements of the Federal Trade Commission for the fiscal year ending September 30, 2008. The audit will also test the internal controls associated with the FTC's financial system and assess compliance with selected laws and regulations. The audited financial statements are required to be included in the financial section of the agency's Performance and Accountability Report to be issued on or before November 15, 2008.

The size and tight deadlines needed for this audit require that the OIG hire an independent public accountant to perform this work. The OIG will act as the Contracting Officer's Technical Representative (COTR) and provide oversight on the contract.

*AR 09-XXX -Annual FISMA Review for Fiscal Year 2008*

The Federal Information Security Management Act of 2002 (FISMA) requires an independent assessment of federal agency information security programs and practices to determine their effectiveness. The review includes evaluating the adequacy of the FTC's computer security program and practices for its major systems. This year, the review will again focus on the FTC's *Plan of Action and Milestones* to determine the extent to which the agency has implemented previously agreed upon OIG and other internally identified recommendations. This will enable the OIG to provide feedback to management on the results of its efforts to address program weaknesses.

The complexity of this audit requires us to hire an independent consultant to perform this work. The OIG will act as the COTR and perform oversight during the performance under this contract.

*AR 09-XXX - Audit of Employee Leave*

Initially the OIG will conduct a survey of employee leave: annual, sick compensatory, leave without pay, and religious compensatory. From our survey we will determine additional areas, if any, and report on the results of our review.

*AR 09-XXX - Review of Redress Administration Office (RAO) Tracking of Judgments and Collections in Bureau of Consumer Protection Cases*

In the past, the OIG found that accounting and reporting on judgments, collections and redress distributions by the Bureau of Consumer Protection Redress Office contained errors and omissions.

In response to the OIG's findings, the Bureau of Consumer Protection launched a new Redress/Enforcement database that incorporates data about court orders, defendants, receivers, redress distributions, and other financial data for redress matters. The OIG will undertake a follow-up review of the tracking and reporting of judgments and collections by the RAO to assure that the goals of this important management challenge are achieved.

#### *AR 09-XXX -Domestic and International Travel*

The objective of this audit will be to determine compliance with applicable travel regulations. We will determine if internal controls are in place to deter fraud, waste and abuse.

### **Other Potential Reviews**

During the year we will also conduct research on the following FTC operations to determine any areas for audit:

- *Review of the procurement process*
- *Review of FTC's A-123 process*
- *Inventory controls over accountable property*

### **INVESTIGATIVE ACTIVITIES**

The Inspector General is authorized by the IG Act to receive and investigate allegations of employee misconduct as well as fraud, waste and abuse occurring within FTC programs and operations. Matters of possible wrongdoing are referred to the OIG in the form of allegations or complaints from a variety of sources, including FTC employees, other government agencies and the general public. Reported incidents of possible fraud, waste and abuse can give rise to administrative, civil or criminal investigations.

In conducting criminal investigations during the past several years, the OIG has sought assistance from, and worked jointly with other law enforcement agencies, including other OIGs, the Federal Bureau of Investigation, the U.S. Postal Inspection Service, the U.S. Secret Service, the U.S. Marshals Service, the Internal Revenue Service, U.S. Capitol Police, Federal Protective Service as well as state agencies and local police departments.

### **Investigative Summary**

During this reporting period, the OIG received 32 consumer and other inquiries and reports of possible wrongdoing. Of the 32 complaints, 11 involved issues that fall under the jurisdiction of FTC program components (identity theft, credit repair, etc.). These matters were referred to the appropriate FTC component for disposition. Of the remaining complaints, the OIG opened three new investigations and 16 complaints were closed with no further OIG action. Notably, one of the closed complaints consumed considerable OIG resources in connection with the preliminary inquiry conducted by this office, prior to referral of the matter to an agency program component. The remaining two complaints were ongoing at the close of this reporting

period. The OIG is currently conducting a preliminary inquiry into these related complaints.

In addition, the OIG successfully recovered \$45,000 in unclaimed funds held by the State of Ohio on behalf of the FTC. Following a referral to the OIG, we conducted a preliminary inquiry and determined that the specified amount was being held in the state's agency responsible for holding unclaimed funds. The OIG submitted a claim on behalf of the FTC and supporting materials and recovered the funds. The money was transferred to the FTC's program office for appropriate disposition.

Following is a summary of the OIG's investigative activities for the six-month period ending March 31, 2008:

- Cases pending as of 9/30/07 6
- PLUS: New cases 3
- LESS: Cases closed (3)
- Cases Pending as of 3/31/08 6

### **Investigations Closed**

During this reporting period, the OIG closed three investigations. The first investigation, opened during a prior reporting period, involved an allegation that individuals were impersonating FTC officials. The OIG received two separate allegations from different business owners in the same geographic area who each described contacts that were made by different individuals purportedly from the FTC. The impersonators falsely represented that the business owners might be violating a statute that the FTC enforces and each impersonator sought to meet with company employees in an attempt to sell a service. As part of the investigation, the OIG contacted the complainant business owners after the initial complaint period to determine whether the impersonators had made any further contact with the complainants. Because no further contact had been made with the complainants and no additional victims could be identified, the OIG closed its investigation.

The OIG closed an investigation opened during the prior reporting period involving alleged misuse of a Government travel card by an FTC employee. The OIG investigation focused on an allegation that an FTC employee used her government issued travel card to purchase twenty-one round-trip airline tickets to a vacation destination in connection with a private business she was operating. Our investigation revealed that the employee was operating a business without agency approval, as required by the agency's Standards of Conduct and used agency resources in conducting the business. The Department of Justice declined prosecution of the matter and the OIG referred its investigative findings to management for further action.

The third closed investigation involved an alleged unauthorized disclosure of nonpublic information. The OIG received an allegation that "an unnamed government lawyer" provided nonpublic information to a reporter for an online industry publication. The reporter published an online article stated that the FTC was expected to vote on an upcoming specified date to block a specific proposed acquisition that was reported under the Hart-Scott-Rodino premerger notification statute. Counsel for one of the merging parties reported that the nonpublic information contained in the online article resulted in a sharp decline in stock values for the affected companies and shareholders lost over \$120 million. The OIG conducted multiple



interviews of FTC personnel and sought information directly from the online reporter who refused to cooperate, citing statutory protections for the press. The investigation was closed without identification of the source who disclosed the nonpublic information to the reporter.

### **Matters Referred for Prosecution**

During this reporting period the OIG did not refer any new matters to the Department of Justice (DOJ) for consideration of potential criminal action. We consulted with DOJ regarding the Government travel card misuse investigation described above. Both the OIG and DOJ agreed that a declination for prosecution was appropriate, based on the facts presented.

A matter referred to DOJ during the previous reporting period remains pending at DOJ, with no final action to date.

### **OTHER ACTIVITIES**

During this reporting period, our investigative staff assisted the Legal Services Corporation (LSC) OIG in the presentation of a matter before the Grand Jury in the Western District of Texas. Our staff member investigated the matter as an employee of LSC OIG prior to joining the FTC OIG. In similar manner, our OIG has sought the technical expertise of the United States Postal Service OIG in conducting an ongoing investigation in our office.

Our Counsel participates regularly in the monthly meeting of the Council of Counsel to the Inspectors General, as well as contributes to the legal discourse within that Council on matters that are germane to the entire IG community.

### **Management Advisories**

The OIG issued no new Management Advisories during this reporting period.

### **Significant Management Decisions**

Section 5(a)(12) of the Inspector General Act requires that if the IG disagrees with any significant management decision, such disagreement must be reported in the semiannual report. Further, Section 5(a)(11) of the Act requires that any decision by management to change its response to a significant resolved audit finding must also be disclosed in the semiannual report. For this reporting period there were no significant final management decisions made with which the OIG disagreed, and management did not revise any earlier decisions on OIG audit recommendations.

### **Access to Information**

The IG is to be provided with ready access to all agency records, information, or assistance when conducting an investigation or audit. Section 6(b)(2) of the IG Act requires the IG to report to the agency head, without delay, if the IG believes that access to required information, records or assistance has been unreasonably refused, or otherwise has not been provided. A summary of each report submitted to the agency head in compliance with Section 6(b)(2) must be provided in the semiannual report in accordance with Section 5(a)(5) of the Act. During this reporting period, the OIG did not encounter any problems in obtaining assistance or access to agency records. Consequently, no report was issued by the IG to the agency head in accordance with Section 6(b)(2) of the IG Act.

### **Audit Resolution**

As of the end of this reporting period, all OIG audit recommendations for reports issued in prior periods have been resolved. That is, management and the OIG have reached agreement on what actions need to be taken.

### **Review of Legislation**

Section 4(a)(2) of the IG Act authorizes the IG to review and comment on proposed legislation or regulations relating to the agency or, upon request, affecting the operations of the OIG. During this reporting period, the OIG reviewed no legislation.

### **Contacting the Office of Inspector General**

Employees and the public are encouraged to contact the OIG regarding any incidents of possible fraud, waste, or abuse occurring within FTC programs and operations. The OIG telephone number is **(202) 326-2800**. A confidential or anonymous message can be left 24 hours a day. Complaints or allegations of fraud, waste or abuse can also be emailed directly to [OIG@ftc.gov](mailto:OIG@ftc.gov). OIG mail should be addressed to:

Federal Trade Commission  
Office of Inspector General  
Room NJ-1110  
600 Pennsylvania Avenue, NW  
Washington, D.C. 20580

OIG reports can be accessed via the internet at: [www.ftc.gov/oig](http://www.ftc.gov/oig). A visitor to the OIG home page can download recent (1996-2007) OIG semiannual reports to Congress, the FY 1998 - 2007 financial statement audits, and other program and performance audits issued beginning in FY 1999. A list of audit reports issued prior to FY 1999 can also be ordered via an e-mail link to the OIG. In addition to this information resource about the OIG, visitors are also provided a link to other federal organizations and Office of Inspectors General.

**TABLE I  
SUMMARY OF INSPECTOR GENERAL  
REPORTING REQUIREMENTS**

<b><u>IG Act Reference</u></b>	<b><u>Reporting Requirement</u></b>	<b><u>Page(s)</u></b>
Section 4(a)(2)	Review of legislation and regulations	8
Section 5(a)(1)	Significant problems, abuses and deficiencies	3
Section 5(a)(2)	Recommendations with respect to significant problems, abuses and deficiencies	3
Section 5(a)(3)	Prior significant recommendations on which corrective actions have not been made	8
Section 5(a)(4)	Matters referred to prosecutive authorities	7
Section 5(a)(5)	Summary of instances where information was refused	8
Section 5(a)(6)	List of audit reports by subject matter, showing dollar value of questioned costs and funds put to better use	10-11
Section 5(a)(7)	Summary of each particularly significant report	1-3
Section 5(a)(8)	Statistical tables showing number of reports and dollar value of questioned costs	10
Section 5(a)(9)	Statistical tables showing number of reports and dollar value of recommendations that funds be put to better use	11
Section 5(a)(10)	Summary of each audit issued before this reporting period for which no management decision was made by the end of the reporting period	8
Section 5(a)(11)	Significant revised management decisions	7
Section 5(a)(12)	Significant management decisions with which the Inspector General disagrees	7

**TABLE II  
INSPECTOR GENERAL ISSUED REPORTS  
WITH QUESTIONED COSTS**

		<u>Dollar Value</u>	
<u>Number</u>	<u>Questioned Costs</u>	<u>Unsupported Costs</u>	
A. For which no management decision has been made by the commencement of the reporting period	<u>0</u>	<u>0</u>	<u>(0)</u>
B. Which were issued during the reporting period	<u>0</u>	0	(0)
<b>Subtotals (A + B)</b>	<b><u>0</u></b>	<b>0</b>	<b>(0)</b>
C. For which a management decision was made during the reporting period	0	0	(0)
<b>(i) dollar value of disallowed costs</b>	<b>0</b>	<b>0</b>	<b>(0)</b>
<b>(ii) dollar value of cost not disallowed</b>	<b><u>0</u></b>	<b>0</b>	<b>(0)</b>
D. For which no management decision was made by the end of the reporting period	0	0	(0)
Reports for which no management decision was made within six months of issuance	<u>0</u>	0	(0)

**TABLE III**  
**INSPECTOR GENERAL ISSUED REPORTS**  
**WITH RECOMMENDATIONS THAT FUNDS BE PUT TO BETTER USE**

	<u>Number</u>	<u>Dollar Value</u>	
		<u>Questioned Costs</u>	<u>Unsupported Costs</u>
A. For which no management decision has been made by the commencement of the reporting period	0	0	0
B. Which were issued during this reporting period	0	0	0
C. For which a management decision was made during the reporting period	0	0	0
<b>(i) dollar value of recommendations that were agreed to by management</b>	<b>0</b>	<b>0</b>	<b>0</b>
- based on proposed management action	0	0	0
- based on proposed legislative action	0	0	0
<b>(ii) dollar value of recommendations that were not agreed to by management</b>	<b>0</b>	<b>0</b>	<b>0</b>
D. For which no management decision has been made by the end of the reporting period	0	0	0
Reports for which no management decision was made within six months of issuance	0	0	0