DEPARTMENTS OF TRANSPORTATION, TREASURY, THE JUDICIARY, HOUSING AND URBAN DEVELOPMENT, AND RELATED AGENCIES APPROPRIATIONS FOR FISCAL YEAR 2007

THURSDAY, APRIL 6, 2006

U.S. SENATE,
SUBCOMMITTEE OF THE COMMITTEE ON APPROPRIATIONS,
Washington, DC.

The subcommittee met at 9:37 a.m., in room SD–138, Dirksen Senate Office Building, Hon. Christopher S. Bond (chairman) presiding.

Present: Senators Bond, Murray, and Dorgan.

DEPARTMENT OF THE TREASURY

OFFICE OF THE SECRETARY

STATEMENT OF JOHN W. SNOW, SECRETARY

OPENING STATEMENT OF SENATOR CHRISTOPHER S. BOND

Senator BOND. Good morning. The Subcommittee on the Appropriations Committee on Transportation, Treasury, Judiciary, HUD and Related Agencies will come to order.

This morning, the Senate committee will conduct its budget hearing on the fiscal year 2007 budget on the Department of the Treasury. In addition, due to the important role of the Treasury in fighting the war on terrorism, today's hearing also will focus on the Treasury's Office of Terrorism and Financial Intelligence. Senator Murray is on the way, but her staff has graciously agreed to allow me to proceed, even though she will miss part of my opening statement. I will promise to give it to her in full when she gets here later on. But because of the schedule, and we have a vote scheduled at 10:30, Mr. Secretary, if it is all right with you, we would like to finish up your part of the testimony by 10:15. I am going to wield the gavel so we can have the second panel testify before we have to go to the vote. If you don't mind, we will try to keep it short and get you out of here at 10:15 to accommodate our schedule.

As I said, we have two panels. On the first panel, Treasury Secretary John Snow, and we welcome Secretary Snow back, and we look forward to hearing his views on the accomplishments and challenges facing Treasury. After Secretary Snow, we will hear from a second panel of high-level Treasury officials who help lead the Department's efforts on combatting terrorists' financing. Specifically, we will hear from Under Secretary for Terrorism and Financial Intelligence Stuart Levey, and Assistant Secretary for Intelligence and Analysis Janice Gardner.

I have had the great pleasure of getting to know both Mr. Levey and Ms. Gardner through my work on the Senate Select Committee on Intelligence. Both have done an outstanding job of bringing together the unique capabilities and resources of the Treasury Department in intelligence gathering and analysis. The result has made the Department a key player and a true asset in the intelligence community and in the war on terrorism.

A lot has changed at the Treasury since our hearing last year, Mr. Secretary. One year ago, the Department was floundering due to a vacancy overload at its most senior-level positions. Now most of these vacancies have been filled and the Department is currently playing a much more significant and visible role in many important areas, especially having reestablished its role as a leader in combatting elicit financing with regard to money laundering and terrorist financing.

Mr. Secretary, I congratulate you and the President for responding to our concerns and filling these important positions. I am pleased by the Treasury's commitment to these important challenges, and I am especially impressed with the quality of leadership at the Office of Terrorism and Financial Intelligence, TFI. If anybody can follow all of these acronyms during the discussion, you are a little bit quicker than I am, but I have a cheat sheet to read them from.

That said, I remain concerned about the Department's ability to handle its management responsibilities, particularly in the IT area since the Office of Inspector General continues to cite management as a major challenge area, especially due to the recent failure of the BSA Direct Information Technology Project. It is a critical system, intrinsic to the success of the Financial Crimes Enforcement Network, or FinCEN's mission, and I am very frustrated that it did not receive greater oversight and support prior to and during its development. I intend to ask the GAO and the Inspector General, or the OIG, to review this issue and to provide some specific recommendations for preventing this kind of problem.

I acknowledge your current management team is relatively new, and to some degree they are still getting their feet wet. However, on your watch, Mr. Secretary, BSA Direct and other large capital-investment projects like the Treasury Building and Annex repair and restoration, HR Connect and the Treasury Communications Enterprise have experienced significant problems.

In terms of the latest failure, BSA Direct, I am fully committed to working with FinCEN's director Bob Werner in fixing these problems, and I credit the Director for taking action. However, we need to understand why your team did not act sooner, or at least ask questions on why milestones were being missed and costs were exceeding the original award amount. Senator Murray and I expect answers, Mr. Secretary, not excuses.

We also want your commitment, Mr. Secretary, to assist Director Werner in ensuring that these types of problems do not happen again. Finally, this subcommittee expects a clear action plan designed to address these IT management issues. The action plan should be submitted no later than 45 days of this hearing, but I expect, because I know this is a high priority for you, as it is for us, that it will be sooner than that.

Let us be clear, we expect better management, better oversight, and better accountability from the Department or else the chairman, and I believe I speak for my ranking member, will be reluctant to appropriate any additional funds for IT projects at the Treasury or Treasury priorities. This is that important to us.

Turning to the Treasury's budget request, the administration requests some $13.1 billion for the Department for 2007. About $11.6 billion falls under the purview of this subcommittee. For the THUD account, the budget requests a $24.7 million or 0.2 percent increase over the 2006. Most of the Treasury's budget and the budget increases are for the Internal Revenue Service, which compromises some 92 percent of the Department's budget under the THUD Subcommittee—a significant budget request in a very tight budget year. We will not be rubber-stamping any budget proposals because we do not have the money to do it. Instead, a budget anchored by a demonstrated commitment and comprehensive justification is expected. Because of the budget emphasis and the importance of the IRS, the subcommittee plans to hold a separate hearing on the IRS later this month, and we will focus on the IRS at that time.

There are a couple of IRS items, Mr. Secretary, I want to bring to your attention. First, the IRS budget request is disappointing. While the administration proposes an $18.1 million increase for IRS in 2007, the increase is, frankly, insufficient in taking a serious bite out of the $340 billion tax gap. Further, the budget request is filled with a number of budget gimmicks, which, if unattained, could result in significant cuts to IRS programs and core services in both taxpayer service and enforcement.

I also raise our serious concern with the proposed cut to the IRS's Business Systems Modernization, or BSM, program. BSM still has its challenges and risks, but led by the new Associate CIO and his team, BSM is beginning to show results, and for the administration to propose reductions to BSM now makes little sense to us. In fact, cutting BSM greatly damages the momentum built up over the past 2 years. This is a classic example of punishing good behavior.

The second point we raise is with IRS proposed regulations on disclosure and use of taxpayer information. There appears to be growing concerns about taxpayer privacy being compromised by the proposed regulation. Some concerns seem to be based on misunderstandings, whereas others are legitimate issues regarding the disclosure of confidential taxpayer information. It is a complex issue, filled with a lot of land mines. Nevertheless, I hope that Treasury and the IRS can balance out the needs and problems to ensure the maximum confidentiality of all taxpayer information to the greatest extent possible.

The last point I raise is on taxpayer service. The 2006 THUD appropriations laid out some clear directives that restrict the IRS from reducing taxpayer services until a plan for adequate alternative services is provided, and the Treasury Inspector General for

Tax Administration, TIGTA, to offer another acronym, provides a review. I understand the IRS is complying with his directive, and I am optimistic that we will not have problems in the future.

My strongest area of interest within Treasury is in its activities in fighting the war on terror, and in particular, terrorist financing. The Treasury has a long and storied history of successfully combatting organized crime from the Al Capone days, to the Nazis in World War II, and more recently, to the drug lords of Central America. These past and ongoing experiences have helped the Treasury develop a unique set of skills in understanding, deterring, and eliminating a wide variety of elicit funding. For example, the Treasury's Office of Foreign Assets Control, or OFAC, and its predecessor organizations, have had a long history of administering and enforcing economic and trade sanctions beginning with the War of 1812, through the Civil War, and the First and Second World Wars.

In modern times, OFAC has helped combat intelligence narcotics traffickers, and now as a key operational component of TFI, it is also taking on terrorists and WMD proliferators. Due to the Treasury's long experience and its unique role, Congress authorized the creation of the Treasury Office of Terrorism and Financial Intelligence, or TFI, not just to recognize the Treasury's expertise or reorganize existing intelligence, but to take the Treasury with its unique experience to a new level to play a greater role in the war on terror.

As a part of TFI, Congress created the Office of Intelligence and Analysis, or OIA, which is charged with analyzing intelligence and financial information, producing high-level products for administration and Treasury officials, for, as we all know too well from past experiences, there is a lot of information available. The problem is being to put the information together, or connecting the dots.

Since its creation, TFI and OIA are beginning to show some real results. In fact, last December, the 9/11 Commission graded various aspects of the Federal Government on fighting the war on terrorism and gave an A-minus in the area of combatting terrorist financing. That is a pretty good score compared with what everybody else got, and TFI and the Treasury Department deserve a lot of credit. TFI deserves credit and recognition for its strong role in combatting financing due to the excellent work in support of the Department's efforts to designate terrorist entities, shut down financial flows, to individuals from rogue regimes, and uncover clandestine financial networks.

In 2005, the Department designated a number of banks and foreign officials in troubling areas like Syria, North Korea, and Iran. Last December, the Department designated Banco Delta Asia under section 311 of the PATRIOT Act. It is a powerful new tool authorizing the Department to designate various foreign and financial institutions as a primary laundering concern, and to impose sanctions. Under Secretary Levey stated that, "Banco Delta Asia has been a willing pawn for the North Korean government to engage in corrupt financial activities through Macau, a region that needs significant improvement in its money laundering controls. By invoking our USA PATRIOT Act authorities, we are working to protect U.S. financial institutions, while warning the global community of the illicit financial threat posed by Banco Delta Asia."

This bank was a key hub, and having made visits to our officials and our resources in that area, I can tell it has had a major impact from the people doing the job in that area. They are telling me how important and significant this was. The DRPK under Kim Jong-il has bemoaned the action, stating to the President of China that, "The regime might well collapse under the weight of U.S. sanctions." It would be a shame, wouldn't it?

TFI has also been able to assist foreign governments in taking their own actions. It is creating a new unit to tackle terrorists financing in innovative ways. Last year we funded the Joint DOD/Treasury Finance Cells. The pilot cell in Baghdad, known as the Iraq Threat Finance Cell, ITFC, enhances collection, analysis, and dissemination of intelligence. Since I serve on both Appropriations and Intelligence, I am very encouraged to see OIA is up and running strong within the government. I believe it is key to winning the war on terror. It is a focal point for the Department for compartmented intelligence analysis and support, and the critical intelligence it is providing during weekly targeting meetings is very important. It is going to deal with the use of hawalas. Those are the traditional Arab money-transfer and changing organizations. They are now too often being used by terrorist organizations. We need to know how they work and how to regulate them. The Office of Terrorist Finance and Financial Crime, TFFC, is looking at the use of hawalas by terrorist organizations and is working with other Federal agencies and international counterparts, for example, in tackling illicit financial flows associated with Afghan narcotics.

I am pleased with the TFI's progress, but it has to adapt to the continually changing efforts to defeat our efforts. Now, the financing is fragmented into a constellation of small entities, transferring smaller amounts. The experts tell us the 9/11 attacks cost $500,000, the March 11 bombings in Spain cost about $15,000, and the recent attacks in London last July cost the terrorists as little as $2,000. Therefore, combatting terrorist financing has to remain front and center. It is going to be a critical part of our counterterrorism efforts. We have to anticipate the imagination of terrorists because they will go through any means to cause chaos.

One final point before I close. The Committee on Foreign Investment in the United States, or the CFIUS process, in regard to the recent Dubai Ports World controversy: my strong opinion is that DPW was treated very badly since a perfectly legitimate company owned by one of our closest allies in the Middle East was slapped in the face. I can tell you from visiting with foreign officials that that has not only affected our allies in the UAE, but our allies around the world. There are definitely some significant questions about the CFIUS process, they are already being addressed, and I think that some of the intelligence concerns can be addressed by OIA within Treasury. Congress is going to be working on updating that, and I am pleased that the Senate Banking Committee is taking on this issue and has recently passed legislation to reform CFIUS. Notwithstanding any legislation, I believe that Treasury needs to develop a better system of communicating to the Hill on the deals it is considering. Mr. Secretary, we saw a classic example of that wonderful process on DPW of ready, fire, and aim. Perhaps some additional information to Congress would allow Congress to aim before firing, and I hope we can do that in the future.

Now with apologies, I turn to my colleague, Senator Murray.

STATEMENT OF SENATOR PATTY MURRAY

Senator MURRAY. Thank you very much, Mr. Chairman. Today we are joined by Treasury Secretary John Snow, and I want to welcome him here this morning.

Most Americans view the Treasury Secretary as the leading Cabinet official for our Nation's fiscal policy. Indeed, the Treasury Secretary plays a critical role on overseeing our financial markets and coordinating policy with our international partners. The Secretary is responsible for taking the lead on tax policy and overseeing the collection of tax revenues.

As members of this subcommittee, we have a special obligation to look at another important role of the Treasury Secretary, namely, as the administrator of the funds appropriated by this subcommittee. We have the job of evaluating whether the tax dollars we have appropriated have been well spent, and whether taxpayers have gotten value for their money. In that regard, the record of this Treasury Department is deeply disturbing. Time after time, this subcommittee has been required to sound the alarm about misguided, multimillion-dollar initiatives that have resulted in lengthy delays and massive cost overruns. At this hearing last year, I talked about the unfortunate history of the TBARR program—the Treasury Department's building modernization project. That program is now nearing completion, but not before it spent almost $100 million more than initially budgeted, and taking 3 years longer than we were promised when we made our initial appropriation.

Last year we also talked about Treasury's so-called HR Connect program, an initiative to modernize the human resources information system at the Treasury Department. That initiative has also been plagued with costly delays and cost overruns.

As we observe the Treasury Department's performance over the last year, we are faced with still more examples of mismanagement and waste. The Treasury Department has been attempting to launch a Treasury Communications Enterprise, or TCE, initiative. As far as we can tell, absolutely nothing has gone right with this program since its inception. The GAO found fault with the competition process, so the Treasury Department decided to terminate its contract and procure services through the General Services Administration. The Treasury Department then reversed its decision and decided to launch a separate competition process for the TCE initiative, despite the fact that the GSA system will have the services Treasury needs at a lower cost. The Treasury Inspector General found that the entire project was fraught with poor planning and execution. The Treasury IG also observed that there was little evidence of adequate senior management oversight of the project.

Even more disturbing have been the missteps that directly affect services to taxpayers, and our ability to combat terrorist financing. Last year, Secretary Snow's IRS Commissioner proposed to eliminate more than 60 Taxpayer Assistance Centers across the country.

I opposed that initiative. He intended to close those centers in order to free up money for enhanced tax law enforcement. Now, while I support efforts to collect the taxes that are owed, I do not believe that enhanced enforcement should come at the cost of services to taxpayers. Despite my opposition and that of many legislators, the IRS Commissioner persisted. In the end, we included bill language prohibiting him from closing these Taxpayer Assistance Centers until the Inspector General could review the methodology and data that he used to determine which centers to close.

We now have the results from the Inspector General. He found that the IRS was using faulty data or data that was not the most current data. He also found that the IRS did not have the necessary management information systems to interpret this data. Had this been allowed to go through, the Commissioner would have, quite possibly, been closing the wrong Taxpayer Assistance Centers, leaving taxpayers who need help in the lurch.

Finally, when it comes to the area of terrorist financing, we have the deeply troubling efforts of Treasury launching its new computer communications system for administering the Bank Secrecy Act, known as BSA Direct. As recently as February 17, 2006, the Treasury Department maintained that this new IT system would be a critical and essential new tool to provide greater access and analytical capability. Indeed, our subcommittee attached such importance to this initiative that we provided $5 million that the Treasury Department did not request to expedite the deployment of this critical new system. Now, just this past March, a new agency head was put in charge. He found numerous problems surrounding this initiative and issued a stop-work order. It remains to be seen whether BSA Direct should be continued and will add any real value to our efforts to combat terrorist financing. It might make sense for Treasury to use the IRS's new BSA data management system that is already up and running at a fraction of the BSA Direct.

The bottom line is this: just because the Treasury Department prints the Nation's money and collects the Nation's tax dollars, it does not give the Department the right to waste those dollars. This Department has an obligation to learn from its mistakes, and as far as I can tell, these mistakes with major procurements are happening over, and over, and over again. The Treasury Secretary is responsible for many critical matters of international finance. He is also responsible for every dollar we appropriate to his Department. I hope and expect that he will have clear answers for us today about why we continue to encounter these repeated management failures and waste of taxpayer dollars in the Department.

Finally, Mr. Chairman, I want to thank you for scheduling a separate panel of witnesses so that we can deal with the matter of terrorist financing. There is certainly no greater calling on the part of this agency than its effort to cut off the financial lifeline from those terrorists who wish to do us harm. It is one of the reasons that I am so disturbed by the Department's failure in the BSA Direct program. Thank you, Mr. Chairman.

Senator BOND. Thank you very much, Senator Murray. Now Mr. Secretary, we have outlined a few areas of concern. We would welcome your comments.

SUMMARY STATEMENT OF JOHN W. SNOW

Secretary SNOW. I thank you, Mr. Chairman, and Senator Murray. It is always a privilege and a pleasure to appear before you, to hear your comments, exchange views and get your insights and have an opportunity to talk to you about these important issues. You have raised a lot of good issues, both you and Senator Murray. We put in place, I think, a set of processes that are going to get at these issues more effectively.

First of all, we have identified a pretty good team. I appreciate some of your good comments, frankly, on that team. It is encouraging to hear that from the chairman of this committee. So getting the right team in place, you know, you are right, a year ago we had vacancies across the board, and today, virtually all of those vacancies are filled, and filled with really top-flight people.

On the IT issues, we recognize we have got to do better. We know that, again, getting the right people in place and the right management structures. I have had a lot of experience, Senator Murray and Mr. Chairman, over the years, probably at least as much as you have, in overseeing and managing IT systems. The Government's IT systems are more complex than any you ever see in the private sector, and when it comes to something like BSA, go to your corner software store and you can't pick it up off the shelf. You got to develop these systems on your own, and they are inherently very, very complex. I am not making excuses. We are going to do better. We have realigned the CIO under the Assistant Secretary for Management. We are going to apply the lessons that we have learned from past mistakes.

One of those lessons is you put in place real project management and you understand going in what you are trying to accomplish. You know your requirements. You lay out your requirements. You have milestones. You follow the success in achieving those milestones, all those things that are good management, and providing better coordination across all the functions. I am confident that we are going to do better on that score.

Let me say, you know this Department has changed enormously over the few years that I have been here. When I came in, it was going through that massive restructuring to create Homeland Security. We did not have the TFI functions fully developed, and I want to thank you for your support in helping us put in place this strong TFI function.

What is Treasury all about? It has an important role, as Senator Murray said, in trying to keep the American economy on the right path, and in dealing with counterparts in the global economy. I think we do that pretty well. The American economy today you know is performing very well. We are growing at close to 4 percent for the last nearly 3 years since the Jobs and Growth Bill went into effect, 5 million new jobs, and I think we are going to continue on that good path. The Treasury Department's counsel with the President and putting in place the Tax Program of 2003 I think has a lot to do with that. So I hope Congress will move to extend those reductions on dividends and cap gains, and do it soon.

We also have an important role in securing our country from terrorist threats. You have alluded to that and I will not go into it except to say it is a top priority with me, and I think we have the right people in place to drive those efforts.

The Treasury stands at the center of the national and the global fiscal policy issues, the Current Account issues, global growth issues, all of those. We participate in the G–7 and the G–20 and APEC, and we lead this country's efforts at the World Bank and the IMF, all critically important functions. Senator Murray, I take seriously your comments about the deficit. We are a voice for restraining spending and keeping the economy strong to get revenues coming in, and revenues, of course, are now at an all time high for the United States Government, and on a path as a percent of GDP to achieve their historic level.

You have raised other issues that I will look forward to getting into in the Q and A. On the 7216 question, that regulation, Mr. Chairman, you are right, that has been grossly misperceived in the press. It is actually a tightening of the rules on privacy, not a weakening of those rules. We can get into that later.

PREPARED STATEMENT

Again, I very much value the close working relationship with this committee and your excellent staff. We take seriously their comments, we take seriously the GAO's comments, and working together, I think we will continue to make good progress at the Department. I thank you.

[The statement follows:]

PREPARED STATEMENT OF JOHN W. SNOW

Chairman Bond, Senator Murray, and members of the subcommittee, I appreciate the opportunity to appear before you today to discuss the President's fiscal year 2007 budget for the Department of the Treasury.

The President's budget for Treasury in fiscal year 2007 reflects the Department's dedication to promoting economic opportunity, strengthening national security and exercising fiscal discipline. The budget supports activities that help ensure all Americans will have the opportunity to live in a Nation that is more prosperous and more secure.

The Treasury appropriations request for fiscal year 2007 is $11.6 billion, slightly above the fiscal year 2006 enacted budget. This request is consistent with the President's overall goal of cutting our deficit in half by 2009. The Treasury Department is committed to fiscal austerity and to the most efficient and effective use of taxpayer dollars while at the same time boosting revenues through continued economic growth.

Mr. Chairman, we have provided the committee with a detailed breakdown and justification for the President's fiscal year 2007 budget request for Treasury. I would like to take the opportunity today to highlight portions of our request and then I would be happy to take any questions you may have.

PROMOTING A PROSPEROUS AND STABLE U.S. ECONOMY

The Treasury Department plays a predominant role in the development and implementation of the President's goals for domestic and international economic growth, and the communication of his agenda. To reach our greatest potential, the economy must increase its rate of growth and create new, high quality jobs for all Americans.

The legal and regulatory framework must also support this growth by providing an environment where businesses and individuals can grow and prosper without the burdens and costs of unnecessary taxes and regulations. In addition, the role of the tax system in supporting economic growth is critical. The economic indicators since the President signed the Jobs and Growth Act in May 2003 provide validity to this notion. Since that time, we have seen 11 straight months of positive business investment; nearly 5 million jobs have been created; the unemployment rate stands at a remarkable 4.8 percent; and now we are also seeing a rise in American's income and wealth. What's also impressive is the fact that tax revenues are surging; Federal revenues for fiscal year 2005 totaled $2.15 trillion—the highest level ever.

The budget addresses the need to consider the economy when considering tax policy with the proposed creation of a new Dynamic Analysis Division within Treasury's Office of Tax Policy. Understanding the full range of behavioral responses to tax changes, including how tax changes affect the size of the economy and, eventually, tax revenues, is critical to designing meaningful, effective tax policy, and tax reform. This small expenditure will have a substantial pay-off for the American taxpayer.

Treasury's Office of International Affairs also plays a key role in supporting growth by advancing our Nation's interests in an increasingly complex world economy. The office improves access to foreign markets for U.S. financial service firms, promotes domestic demand-led economic growth abroad, and fosters economic restructuring and stability. These activities contribute to rising standards of living in both the United States and other countries.

As globalization has progressed, Treasury's on-the-ground presence in international finance and economic centers has steadily receded. The $9.4 million requested to increase Treasury's overseas presence will enable the Department to carry out its international mission in the global economy more effectively. Treasury attachés will work in tandem with the Office of International Affairs and the Office of Terrorism and Financial Intelligence to build relationships with foreign officials and work with local U.S. industry and agency representatives to advance U.S. interests. They will also provide much-needed intelligence and expertise to U.S. officials in Washington formulating policy on international economics, trade, finance, and terrorist finance.

The budget also seeks $7.8 million for the Community Development Financial Institutions (CDFI) Fund to administer the New Markets Tax Credit and manage the existing loan portfolio. The budget proposes to consolidate CDFI's remaining programs into the Strengthening America's Communities Initiatives (SACI) within the Departments of Commerce and Housing and Urban Development.

FIGHTING THE GLOBAL WAR ON TERROR AND SAFEGUARDING OUR FINANCIAL SYSTEMS

While promoting financial and economic growth at home and abroad, Treasury performs a critical and far-reaching role in homeland security. The Department battles national security threats by coordinating financial intelligence, targeting and sanctioning supporters of terrorism and proliferators of weapons of mass destruction (WMD), improving the safeguards of our financial systems, and promoting international coordination to attack the financial underpinnings of terrorist and other criminal networks. To support these efforts, the President requests $388.7 million for fiscal year 2007.

The Office of Terrorism and Financial Intelligence (TFI) supports Treasury's national security efforts by safeguarding the U.S. financial systems against illicit use. TFI provides financial intelligence analysis, develops and implements anti-money laundering measures, administers the Bank Secrecy Act, and enforces economic and trade sanctions. In addition, TFI provides policy guidance for the Internal Revenue Service's (IRS) Criminal Investigation staff. IRS special agents are experts at gathering and analyzing complex financial information from numerous sources and applying the evidence to tax, money laundering, and Bank Secrecy Act violations. These agents support the national effort to combat terrorism and participate in the Joint Terrorism Task Forces and similar interagency efforts focused on disrupting and dismantling terrorist financing.

Financial intelligence exposes the infrastructure of terrorist and criminal organizations. It provides a roadmap for investigators to find those who help facilitate criminal activity. These investigations lead to the recovery and forfeiture of illegally obtained assets and create broad deterrence against criminal activity. Treasury plays a crucial role in linking law enforcement and intelligence communities with financial institutions and regulators. To support these efforts, Treasury requests an increase of $16.9 million for the Financial Crimes Enforcement Network to improve coordination with State and local regulators, strengthen regulatory training and outreach, and enhance Bank Secrecy Act collection, retrieval, analysis, and sharing.

Treasury exercises a full range of intelligence, regulatory, policy, and enforcement tools in tracking and disrupting terrorists' support networks, proliferators of weapons of mass destruction, rogue regimes and international narco-traffickers, both as a vital source of intelligence and as a means of degrading the terrorists' ability to function. Treasury's actions include:

—Freezing the assets of terrorists, drug kingpins, and support networks;

—Cutting off corrupt foreign jurisdictions and financial institutions from the U.S. financial system;
—Developing and enforcing regulations to reduce terrorist financing and money laundering;
—Tracing and repatriating assets looted by corrupt foreign officials; and
—Promoting a meaningful exchange of information with the private financial sector to help detect and address threats to the financial system.

The fiscal year 2007 President's budget requests $7.8 million to enable Treasury to continue to enhance its abilities to identify, disrupt, and dismantle the financial infrastructure of networks of terrorists, proliferators of WMD, narco-traffickers, criminals, and other threats. Treasury will also improve its analytical capabilities, to provide actionable intelligence and to target, designate and implement sanctions against the financiers of WMD proliferation.

This budget request funds Treasury's national and homeland security mission at a level that provides increasingly effective support to the war on terror. Treasury will enhance this support with an increased international presence funded in this request. Treasury attachés located at critical embassies throughout the world will enable close liaison with the international financial institutions and foreign governments to promote the national and economic security interests of the United States.

COLLECTING TAXES AND MANAGING THE GOVERNMENT'S FINANCES

Treasury's strategic goal to manage the U.S. Government's finances effectively is the largest part of the President's fiscal year 2007 request for the Department. The budget request of $10.9 billion—the majority of which is for the Internal Revenue Service—underscores Treasury's commitment to provide quality service to taxpayers and enforce America's tax laws in a balanced manner.

The Internal Revenue Service (IRS) provides taxpayers with top-quality services by helping them understand and meet their tax responsibilities through a commitment to integrity and fairness. The IRS supports the administration's goal of reducing the Federal deficit by increasing tax receipts collected through taxpayer services, enforcement compliance, and identifying improvements that will reduce the cost of revenue collection. Treasury's enforcement efforts yielded a record $47.3 billion in enforcement revenue in fiscal year 2005. The fiscal year 2007 budget will provide funding to continue the IRS's dedication to service and maintain efforts to improve the enforcement of tax laws.

Increasing compliance with the tax code is at the heart of the Treasury's enforcement programs. The IRS will continue to expand enforcement efforts by targeting its casework and enforcement activities to deliver results more effectively. The IRS will continue to analyze tax information and data from compliance research studies to better understand and counter the methods and means of those taxpayers who fail to report or pay what they owe. The IRS is focusing on discouraging and deterring non-compliance such as corrosive activity by corporations and high-income individual taxpayers. In order to ensure funding for tax enforcement, the administration is again proposing a program integrity cap adjustment. I am pleased that the Senate Budget Committee included this adjustment in their Budget Resolution.

To reinforce this effort, the budget proposes new tax legislation that will improve the ability of the IRS to identify underreporting and collect unpaid taxes, while minimizing the burden on those who comply with the tax code. These legislative proposals strategically target areas where research reveals the existence of substantial compliance issues. The improvements will burden the taxpayers as little as possible, and the changes support the administration's broader focus on identifying legislative and administrative changes to increase compliance with the tax code.

The IRS continues to make progress with the Business Systems Modernization (BSM) program. BSM aims to modernize the tax system by providing real business benefits to taxpayers and IRS employees through new technology. In fiscal year 2006 and continuing in fiscal year 2007, BSM is revising its modernization strategy to emphasize the incremental release of projects to deliver business value sooner and at lower risk.

The Treasury Inspector General for Tax Administration (TIGTA) continues to partner with the IRS in increasing compliance with the tax code by ensuring that the IRS can pursue the effective administration of Federal tax laws without hindrance from internal and external attempts to corrupt the tax system. TIGTA serves to highlight opportunities for cost savings in IRS operations, protect taxpayer rights and privacy, and generally promote the economy, efficiency and effectiveness of tax administration.

The Alcohol and Tobacco Tax and Trade Bureau (TTB) also works to ensure that taxes due become taxes collected. TTB is the Nation's leader on regulating alcohol, tobacco, firearms, and ammunition excise taxes. The bureau is responsible for the collection of approximately $15 billion annually. TTB ensures that alcohol beverages are labeled, advertised, and marketed in compliance with the law. TTB's efforts assure the public that alcohol and tobacco products reaching the marketplace are unadulterated, thereby providing marketing and sales value to the industry. The budget proposes to establish user fees to cover a portion of the costs of these regulatory functions.

Treasury also works to disburse, manage, and account for the Nation's monies as it distributes payments, finances public services, and balances the government's books.

The Financial Management Service (FMS) is the government's financial manager and as such administers the government's payments and collections systems. In fiscal year 2005, FMS issued over 952 million non-defense payments valued at $1.5 trillion, of which 76 percent were made electronically. The President's budget includes proposed legislation that would enhance non-tax debt collection opportunities, including allowing FMS to collect an estimated $3.8 billion in past due unemployment compensation debts over the next 10 years.

The Bureau of the Public Debt (BPD) facilitates Treasury's debt financing operations by issuing and servicing Treasury securities. BPD will continue its goals of increased efficiency and achieve its mission to borrow the money needed to operate the Federal Government and to account for the resulting debt.

STRENGHENING FINANCIAL INSTITUTIONS

Treasury, through the Office of the Comptroller of the Currency (OCC) and the Office of Thrift Supervision (OTS), maintains the integrity of the financial system of the United States by chartering, regulating, and supervising national banks and savings associations. Ongoing supervision and enforcement ensure that each national bank or saving association is operating in a safe and sound manner, which enhances the reliability of the U.S. financial system. In fiscal year 2005, OCC and OTS oversaw assets held by these insured depository institutions totaling $7.3 trillion.

The United States Mint and the Bureau of Printing and Engraving (BEP) share the responsibility of meeting global demand for the world's most accepted coins and currency. Neither the U.S. Mint nor the BEP receive any appropriated funds from Congress. In fiscal year 2005, the Mint returned $775 million to the Treasury's General Fund. The U.S. Mint continues its work to streamline operations and remain highly effective, while providing coins for circulation and numismatic purposes. BEP continues its work of developing new methods of designing our currency to guard against counterfeiting. The bureau plans to release the redesigned $100 dollar bill later this year.

MANAGING TREASURY EFFECTIVELY

The President has requested $219.8 million to ensure proper stewardship of the Department. Treasury is committed to using the resources provided by taxpayers in the most efficient manner possible.

The Departmental Offices and Department-wide Systems and Capital Investments Program (DSCIP) account funds technology investments to modernize business processes throughout Treasury, helping the Department improve efficiency. In fiscal year 2007, the President's budget requests $34 million for ongoing modernization and critical information technology projects and to invest in other new technologies that will improve efficiency and service. Included in this request is $21.2 million to complete the redesign and modernization of Treasury's Foreign Intelligence Network (TFIN), a Top Secret/Sensitive Compartmented Information system critical to the support of Treasury's national security mission.

Included in this budget request is $17.4 million to fund the Department's Office of Inspector General (OIG) audit and investigative programs. The budget also includes $136.5 million for the Treasury Inspector General for Tax Administration (TIGTA) and its efforts to oversee the Nation's tax administration.

The Treasury Franchise Fund, recognized as a Financial Management Center of Excellence, is a self-supporting business-like entity that provides common administrative services to other Federal agencies on a fully reimbursable basis. The Fund will continue to support Treasury's stewardship of the Department by promoting excellence in its management and increase competition for government and financial services.

TREASURY AND THE PRESIDENT'S MANAGEMENT AGENDA

Treasury is meeting the President's challenge to improve the management of the Department's people and resources. On the most recent President's Management Agenda (PMA) scorecard, the Department achieved a Green progress score in five out of six initiative areas, indicating that plans are in place and implementation is progressing to accomplish the PMA objectives.

The Office of Management and Budget's Program Assessment Rating Tool (PART) is intended to improve program performance. Treasury made a strong commitment to improve its program performance, and PART scores subsequently have improved. Currently, 70 percent of Treasury's PART evaluations have scored "adequate" or better and Treasury has set a target of 76 percent scoring "adequate" or better in fiscal year 2006.

Treasury will continue to work closely with the Office of Management and Budget and other stakeholders to make improvements in implementing the initiatives set forth in the President's Management Agenda.

CONCLUSION

Mr. Chairman, I look forward to working with you, members of the committee, and your staff to maximize Treasury's resources in the best interest of the American people and our country as we move into fiscal year 2007. We have hard work ahead of us and I am hopeful that together we can work to make the Treasury a model for management and service to the American people, and continue to generate economic growth, increase the number of jobs for our citizens, and keep our financial systems strong and secure.

Thank you again for the opportunity to present the President's budget for the Treasury Department today. I would be pleased to answer your questions.

INFORMATION SYSTEMS

Senator BOND. Mr. Secretary, thank you very much. Let's get right to the questions.

We have talked about BSA Direct, raising serious questions about the Treasury's ability to procure, manage and oversee IT. Can you give me your personal commitment that high-risk projects like the Treasury Financial Intelligence Network, critical for the TFA analysts to perform their jobs, will not experience the same problems as BSA Direct? How can you assure us that there will be the necessary support and resources for TFIN and other IT projects based on the lessons learned?

Secretary SNOW. There are lessons learned here. I think the major lesson learned is get those requirements well specified in advance, and have somebody with knowledge about IT matters watching it closely. I have asked the Assistant Secretary for Management to make that a priority, and I have asked her, working with the CIO, to make sure they keep me regularly posted on these IT projects. There are a number of them, TFIN and others, that will get my personal attention. They will be managed by people who know a lot more about the management of IT than I do, but as somebody who has been in this world for a long time, I think I can see problems, spot problems, and help keep us on the right track. I pledge to you I am going to do everything I can.

INCREASED OVERSEAS PRESENCE

Senator BOND. Thank you, sir. As you know, I have supported the major expansion of the Overseas Attaché Program. Can you describe your short-and long-term goals for it, how it will help the American people, and describe the coordination efforts between the Office of International Affairs and the Office of Terrorism and Financial Intelligence in this program?

Secretary SNOW. Absolutely, Mr. Chairman, and I appreciate the chance to do so.

Treasury today has attaché posts at a limited number of places, Baghdad, I think Kabul, Afghanistan, and Tokyo. At one point we had many more, and we see a real need to expand the number to go to critical places on the globe. The attachés would have a dual role. It would be advancing the objectives of good economic policies in those countries, but also the TFI objectives of coordinating on terrorist finance issues, coordinating on issues of putting place better regulatory regimes in many countries. The United States is way ahead of most of the rest of the world in having the PATRIOT Act and 311 and 326 and the various rules we have that allow us to freeze, block and get at terrorist monies. Augmenting the effort to fight terrorists' finances will be a big part of these attachés' roles as well. And they are going to critical places in the Middle East as well as to financial centers around the world.

Senator BOND. I am delighted to see that you are looking at Southeast Asia where I think there are lots of problems, and I would also suggest you look at Pakistan where there could be some real challenges.

IRS 7216 REGULATIONS

Moving very quickly to 7216, do you think the proposed regulations adequately address consumer-protection issues? And how are they stronger than current regulatory protections?

Secretary SNOW. Thank you very much, Mr. Chairman. They are much stronger than current law. Current law does not prescribe the form of a warning, and 7216 does prescribe the form of a warning, a much stronger warning. It also puts time limits on the period through which the third party can use that data of 1 year. It had been open-ended. I think the testimony of the fact that this protects taxpayers better is that Nina Olson, the National Taxpayer Advocate, has supported the issuance of these regulations. So I think there was a miscommunication, and the real facts are this tightens privacy with respect to use of taxpayer information.

OFFICE OF DYNAMIC ANALYSIS

Senator BOND. Mr. Secretary, the budget proposes $500,000 to create a new Dynamic Analysis Office within the Treasury. What types of analysis would this office conduct that is not being conducted now? I have a personal feeling about the need for this, but what is the long-term plan for the office in terms of funding and staffing?

Secretary SNOW. When we come to you, Mr. Chairman, with tax proposals, you have the right to say to us: "What will that do to GDP? What will that do to growth? What will that do to macroeconomic variables?" The Dynamic Analysis Office will develop models to enable us to answer those questions so that when we come forward with major tax analyses, major tax proposals, we will have analyses behind those proposals to answer questions about the broad macroeconomic effects.

Senator BOND. I think we have seen it demonstrated that strict, static budget analysis leads to some very bad guesses about future performance.

TAX GAP

Finally, I would like to ask you about the tax gap, a $345 billion tax gap. That is the amount of money estimated that is owed and that is not collected. That means those of us who are sweating as hard as we can to pay the taxes we owe by April 15 are carrying the burden for some slugs who are out there not paying the $345 billion. How can we take a bite out of that with the reduction in the money for the IRS?

Secretary SNOW. Mr. Chairman, the budget proposal includes five new specific legislative proposals that I think would help. The Commissioner I think you know is keen on strengthening enforcement and has done a good job of doing so, with more audits, more enforcement activity, more focus on the enforcement side. We always have to get that balance right, though, between enforcement and taxpayer service. We are just going to continue to do the best we can, and in Commissioner Everson we have somebody who is absolutely dedicated to this purpose.

Senator BOND. Thank you very much, Mr. Secretary. Senator Murray.

TAX PREPARATION ERROR RATES

Senator MURRAY. Mr. Secretary, let me start by addressing some of the problems that exist at our major tax preparation companies. Just 2 days ago the GAO reported that there may be some serious problems with the accuracy of the tax returns prepared by many of the private tax preparation companies. The GAO found that these companies often prepared returns that were incorrect, with tax consequences that were sometimes significant. Some of these mistaken returns could have exposed taxpayers to penalties for things like negligence and willful or reckless disregard of tax rules. What are you doing now to rectify that situation?

Secretary SNOW. This is a recurring issue, Senator, as you know. I think every year about this time we see newspaper accounts of this. I do not think it is an intent to defraud anybody. I think the problem that you are talking about is the result of the bewildering complexity of the Code itself. You can get 15 tax people of impeccable credentials looking at one tax return and coming up with 15 different results. I think that that is fundamental in the nature of the Code, and we have to address the complexity of the Code.

Senator MURRAY. That could be, but still we have people who go to a tax preparer and believe that they know what they are doing, and I think it is of serious consequence if we do not have an aggressive agency that is doing something to help regulate these tax preparation companies.

Secretary SNOW. Senator, to put this in a little perspective, the IRS itself gives differing interpretations, so that the issue here, and I think it is really a serious one, is not an effort to defraud anybody. It is a reflection of the inherent complexity.

Senator MURRAY. People in your agency give different interpretations? Is that not a problem in itself?

Secretary SNOW. It is a problem of how complex the Code is. My wife is a volunteer to the IRS to help elderly people and poor people prepare their tax returns. She came back to me after a session recently and said, "John, you cannot imagine how bewildering and confusing the Tax Code is. How do you expect people to comply with the Tax Code when I, a reasonably intelligent person who has had a course in taxes, can hardly figure it out myself?" I think that is a common refrain.

Senator MURRAY. I have to disagree with you a little bit. It may be a complex Tax Code, but when we have private tax preparation companies and an IRS that has a function to make sure that they have the correct information, we cannot just say that that is an excuse for giving taxpayers penalties for being negligent. I think we have to do our job better, I think your agency has to do its job better, and I think we have to manage these tax preparation companies and have aggressive oversight with them. Do you disagree with that?

I will tell you if a math teacher gives a complex question to a bunch of high school students and they come back and say: "Gosh, it is complex", I do not think you would accept it, and I know I would not.

Secretary SNOW. Senator, every year your local newspaper and local newspapers all over the country go out with one tax return, take it to acknowledged tax experts, and the tax experts differ themselves on what the amount owed is. Albert Einstein said, and he was a pretty smart fellow, the one thing that he ever encountered that was entirely incomprehensible to human intelligence was the Internal Revenue Code. If it is tough for Einstein, you can see why it is tough for the rest of us.

IRS 7216 REGULATIONS

Senator MURRAY. Mr. Secretary, I do not think anybody would disagree that the complexity of the Tax Code is a challenge for all of us, but it is a challenge we have to aggressively be on top of. Following-up on the chairman's question on the proposed regulations on revising section 7216, I heard you say that some of that improves protection of taxpayer information. That may well be true, but it also very clearly loosens some of the tax preparer companies' obligations and may very easily by just someone accidentally swiping their pen in the wrong place, they lose their private information. I would like to know from you if you are going to follow-up on that, if you are going to take a look at those regulations, take into concern that this has opened up the real question of whether or not taxpayers' private information may accidentally be used without their knowledge?

Secretary SNOW. Senator, absolutely. We have a duty to protect the information of taxpayers, and I pledge to you that we are going to take those responsibilities with the utmost seriousness. This particular regulation was actually an effort on the part of the IRS and the Commissioner to tighten up this regulation.

Senator MURRAY. And I am going to be asking him about it next week, I assure you.

Secretary SNOW. The rulemaking is still open. We invite comments, we invite your comments and others to comment on it.

Senator MURRAY. This has raised serious alarms.

Secretary SNOW. Right.

Senator MURRAY. Since you oversee that division, I wanted you to be aware of it. I want to know that you are aware of it and I want to know that you are following up on it.

Secretary SNOW. And I align myself with your comments on it. It is very important that we protect taxpayer information.

TAXPAYER ASSISTANCE CENTERS

Senator MURRAY. I just have 1 minute left here, and I want to ask about the reference that I made in my opening comments to closing some Taxpayer Assistance Centers, and we found out that that was based on faulty data. I would like to find out from you whether we should just accept the IRS's arguments on other recommendations, or should we now be questioning all of those? Since that was based on faulty data, that gives us a lot of concern.

Secretary SNOW. I think you have important oversight responsibilities, and we benefit from your challenging us and raising questions.

Senator MURRAY. Has your Department now abandoned any of your plans to close any of the Taxpayer Assistance Centers?

Secretary SNOW. Yes, there will be no reduction in service contemplated in this budget.

BSA DIRECT

Senator MURRAY. Let me just comment in my last 10 seconds here on the BSA Direct program, and I heard your comments to the chairman. With all due respect, I really do appreciate your commitment to do better on those procurements, but it is what we heard last year. So I would like to follow up with you, I know I am out of time, but hear from you what we are going to do to make sure we are not sitting here year after year hearing the same story on these complex procedures.

Secretary SNOW. Senator, the new Director, Mr. Werner, came in and looked at the program and saw that it was missing milestones and put a pause on it.

Senator MURRAY. Right.

Secretary SNOW. As he follows through on his analysis, I will keep the committee fully posted on what we think should be done.

Senator MURRAY. Thank you very much, Mr. Secretary.

Senator BOND. Mr. Secretary, I said we were going to suspend your testimony at 10:15, but Senator Dorgan has come in. Senator, I apologize. We are trying to get the second panel on, but if you would like to take 2 minutes for your statement-question-presentation, and then we will come back after the vote to question the second panel.

Senator DORGAN. Mr. Chairman, that is fair. Senator Burns and I have been running another Appropriations subcommittee just across the hall.

Senator BOND. I hope you are doing good things for us. We have some ideas.

Senator DORGAN. We have the Missouri provision in our bill, so we think it is going to go pretty well.

I will be very brief and just make two points to the Secretary. I understand the point has already been made about the sale of taxpayer information by private preparers to third parties. I have sent you a letter about that. Despite the explanations of it, I think it is a horrible idea. I think we ought to have a pretty aggressive public discussion about whether tax preparers under any condition ought to sell taxpayer information that they glean in preparing tax returns to third parties. I understand that that has been raised.

TAX SHELTERS

I want to show you a picture. This is, Mr. Secretary, a picture of a building on Church Street in the Cayman Islands. It is called the Ugland House. You may be familiar with it. The Ugland House on Church Street is the official residence, according to David Evans who did a story at Bloomberg News, for 12,748 corporations. I know they are not in there, but it's what they claim to be their official residence. Why would they claim that? There is one purpose, to avoid paying U.S. taxes. This is a real crisis. I do not think we have the ability, resources or capability at this point to nearly begin to address this.

Here we are in 2006 with 12,748 companies claiming this one building as their residence. Trying to force these companies to pay taxes is like connecting the ends of two plates of spaghetti. The way the IRS goes about it is pretty incompetent in my judgment. Second, the law by-and-large favors and gives opportunity to companies to do this.

I hope very much that we will at the Treasury Department decide to blow a hole in this kind of practice because it is costing us a great deal of lost revenue. It is also unfair to ask working families to pay their taxes and then have these companies park their address simply for residence purposes at a building in the Caymans to avoid paying taxes.

Secretary SNOW. Senator, I look forward to a chance to have a good discussion with you on that. The IRS has tried to tighten up its enforcement activities in this area, but I think, as you said, this also reflects the state of the law, and I would hope is part of the broad-based tax reform efforts we would look at these issues very, very closely. I agree with you.

Senator DORGAN. It is both the law and enforcement. Maybe you and I should just fly down to Church Street at the Caymans and park in the lobby there and see who comes and goes from that building. Thanks, Mr. Secretary.

Secretary SNOW. Thank you, Senator.

Senator BOND. Senator Dorgan, I think there is some good fishing down there, so maybe we could spend a couple hours down there and then see about the other resources.

Mr. Secretary, thank you very much for being here. Now we will call Mr. Levey and Ms. Gardner, and do as much as we can before the vote starts.

Senator BOND. Thank you very much, and we will begin with Mr. Levey. Sir.

OFFICE OF TERRORISM AND FINANCIAL INTELLIGENCE

STATEMENT OF STUART LEVEY, UNDER SECRETARY

ACCOMPANIED BY:

JANICE GARDNER, ASSISTANT SECRETARY, OFFICE OF INTELLIGENCE AND ANALYSIS

ROBERT W. WERNER, DIRECTOR, FINANCIAL CRIMES ENFORCEMENT NETWORK

Mr. LEVEY. Thank you, Mr. Chairman, Senator Murray, and Senator Dorgan. Thank you for the opportunity to speak before you today about the President's 2007 year request for the Office of Terrorism and Financial Intelligence at the Treasury Department. And thank you especially, Mr. Chairman, for all the kind remarks you made in your opening statement. I hope we can live up to them.

The funding that is in the President's budget will provide us with the resources needed to support the Department's essential and growing terrorist financing, money-laundering, WMD proliferation, narco-trafficking, and economic sanctions programs, as well as the intelligence capabilities that are critical to the success of those programs.

Treasury has continued, with the strong support of this committee, to build much needed resources for the Office of Terrorism and Financial Intelligence, and we have achieved some important successes. I attribute those successes to the unbelievably dedicated work force that I have been blessed with, and an extraordinary management team that I work with, including Assistant Secretary Gardner, as well as Assistant Secretary O'Brien who is here today, the Director of FinCEN, Bob Werner who is here, and the Acting Director of OFAC, Barbara Hammerle who is also here today, they make my job a very easy one.

Over the past year alone, TFI has designated and financially isolated front companies, nongovernmental organizations, and facilitators supporting terrorist organizations such as al Qaeda, Jemaah Islamiyah, and Egyptian Islamic Jihad. We have implemented targeted financial sanctions under a new Executive Order aimed at North Korean, Iranian, and Syrian facilitators of WMD proliferation, and we have struck a deep blow to North Korea's illicit conduct and ability to abuse the international financial system to facilitate that conduct. Those accomplishments are only the tip of the iceberg, but they demonstrate without question not only that our resources are being put to good use, but that the Treasury Department is fulfilling its vitally important role.

On terrorist financing, as you note, Mr. Chairman, the 9/11 Commission's Discourse Project awarded its highest grade, an A−, to the U.S. Government's efforts to combat terrorist financing. This praise truly belongs to the dedicated individuals not only in the Office of Terrorism and Financial Intelligence, but our partner agencies around the government who aggressively track and combat this threat.

As you know, Mr. Chairman, from your service on the Intelligence Committee, it is very hard to measure success in an area like terrorist financing. The meaningful indicators of our success are typically complex and not readily quantifiable, such as anecdotal reporting about terrorist cells having difficulty raising money or paying operatives. We focus on those intelligence reports, even though they are often fragmentary, and try to identify the difficulties that the terrorists are having raising or moving money and adjust to it. In recent months we have seen at least one instance of what we look for most, a terrorist organization indicating that it could not pursue sophisticated attacks because it lacks adequate funding.

We have also seen success, in my view, in preventing terrorist financing by deterring would-be donors. In my opinion, if we are going to succeed in our fight against terrorist financing, we need potential donors to know that responsible governments will treat them as the terrorists that they are. Those who reach for their wallets to fund terrorism must be pursued and punished in the same way as those who reach for a bomb or a gun.

This requires cooperation from other governments, and in that regard, I was heartened by a recent statement by the Saudi Arabian Foreign Minister, Prince Saud al-Faisal, who publicly called for those who support terrorism to be held to account. If Saudi Arabia and others in the region see this commitment through, it will send a powerful message of deterrence to would-be terrorist financiers.

In other areas of this fight, to be honest, we are not where we need to be. State sponsors of terrorism like Iran and Syria present a very difficult problem, providing not only money and safe haven to terrorists, but also financial infrastructure through which terrorists can move, store, and launder their funds. Secretary Rice had it right when she referred to Iran in particular as the "central bank of terror."

While this is a daunting challenge we face, the impact of our actions over the past year with respect to Syria show that we can make progress in isolating state sponsors of terrorism. Among other things, we finalized the designation of the Commercial Bank of Syria under section 311 of the PATRIOT Act in part because of the risk of terrorist financing posed by a bank owned and controlled by an active and defiant state sponsor of terror like Syria.

Success in all of our efforts depends on cooperation from responsible financial institutions both in the United States and abroad. The recent announcement by UBS that it would cut off all business with Iran and Syria provides a notable example of a financial institution making clear that the business of terrorist states is just not worth the risk. Other financial institutions are similarly reviewing their business arrangements and taking special precautions to ensure that they do not permit terrorist financiers or WMD proliferators, which are increasingly able to identify and combat using our new authorities, access to the global financial system. On WMD proliferation, Mr. Chairman, the exposure of a WMD proliferation network headed by A.Q. Khan provided the world with a window into one of the most frightening scenarios that we face.

The U.S. Government is doing everything in its power to deter, disrupt and prevent the spread of weapons of mass destruction and ensure especially that they do not fall into the hands of terrorists, and the reason for this is that proliferators, just like terrorists, require a substantial network to support them. And by cutting off the supply lines of that network, we can isolate the individual proliferators, paint a clear picture of how and with whom they operate, and erode the infrastructure that supports them.

In June 2005, the President issued a new Executive order which allows us to do just that, essentially to apply the same tools that we do against terrorist financiers to WMD proliferators. A designation under this Executive order cuts the target off from access to the U.S. financial and commercial system, and puts the international community on notice about the threat it poses. Thus far, we have designed a total of 20 entities for proliferation related to Iran, Syria, and North Korea. Our efforts to prepare additional designation packages are ongoing, and will continue through the end of this year and next. One of our major initiatives in the President's budget is a request for 10 additional analysts to work on this program.

As you noted also, Mr. Chairman, in September 2005, we exercised a new authority under the PATRIOT Act, section 311 of the PATRIOT Act, to list Banco Delta Asia as a primary money-laundering concern. The regulatory action against this bank that was facilitating a range of North Korean illicit activity has dealt a blow to North Korea's ability to engage in illicit conduct and obtain financial services to facilitate that conduct. As a result of that 311 action against this bank, and our office's subsequent and continuing outreach efforts, a number of responsible jurisdictions and institutions have taken steps to ensure that North Korean entities engaged in illicit conduct are not receiving financial services. In fact, press reports indicate that some two-dozen financial institutions across the globe have cut back or terminated their financial dealings with North Korea, thereby constricting the flow of dirty cash to Kim Jong-il's regime.

PREPARED STATEMENT

If there is time in the questions and answers, I would like to explain to the committee how that worked in more detail.

Mr. Chairman, I look forward to working closely with you and your staff, and thank you again for the opportunity to testify today.

[The statement follows:]

PREPARED STATEMENT OF STUART LEVEY

Chairman Bond, Ranking Member Murray, and other distinguished members of the subcommittee, thank you for the opportunity to speak before you today about the President's fiscal year 2007 request for the Office of Terrorism and Financial Intelligence (TFI) at the Department of the Treasury. This funding will provide us with the resources needed to support the Department's essential and growing terrorist financing, money laundering, WMD proliferation, narco-trafficking, and economic sanctions programs, as well as the intelligence capabilities that are critical to the success of these programs.

As you know, TFI is a relatively new office. It was created in 2004 to oversee the Treasury Department's enforcement and intelligence functions aimed at severing the lines of financial support to international terrorists, WMD proliferators, narcotics traffickers, and other criminals. The office consolidates the policy, enforcement, regulatory, and analytical functions of the Treasury and adds to them critical intelligence components by bringing under a single umbrella the Office of Intelligence and Analysis (OIA), the Office of Terrorist Financing and Financial Crimes (TFFC), the Financial Crimes Enforcement Network (FinCEN), the Office of Foreign Assets Control (OFAC), and the Executive Office for Asset Forfeiture. TFI also works closely with the IRS-Criminal Investigative Division in its anti-money laundering, terrorist financing, and financial crimes cases.

Together, we leverage a wide range of tools to pressure obstructionist regimes. Using various authorities, we also have the ability to freeze the assets of terrorists, proliferators, and other wrongdoers. We use regulatory authorities to help banks and other institutions implement systems to detect and halt corrupt money flows. And, diplomatically, we work with other governments and international institutions, urging them to act with us against threats and to take critical steps to stem the flow of illicit finances.

KEY ACHIEVEMENTS

As Treasury has continued—with your support—to build much-needed resources for this new office, we have achieved some important successes. Over the past year alone, TFI has designated and financially isolated front companies, non-governmental organizations, and facilitators supporting terrorist organizations, such as al Qaeda, Jemaah Islamiyah, and Egyptian Islamic Jihad; implemented targeted financial sanctions under a new Executive order against North Korean, Iranian, and Syrian facilitators of WMD proliferation; and struck a deep blow to North Korea's illicit conduct and ability to abuse the international financial system to facilitate that conduct. These efforts have required a contribution from all of TFI's components, as well as the hard work of other Departments and agencies.

These accomplishments are only the tip of the iceberg, but they demonstrate without question not only that our resources are being put to good use, but that the Treasury Department is fulfilling its vitally important role to play in deterring and defending against our country's greatest national security challenges. Our financial authorities complement other national security instruments, providing policymakers with a range of options for isolating and pressuring hostile regimes, terrorists, and proliferators of weapons of mass destruction. When we are confronted with a foreign threat that is not susceptible to diplomatic pressure, financial authorities are among the rare tools short of military force that we can use to exert leverage.

I would like to highlight some of TFI's key achievements in greater detail.

Terrorist Finance

The 9/11 Commission's Public Discourse Project awarded its highest grade, an A−, to the U.S. Government's efforts to combat terrorist financing. This praise truly belongs to the dozens of intelligence analysts, sanctions officers, regional specialists, and regulatory experts in the Treasury's Office of Terrorism and Financial Intelligence (TFI) who focus on terrorist financing, along with their talented colleagues in other agencies—law enforcement agents who investigate terrorism cases, Justice Department prosecutors who bring terrorist financiers to justice, foreign service officers in embassies around the world who seek cooperation from other governments and many others from the intelligence community. You will not find a more talented and dedicated group of people, with a complete focus on the mission.

Teamwork across agencies has translated into effectiveness. We have continued to improve our ability to track key targets and to take the most appropriate action against the terrorist target. Sometimes that means that the Treasury will take public action, sometimes it involves persuading another country to take action, and sometimes we decide to continue to quietly collect intelligence to better map out the terrorist network. From the formation of TFI, we have been committed to that philosophy, resisting the application of metrics to our activities that would distort our incentives, for example, by emphasizing the number of terrorism designations.

The meaningful indicators of our success are typically complex and not readily quantifiable, such as anecdotal reporting about terrorist cells having difficulty raising money or paying salaries or benefits. In recent months, we have seen at least one instance of what we look for most—a terrorist organization indicating that it cannot pursue sophisticated attacks because it lacks adequate funding.

Typically, though, the information we receive is not as clear. As an example, one interesting trend that we have witnessed is a decrease in the average amount of transactions that we learn about. Obviously, we are only privy to a subset of the total transactions, but this observation carries across various financial conduits and terrorist organizations and we have no reason to believe that it is unrepresentative. Interpreting this indicator is more difficult. It could reflect an overall decrease in the amount of money moving to and from terrorists. Just as easily, it could indicate that terrorists are breaking their transactions out into smaller sums, fearing interception. Alternatively, the trend could be an outgrowth of a movement by terrorist organizations away from banks towards less formal mechanisms, like cash couriers. These couriers may offer concealment, but some get caught and some get greedy, and so it is very risky to entrust them with large sums of money. Any of these alternatives would indicate that our efforts are having an impact and this trend may bear out our assessment that terrorists who fear using the banking system do not have a ready and reliable alternative for moving large sums of money. We will continue to monitor developments, but I hope this provides a sense of how complex a task it is to assess the overall impact of our efforts to combat terrorist financing.

In specific areas, we can point to more concrete indicators of success. We have made dramatic progress in combating terrorist abuse of charities. Prior to 9/11 and even afterwards, terrorists used charities as safe and easy ways to raise and move large sums of money. Al Qaeda and Hamas, in particular, relied on charities to funnel money from wealthier areas to conflict zones with great success. Through a combination of law enforcement and regulatory actions against several corrupt charities, both at home and abroad, we have taken out key organizations and deterred or disrupted others. In tandem, active engagement with the legitimate charitable sector has succeeded in raising transparency and accountability across the board.

We have thus far designated more than 40 charities worldwide as supporters of terrorism, including several U.S. charities such as the Holy Land Foundation, the Global Relief Foundation, the Benevolence International Foundation, the Al Haramain Islamic Foundation, and the Islamic African/American Relief Agency (IARA). The impact of these actions is serious, and sometimes decisive. IARA once provided hundreds of thousands of dollars to Osama bin Laden. More recently, IARA country offices have experienced increased pressure and its leaders have expressed concern about the organization's future.

Our most recent action targeted KindHearts, a purported charity in Ohio that was supporting Hamas. In that instance, we took coordinated action with DOJ prosecutors and the FBI, which executed a search warrant at the moment that we froze the group's assets. Although we generally do not disclose specific blocked asset information, KindHearts has stated that over $1 million of its assets were blocked. Overall, engagement with the charitable sector combined with enforcement actions against bad organizations have radically altered the dynamic, leaving dirty charities isolated and imperiled.

Another important measure of our progress is an increase in the number of countries approaching the U.N. Security Council to seek the designation of terrorist supporters. This global designation program, overseen by the U.N.'s 1267 Committee, is a powerful tool for global action against supporters of al Qaeda. It envisages 191 U.N. Member States acting as one to isolate al Qaeda's supporters, both physically and financially. Increasingly, countries have begun to look to this committee, and administrative measures in general, as an effective complement to law enforcement action. In 2005, 18 Member States submitted names for the Committee's consideration, many for the first time, and we will continue to support this process and encourage others to do so as well.

In other arenas of this fight, however, we are not where we need to be. State sponsors of terrorism, like Iran and Syria, present a vexing problem, providing not only money and safe haven to terrorists, but also a financial infrastructure through which terrorists can move, store, and launder their funds. While this is a daunting challenge, I believe that the Treasury Department's tools, combined with cooperation from responsible financial institutions, can make a difference. In the past year, for example, we have designated top Syrian officials, including the then-interior minister Ghazi Kanaan and the head of Syrian Military Intelligence, Assaf Shawkat, in part for their support to terrorist organizations. Also, on March 9, we issued a final rule under Section 311 of the PATRIOT Act confirming that the Commercial Bank of Syria (CBS) is a "primary money laundering concern" and forbidding U.S. financial institutions from holding correspondent accounts for CBS. Among our reasons for that action was the risk of terrorist financing posed by a significant bank owned and controlled by an active and defiant state sponsor of terror like Syria.

We have ample reason to believe that responsible financial institutions around the world pay close attention to such actions and other similar indicators and adjust their business activities accordingly, even if they are not required to do so. A recent example of interest was the announcement by the international bank UBS that it intended to cut off all business with Iran and Syria. Other financial institutions are similarly reviewing their business arrangements and taking special precautions to ensure that they do not permit terrorist financiers or WMD proliferators—which we are increasingly able to identify and combat using a new authority—access to the global financial system.

WMD Proliferation

The exposure of the WMD proliferation network headed by A.Q. Khan—father of Pakistan's nuclear bomb and, more recently, nuclear technology dealer to Libya, Iran, and North Korea—provided the world with a window into one of the most frightening scenarios that we face. The U.S. Government is doing everything in its power deter, disrupt, and prevent the spread of weapons of mass destruction and ensure that they do not fall into the hands of terrorists. Treasury plays a key role in this effort.

Proliferators, like terrorists, require a substantial support network. By cutting off the support lines of that network, we can isolate individual proliferators, paint a clearer picture of how, and with whom, they operate, and erode the infrastructure that supports them. In June 2005, the President issued Executive Order 13382, which allows us to do just that.

This Executive Order authorizes the Treasury and State Departments to target key nodes of WMD proliferation networks, including their suppliers and financiers. A designation under this Executive Order cuts the target off from access to the U.S. financial and commercial systems and puts the international community on notice about the threat it poses. Based on evidentiary packages prepared primarily by OFAC, the President initially designated a total of eight entities in North Korea, Iran, and Syria. Continuing investigations by OFAC resulted in the subsequent designation of eight additional North Korean, and two additional Iranian, entities. And, just last week, Treasury designated two more proliferators, Kohas AG and its president, Jakob Steiger. Kohas AG, a Swiss company, acts as a technology broker in Europe for the North Korean military and has procured goods with weapons-related applications. Nearly half of the company's shares are owned by a subsidiary of Korea Ryonbong General Corporation, a previously-designated North Korean entity that has been a focus of U.S. and allied efforts to stop the spread of controlled materials and weapons-related goods, particularly ballistic missiles.

OFAC's efforts to prepare additional designation packages—with the support of the Office of Intelligence and Analysis—are ongoing and will continue throughout fiscal years 2006 and 2007. In fact, one major OFAC initiative for 2007, which I will discuss shortly, relates directly to the WMD program.

This new authority provides a powerful tool to combat the financial underpinnings of WMD proliferation and also underscores the President's commitment to work with our international partners to combat this threat. We hope our program can provide a model for other governments to draw upon as they develop their own laws to stem the flow of financial and other support for proliferation activities, as called for in U.N. Security Council Resolution 1540 and by the G–8 at Gleneagles.

The Treasury and State Departments have been engaged in aggressive international outreach in order to promote this important concept. Assistant Secretary Pat O'Brien, Deputy Assistant Secretary Daniel Glaser, and I have met with our counterparts in a number of countries in Europe, Asia, and the Middle East to urge them to ensure that U.S.-designated proliferators are not able to do business in their countries and to develop their own 13382-like authorities.

Although our WMD program is in its early stages, and while I am limited in what I can say in this public forum, I am pleased to be able to assure you that, through cooperation with both governments and the private sector, we are already seeing an impact on our targets. Indeed, this program has significantly enhanced the U.S. Government's overall counterproliferation efforts.

Section 311 Designation of Banco Delta Asia SARL

In September 2005, not long after the President signed this new WMD Executive Order, the Treasury Department used a separate authority—Section 311 of the USA PATRIOT Act (PATRIOT Act)—to list Banco Delta Asia SARL (BDA) as a "primary money laundering concern." This regulatory action against a bank facilitating a range of North Korean illicit activities has dealt a blow to Pyongyang's ability to engage in illicit conduct and obtain financial services to facilitate that conduct. Along with our offensive targeting of several entities under E.O. 13382 for supporting North Korea's WMD and missile proliferation-related activities, it has frustrated North Korea's efforts to conduct proliferation-related transactions.

Section 311 authorizes the Secretary of the Treasury—in consultation with the Departments of Justice and State and appropriate Federal financial regulators—to find that reasonable grounds exist for concluding that a foreign jurisdiction, institution, class of transactions, or type of account is of "primary money laundering concern" and to require U.S. financial institutions to take certain "special measures" against those jurisdictions, institutions, accounts, or transactions. Potential measures include requiring U.S. financial institutions to terminate correspondent relationships with the designated entity. Such a defensive measure effectively cuts that entity off from the U.S. financial system. It has a profound effect, not only in insulating the U.S. financial system from abuse, but also in notifying financial institutions and jurisdictions globally of an illicit finance risk.

The success of the BDA action offers an instructive case study of the impact of this authority. BDA provided financial services for over 20 years to North Korean government agencies and front companies, some of which were engaged in illicit activities, including currency counterfeiting, narcotics trafficking, production and distribution of counterfeit cigarettes and pharmaceuticals, and the laundering of the associated proceeds. We also know that North Korean entities engaged in WMD proliferation, including Tanchon Bank—the primary financial facilitator of North Korea's ballistic missile program—held accounts at BDA. BDA tailored its services to the needs and demands of North Korean entities with little oversight or control. In fact, bank officials intentionally negotiated a lower standard of due diligence with regard to the financial activities of these clients.

—BDA helped North Korean agents conduct surreptitious, multimillion dollar cash deposits and withdrawals without question for the basis of those transactions.

—BDA knowingly accepted counterfeit currency from North Korean companies. In that regard, it is worth noting that the U.S. Secret Service has been investigating North Korean counterfeiting since 1989, and, over the past 16 years, has seized more than $48 million in high quality U.S. currency, or "supernotes."

—A well-known North Korean front company that has been a client of BDA for over a decade has conducted numerous illegal activities, including distributing counterfeit currency and smuggling counterfeit tobacco products. In addition, the front company has also long been suspected of being involved in international drug trafficking.

Treasury's ongoing investigation of BDA has not only confirmed our original concerns about BDA's complicity in facilitating this type of conduct, but has shed additional light on the wide spectrum of North Korea's corrupt and dangerous activities, as well as its vast illicit financial network.

As a result of the 311 action against BDA and TFI's subsequent and continuing international outreach efforts, a number of responsible jurisdictions and institutions have taken proactive steps to ensure that North Korean entities engaged in illicit conduct are not receiving financial services. Press reports indicate that some two dozen financial institutions across the globe have cut back or terminated their financial dealings with North Korea, constricting the flow of dirty cash into Kim Jong Il's regime.

Treasury's efforts with respect to Banco Delta Asia, specifically, and combating North Korea's illicit activities, more generally, are ongoing. The Internal Revenue Service—Criminal Investigation Division is leading an investigation to exploit underlying North Korean account information at Banco Delta Asia provided by the Macau authorities. This investigation will allow the United States to gain an even greater understanding of the illicit activities highlighted in our Section 311 designation, and to uncover additional leads regarding DPRK entities of concern. Additionally, TFI officials continue international outreach efforts to raise awareness of North Korea's illicit conduct, explain the actions that Treasury has taken, and encourage governments and institutions to not to do business with individuals and entities engaged in illicit conduct. By all accounts, that outreach is working.

OVERVIEW OF THE FISCAL YEAR 2007 TFI REQUEST

The 2007 request of $135.2 million for TFI, including $89.8 million for the Financial Crimes Enforcement Network, provides critical funding to expand TFI's ability to combat terrorist financing and other key national security challenges. It will allow us to continue and build upon these past achievements and current efforts. I know the members of the subcommittee are aware of this request in detail, so I will just touch on a few important highlights of new initiatives.

Office of Intelligence and Analysis

TFI's Office of Intelligence and Analysis (OIA) was created to focus expert analytical resources on the financial and other support networks of terrorists, WMD proliferators, and other key national security threats. Over the past year, OIA has assumed an increasingly important role in the Treasury's efforts to combat key national security threats in Iran, Syria, and North Korea. OIA's top strategic priority is to provide policymakers with relevant intelligence and expert analysis to support policy formulation and carry out the Treasury's role in the war on terror. Other OIA strategic priorities include providing intelligence support to senior Treasury officials on the full range of economic and political issues and communicating with other members of the Intelligence Community.

As Assistant Secretary Janice Gardner will describe shortly, the 2007 request provides funding for OIA to continue its efforts to build Treasury's intelligence capabilities by improving its key infrastructure and adding to its analytic breadth and expertise.

Office of Foreign Assets Control

The Office of Foreign Assets Control (OFAC) administers and enforces economic and trade sanctions based on U.S. foreign policy and national security goals against targeted foreign countries, terrorists, international narcotics traffickers, and those engaged in activities related to the proliferation of weapons of mass destruction. Since receiving expanded designation authority in 2001, the United States has designated 428 terrorist-related individuals and entities; 320 of those designations have been carried out in coordination with our allies and designated at the United Nations. The fiscal year 2007 budget provides additional resources for OFAC to monitor and update existing designations and track the development of new support structures and funding sources. It includes:

—Ten additional positions to continue to implement and administer the new Executive Order 13382, combating the proliferation of weapons of mass destruction.

—Fifteen additional positions to monitor and update existing terrorist designations. This is critical given that Specially Designated Global Terrorists and their support networks continuously seek new ways of evading U.S. and international sanctions by changing the names and locations of front companies and altering their financing methods.

Office of Terrorist Financing and Financial Crime

As the policy development and outreach office for TFI, the Office of Terrorist Financing and Financial Crime (TFFC) collaborates with the other elements of TFI to develop policy and initiatives for combating money laundering, terrorist financing, WMD proliferation, and other criminal activities both at home and abroad. TFFC works across the law enforcement, regulatory and intelligence communities and with the private sector and its counterparts abroad to identify and address the threats presented by all forms of illicit finance to the international financial system. TFFC advances this mission by promoting the transparency of the financial system and by developing and facilitating the global implementation of targeted financial authorities to identify and intercept those illicit actors that operate within the financial system. TFFC's efforts focus on:

—developing and facilitating the implementation of global anti-money laundering and counter-terrorist financing standards, primarily by working with and through the Financial Action Task Force the various regional bodies, including the IMF and World Bank and each of the regional development banks;

—promoting the development of effective targeted financial sanction regimes and the use of other targeted financial authorities through the G7, G20, FATF, United Nations, European Union, and bilaterally with countries of strategic importance;

—addressing financing mechanisms of particular concern by developing AML/CFT protective measures, initiatives, and best practices in vulnerable sectors such as charities, alternative value transfer systems and emerging payment systems; and

—conducting direct outreach to the domestic and international private sector to facilitate and improve development and implementation of sound AML/CFT controls.

In all of these areas, TFFC relies on and works closely with other elements of TFI, the Treasury Department, the interagency and international communities to effectively combat the threats that illicit finance presents to the international financial system. Recently, for example, TFFC worked closely with 16 Federal bureaus and offices from across the law enforcement, regulatory, and policy communities to produce the U.S. Government's first-ever Money Laundering Threat Assessment. This working group pulled together arrest and forfeiture statistics, case studies, regulatory filings, private and government reports, and field observations. The report analyzes more than a dozen money laundering methods and serves as a first step in a government-wide process to craft strategic ways to counteract the vulnerabilities identified.

The fiscal year 2007 request continues the administration's support of TFFC's important efforts.

Treasury Overseas Presence

Treasury attachés serve as the U.S. Treasury's representatives in key economies overseas. Because of their technical expertise, Treasury attachés enjoy unique access to foreign Ministries of Finance and Central Banks. This access provides the U.S. Government with a direct channel to key decisionmakers on economic policy issues, including foreign exchange policy and financial service regulatory policies. Working in tandem with TFI and Treasury's Office of International Affairs, Treasury attachés will be working to prevent the abuse of the international financial system for terrorist finance, money laundering, or other illicit purposes.

—Treasury proposes to increase its overseas presence from 5 attachés to 18 attachés in fiscal year 2007.

Financial Crimes Enforcement Network

TFI's Financial Crimes Enforcement Network (FinCEN) helps to safeguard the U.S. financial system from the abuses of financial crime, including terrorist financing, money laundering, and other illicit activity. This is accomplished primarily through the Bank Secrecy Act, which requires financial institutions to report financial transactions, such as suspicious activities that may be indicative of financial crimes. FinCEN also supports law enforcement, intelligence, and regulatory agencies through sharing and analysis of financial intelligence, and building global cooperation with financial intelligence units (FIUs) in other countries. The fiscal year 2007 request provides additional resources to FinCEN to streamline data processing and enhance its e-filing capabilities to increase the ease of compliance with regulations and improve its abilities to track users' needs. It includes:

—Enhancing components of the BSA Direct Umbrella System, including electronic filing and secure access components. Although FinCEN has entered a stop work order with respect to development of the data storage and retrieval component of the BSA Direct system in order to permit it to assess delays in deploying this component, both the electronic filing component and secure access components are presently operational and need to be upgraded to allow direct input of the BSA filings into the collection system and meet expanded user base.

—Development funding for FinCEN's Cross-Border Wire Transfer System Initiative. The authorizing language (Section 6302 of the Intelligence Reform Act of 2004 (S. 2845 Public Law 108–458)) presents the Bureau with two tasks: (1) a feasibility study to be completed as soon as practicable; and (2) the implementation of enabling regulations and a technological system for receiving, storing, analyzing, and disseminating the reports, to be completed by December 2007. The feasibility study will address whether it is possible to complete the development and implementation of the system by the statutory deadline of December 2007. We anticipate delivery of the study to the Secretary of the Treasury by late spring 2006.

CONCLUSION

Mr. Chairman, the Treasury Department—working closely with other Departments and agencies across the U.S. Government—is playing a key role in deterring and defending against the greatest threats to our security. Indeed, we have achieved some important successes in our 2-year history. I look forward to working closely with you, other members of the committee, and your staff to ensure that TFI has the resources it needs in fiscal year 2007 to build upon that success. Together we can work to maximize the Treasury Department's ability to protect the American people.

Thank you again for the opportunity to testify today.

Senator BOND. Thank you, Mr. Levey.

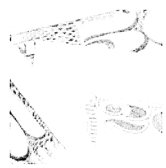
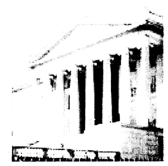
STATEMENT OF JANICE GARDNER

Ms. GARDNER. Good morning, Chairman Bond and Ranking Member Murray. I thank you for the opportunity to testify today on the budget for the Office of Intelligence and Analysis.

I would like to request a copy of our report for fiscal year 2006 to 2008, our Strategic Direction, to be entered into the record. We produced this report for your committee in response to the conference report accompanying the fiscal year 2006 appropriations bill. The report defines our mission, establishes strategic objectives, and outlines OIA's priorities and direction for the next several years.

Senator BOND. Without objection.

[The information follows:]

REPORT FOR SENATE & HOUSE APPROPRIATIONS COMMITTEES

MARCH 01 2006

OFFICE OF INTELLIGENCE AND ANALYSIS
OFFICE OF TERRORISM AND FINANCIAL INTELLIGENCE

Office of Intelligence
and Analysis

Strategic Direction

Fiscal Years (FY) 2006-2008

Office of Intelligence and Analysis
Strategic Direction
Fiscal Years (FY) 2006-2008

Operational Charter

The Office of Intelligence and Analysis (OIA) was established by the Intelligence Authorization Act for FY 2004. The establishment of OIA is codified at Title 31, United States Code, Section 311. The Act specifies that OIA shall be responsible for the receipt, analysis, collation, and dissemination of foreign intelligence and foreign counterintelligence information related to the operation and responsibilities of the Department of the Treasury. The Act established the Assistant Secretary for Intelligence and Analysis as the head of OIA.

On April 28, 2004, Secretary of the Treasury John Snow established the Office of Terrorism and Financial Intelligence (TFI) by Treasury Order 105-17. The Order placed OIA within TFI, and the Assistant Secretary for OIA reports directly to the Under Secretary for TFI. The Order also placed the Office of Terrorist Finance and Financial Crime (TFFC), the Office of Foreign Assets Control (OFAC), Financial Crimes Enforcement Network (FinCEN) and the Treasury Executive Office for Asset Forfeiture (TEOAF) within TFI. The Order specifies that:

- OIA will build a robust analytical capability on terrorist finance by coordinating and overseeing work involving intelligence analysts in all Treasury components. OIA will focus on the Department's highest priorities, as well as ensuring that the existing intelligence needs of OFAC and FinCEN are met.
- OIA also will provide intelligence support to senior Treasury officials on a wide range of international economic and other relevant issues. OIA will serve in a liaison capacity with the Intelligence Community (IC) and represent the Department in various intelligence-related activities.

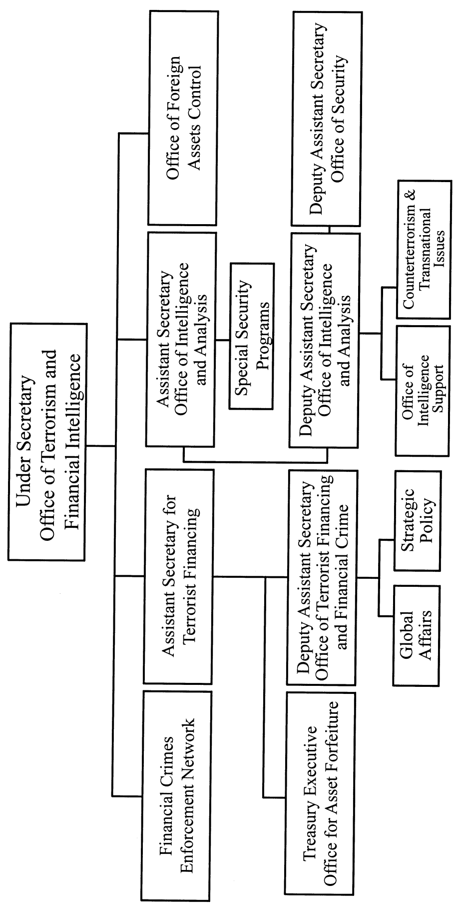
TFI mission

TFI marshals the Department's unique policy focus, financial intelligence, global network, regulatory responsibilities, tools and authorities to safeguard the financial system and counter the financial underpinnings of national security threats.

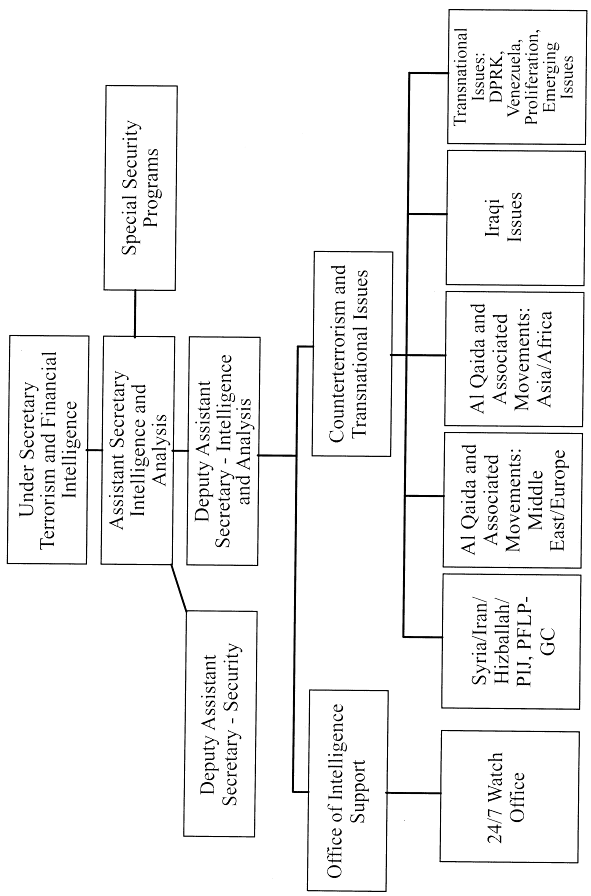
TFI Priority Areas

- Terrorism Financing
- Proliferation
- Rogue Regimes
- Money Laundering/Narcotics

Treasury TFI Structure



Office of Intelligence and Analysis Structure



OIA Mission Statement

Support the formulation of policy and execution of Treasury authorities by providing:

- Expert analysis and intelligence production on financial and other support networks for terrorist groups, proliferators, and other key national security threats
- timely, accurate, and focused intelligence on the full range of economic, political, and security issues

OIA Operating Principles

- Objective, unbiased, and expert analysis on the financial and other support networks for terrorists, proliferators and other key national security threats.
- Communication among workforce and across TFI.
- Development of human capital.
- Acquisition of up to date analytic tools and information technology systems
- Priorities in line with those of Treasury, the National Security Council, and the Intelligence Community.

OIA GOALS

Goal 1. Support the formulation of policy and execution of Treasury authorities by providing expert analysis and intelligence production on financial and other support networks for terrorist groups, proliferators, and other key national security threats.

This goal will remain OIA's top overall priority in FY 2006-2008. The primary responsibility for fulfilling this goal will fall to OIA's Counterterrorism and Transnational Issues section (CTI), OIA's analytic component. As part of their "all source" analysis, CTI's analysts regularly review a broad range of information from the IC, including human and signals intelligence reports, other agencies' analytic assessments, as well as open source information.

OIA's role in this regard is to ensure that the current intelligence information and analysis are incorporated into all aspects of policy deliberations. To accomplish this, OIA will provide decision makers in TFI with strategic targets and policy options in a form that facilitates Departmental action. OIA will also serve as the central focal point for the Treasury Department to fuse financial data from OFAC, FinCEN, TFFC, as well as the IC.

Since OIA was created in 2004, it has made significant progress in building the robust intelligence and analytic program which enables it to provide this type of support to policymakers. OIA was greatly enhanced in FY 2005 by the detail—which is now a permanent transfer--of 23 analysts from OFAC's Foreign Terrorist Division (FTD). Moving the FTD analysts to OIA has helped transform Treasury from a passive consumer of analytic and intelligence products to a full member of the IC. OIA has been using the expertise of these FTD analysts as a foundation for a true center of expertise on material support to terrorist organizations and proliferators. The additional personnel that OIA is planning to hire in FY 2006 will allow OIA and Treasury to further improve its analytic coverage and expertise in priority areas, such as insurgency funding, terrorist financing, and proliferation financing. This will enable OIA to continue to improve its ability to provide policymakers with the relevant intelligence and expert analysis that they need to make policy decisions.

TRANSLATING INTELLIGENCE INTO POLICY: TFI TARGETING MEETINGS

In 2005, OIA initiated weekly targeting sessions led by TFI's Under Secretary, which includes senior officials from OFAC and FinCEN as well. At these sessions, based on a review of the relevant intelligence, potential targets are presented and discussed. The participants assess the full range of potential Treasury actions, including designation, and decide on follow up direction and assignments. OIA will continue to host and participate in these sessions in FY 2006-2008, which have proved to be an effective mechanism for translating intelligence information into policy action.

Objective 1: Provide timely and insightful intelligence analysis that is focused on supporting Treasury authorities.

- Provide intelligence analysis that supports Treasury's designation of persons pursuant to economic sanctions imposed by Executive Order, statute, and/or UN Security Council resolution.
- Provide intelligence analysis on proliferation financing to support OFAC and other Treasury entities in their efforts to target WMD proliferators.
- Provide intelligence analysis that supports Treasury's engagement of foreign authorities to set appropriate standards to safeguard the international financial system, such as Treasury's participation in the Financial Action Task Force and similar fora.
- Coordinate and oversee intelligence analysis that supports designation of foreign jurisdictions, financial institutions, classes of financial transactions, or types of accounts pursuant to Section 311 of the USA PATRIOT Act.
- Provide intelligence analysis that supports the identification and repatriation of assets looted by corrupt foreign officials.

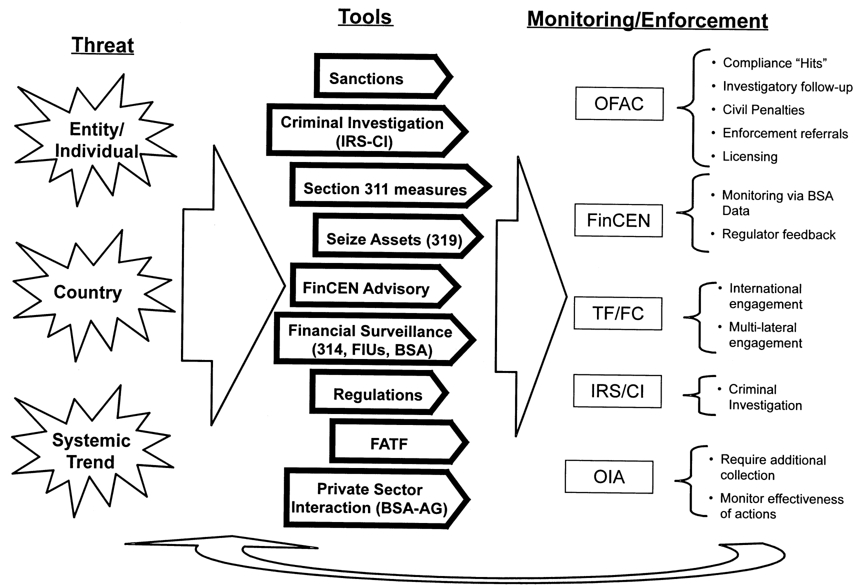
Objective 2: Provide current intelligence analytical support.

- Rapidly alert senior Treasury policymakers to breaking developments affecting their areas of responsibility, and identify opportunities for Treasury Department action associated with those developments.
- Respond to questions from senior Treasury policymakers regarding breaking developments and provide rapid, accurate responses.

Objective 3: Provide strategic intelligence analysis that supports long-term policy development by Treasury regarding the nature and extent of threats to, and abuse of, the financial system.

- Conduct broad, comprehensive analysis of the financial networks of terrorists, proliferators, and other criminals, evaluating their vulnerability to interdiction under existing and potential Treasury authorities.
- Identify financial modalities or techniques used, or potentially used, by terrorists, proliferators, and other criminals; assess the threat they pose to the US and international financial system; and evaluate the effectiveness of existing and potential Treasury authorities to interdict them.

Action Flow-chart



FY 2006 Strategic Analysis Priority Areas

In FY 2006, OIA analysts will be completing strategic research papers, on high priority terrorist and proliferation financing topics. OIA has completed a research and production plan for FY 2006, to help guide OIA's activities during the upcoming year. The plan was coordinated with OIA's primary customers, including TFFC, OFAC, and FinCEN, and is consistent with IC, NSC, and Treasury priorities.

- **Terrorist Financing:** Over the past several years, the terrorist threat has become far more decentralized in nature, and many terrorist groups affiliated with al Qa'ida now pose a serious threat to US national security. In FY 2006, OIA will continue to develop its analytic expertise and expand its analytic coverage on the financial and other support networks of the various terrorist groups and networks bent on attacking the U.S. and its allies.
- **Insurgency Financing:** OIA will attempt to improve its understanding of the insurgency financing in FY 2006, primarily through the Baghdad-based Iraq Threat Finance Cell (ITFC) for which Treasury serves as the co-lead with Department of Defense. ITFC was established to enhance the collection, analysis and dissemination of intelligence to combat the Iraqi insurgency. Such intelligence is critical to support and strengthen U.S., Iraqi and Coalition efforts to disrupt and eliminate financial and other material support to the insurgency.
- **Rogue Regimes/Proliferation Financing:** Over the past year, OIA has assumed an increasingly important role in Treasury's effort to combat other national security threats, including rogues regimes involved in WMD proliferation, such as Iran, Syria, and North Korea. In FY 2006, OIA will continue to build on its nascent effort in this critical area.

Goal 2. Provide timely, accurate and focused intelligence support to the Department on the full range of economic, political, and security issues.

Prior to the creation of OIA, the Office of Intelligence Support (OIS) was Treasury's sole intelligence component. The intelligence support provided by OIS to the senior leadership in the Department had dwindled in recent years, leaving only a minimum viable liaison function and a 24/7 Watch Office. OIS, which is now an office within OIA, is attempting to remedy this situation, by providing enhanced support to the Secretary, Deputy Secretary, Undersecretary for International Affairs, and other senior Departmental officials outside of TFI. OIS has been particularly focused on improving the level of support for Department senior leadership for National Security Council meetings and meetings with foreign leaders. It is crucial that Treasury officials are fully prepared to participate in these forums. Intelligence provides an essential element of this preparation, providing unique insights into context, conditions, and personalities surrounding key national security issues. In FY 2006-2008, OIA will strive to increase both the depth and breadth of intelligence provided to the Department.

Objective 1: Better integrate intelligence support into policymaking process.

- Conduct zero-based review of current intelligence support; identify and address shortfalls through creation of new products/ dissemination means.
- Formalize and expand process for supporting senior officials' requirements with an emphasis on "just-in-time" support for foreign travel, NSC/NEC policy meetings, and meetings with foreign officials.

- Explore means to deliver more intelligence to a wider audience.

- Develop and enhance methodology for providing current intelligence to senior leadership.

Objective 2: Improve integration and collaboration with IC, to foster better IC support to Treasury on economic, financial, and political issues.

- Review, update, and submit Treasury's collection, production, and dissemination requirements to appropriate IC agencies.

- Develop mechanisms to alert IC to Treasury issues of concern.

- Provide regular feedback to IC on quality and focus of their support to Treasury.

Objective 3: Upgrade warning and current intelligence functions.

- Shift focus of Watch Office from information control/distribution and communications support to intelligence operations center.

- Review and reengineer Watch Office processes to expand capabilities and improve effectiveness.

Goal 3. Establish Treasury as a fully integrated member of the IC.

The December 2004 Intelligence Reform and Terrorism Prevention Act (IRPTA) has made this goal particularly critical, as the act places a premium on information exchange and collaboration within the IC. Over the past several years, due to resource constraints, the Department has not effectively engaged with the rest of the community, resulting in the lack of communication and missed opportunities for cooperation. As one of the 15 components of the IC (and the smallest), OIA needs to play a more active role in the community. The newly created position of Assistant Secretary for Intelligence and Analysis has put OIA specifically, and Treasury more generally, in a better position to effectively interact with the IC, particularly with respect to the Director of National Intelligence (DNI).

During its short tenure, OIA has already made great strides in integrating Treasury into the IC, and will continue to build on these efforts in FY 2006-2008. For OIA, an important initial step in improving its integration into the IC was ensuring that OIA's priorities are closely aligned with those of the IC, writ large. As is discussed at greater length below, OIA priorities and direction are closely aligned with those set forth by the Director of National Intelligence in the National Intelligence Strategy. OIA's goals and direction align with key DNI objectives in a number of areas, including: strengthening analysis, WMD proliferation, keeping policymakers informed, and building an integrated intelligence capability. (*See Appendix A*).

In addition, for the first time in FY 2005, Treasury's intelligence office produced all source intelligence analytic products, which were disseminated to the IC, on terrorist financing and other important national security issues. For example, OIA produced a finished piece on the activities of an important Non-Governmental Organization (NGO), which may be providing support to terrorist organizations. TFI's Under Secretary passed a diplomatic note--based on this finished piece--to the foreign government where this NGO is based, demanding that this government take action against the NGO. In addition, OIA disseminated over 50 cables to the IC in 2005. These cables provide valuable information to other IC members on the financial activities of known or suspected terrorists and their networks.

In 2005 OIA analysts also participated in the drafting and coordination on a variety of IC analytic products. These include: National Intelligence Estimates, CIA studies, Senior Executive Intelligence Briefs and Presidential Daily Briefs. The additional personnel OIA is hiring will allow OIA to further increase its contributions to IC products, and to produce additional finished intelligence pieces, for dissemination to the IC.

OIA has also established detail arrangements with various intelligence, law enforcement and military agencies, in an effort to improve information sharing and coordination. These detail assignments include:

- **Military:** OIA has analysts detailed to 3 of the military commands—CENTCOM, PACOM, and EUCOM—and a military officer from CENTCOM is assigned to OIA. OIA also has an established liaison relationship with SOUTCOM.

- **Law Enforcement:** The FBI has detailed an intelligence analyst to OIA.

- **Intelligence:** A representative from NSA is assigned to OIA to provide support to senior Treasury officials, and an analyst from CIA is detailed to OIA to support OIA's counterproliferation efforts.

As OIA grows in size, we plan to expand the scope of our detail assignments with U.S. intelligence, law enforcement and military agencies. For example, in FY 2006, OIA will be integrating a SOCOM detailee into OIA. In addition, over the next several years, OIA also intends to explore the possibility of detailing an OIA analyst to the CIA; working with NSA to detail an additional officer to OIA; and, arranging a temporary assignment of an OIA analyst to the National Counterterrorism Center (NCTC). In FY 2006-2008, OIA is also planning to engage in both formal and informal analytic exchanges with its intelligence and law enforcement partners. For example, the FBI and OIA have agreed to work on several joint analytic projects during the upcoming year. This type of collaboration with FBI will continue in FY 2007-2008.

OIA has also been involved in the efforts by the DNI and the National Security Council/Homeland Security Council to transform the information sharing environment. OIA represents Treasury on the Information Sharing Council and on the Information Sharing Policy Coordinating Committee.

Objective 1: Increase Treasury representation in IC forums and provide Treasury input to IC assessments and plans.

- Increase participation in IC collection and production boards.

- Reinvigorate relationship with National Intelligence Council.

- Provide senior-level input into the production and reviews of IC plans and assessments.

- Increase participation in DNI and NCTC Working Groups and Task Forces.

Objective 2: Develop formal and informal mechanisms for the dissemination of Treasury intelligence products to appropriate IC members.

- Refine and expand process for producing Treasury cables and other formal products, including finished intelligence pieces.

- Develop Intelink and SIPRNet websites.

- Explore possible mechanisms to make information gathered by Treasury officers through overseas travel and contact with foreign officials available to the IC.

Objective 3: Increase Treasury's timely access to relevant IC information.

- Expand analytic details and exchanges with other IC agencies.

- Increase collaboration with other IC agencies on analytic projects.

- Participate in DNI and HSC/NSC Information Sharing Initiatives.

Objective 4: Develop bilateral relationships with key foreign partners through the DNI's office.

- Identify several key potential foreign intelligence/law enforcement partners.

- Develop strategy and objectives for bilateral partnership.

Goal 4. Coordinate and oversee intelligence throughout the Department, including OFAC's and FinCEN's intelligence analysis.

OIA is responsible for coordinating and overseeing intelligence analysis within the Department. As part of these duties, OIA will review all finished intelligence products drafted by individual TFI components and circulate them throughout TFI in order to produce an integrated product for senior policymakers. OIA will also serve as the central coordinating point for the intelligence collection requirements process. An important aspect of this process will involve working with FinCEN to feed collection requirements for the Department of the Treasury to the Financial Intelligence Units (FIU) worldwide. Moreover, OIA will also oversee the Department's intelligence analysis by providing input into performance evaluations of appropriate analysts within TFI.

In 2005, OIA hired a full time Requirements Officer, who is aggressively submitting requirements and evaluations on behalf of all Treasury entities, including OFAC and FinCEN, to the IC. In these requirements submissions, Treasury includes comprehensive background information as well as a detailed statement of Treasury's intelligence gaps to help focus the IC on Treasury's needs. In response to these detailed requirements, Treasury has received a greatly increased level of tailored support from the IC. OIA will attempt to further improve its integration into the IC requirements process in FY 2006-2008.

Objective 1: Drive intelligence analysis throughout the Department and provide guidance on intelligence-related products.

- Prepare target lists, share them with other TFI components, and coordinate prioritization of targets.

- Facilitate regular coordination/information exchanges between OFAC, FinCEN, and OIA analysts, as well as communication with IC.

- Serve as Point of Contact (POC) for tasking from interagency forums dealing with terrorism issues, such as the Terrorist Financing Policy Coordinating Committee or Deputies Committee in order to tap intra-departmental resources in a coordinated, comprehensive manner from the inception of a new project.

Objective 2: Develop efficient and transparent process for execution of common functions.

- Serve as TFI conduit for submission of collection requirements to the IC in order to deconflict and prioritize collection requirements generated by TFI components.

- Establish a common process for submitting downgrade/declassification requests to the IC, including compiling guidance on relevant components at other USG agencies responsible for processing downgrade/ declassification requests. Serve as primary POC to the IC dealing with deliberations regarding modifying the existing declassification process.

- Maintain a library of finished intelligence to be provided to other TFI components in support of ongoing projects.

Objective 3: Serve as the Senior Official of the IC (SOIC), with all DCI Directive-related responsibilities including managing Sensitive Compartmented Information (SCI).

- Appoint and supervise the officers for the handling and protection of SCI, including the Cognizant Security Authority (CSA), Special Security Officer (SSO), and Designated Accrediting Authority (DAA).

- Oversee the secure, timely distribution of all national intelligence and SCI and ensure it is handled in accordance with all applicable directives, plans, and procedures; provide training as appropriate.

- Approve all billets for SCI access, maintain Department-wide security clearance records, and ensure that accurate clearance information is passed to other agencies.

- Oversee the approval, accreditation, and continued security compliance of all Sensitive Compartmented Information Facilities (SCIFs) throughout the Department.

- Ensure appropriate counterintelligence (CI) policies and procedures are in place to protect the Department's sensitive capabilities, to include technical support and travel/threat briefings for senior Treasury officials.

Strategic Goal 5. Invest in people and Information Technology.

In order to fulfill its mission, the Department will need to make a significant investment in OIA's future, particularly in its human resources and analytical tools necessary to get the job done. The office has conducted a zero-based review of its personnel needs, and is working with HR to recruit talented staff with analytical skills. It is also expanding its organizational structure, which will allow for maximum flexibility in meeting the changing priorities of key customers in TFI and International Affairs. Under this structure, the OIA analytic units will be more narrowly focused/tailored than they have been in the past. OIA will also retain the flexibility to "surge" analysts and other resources towards immediate, high priority requirements. OIA will be working to ensure that the new analysts hired in FY 2006 are fully integrated into the units, receive adequate and appropriate training, and have access to the basic analytic tools necessary to identify trends, patterns, and "connect the dots."

OIA will also be working to upgrade TFIN -- the only system used by the Department of the Treasury authorized for Top Secret/Sensitive Compartmented Information (TS/SCI) –which is at risk of catastrophic failure. In FY05, Treasury's Office of the Chief Information Officer, with the Treasury's SOIC providing oversight, began the process of stabilizing TFIN to meet Treasury's current intelligence needs. When the project is complete, TFIN will have:

- New network hardware – servers, routers, firewalls, switches, and workstations

- Up-to-date network software – Operating System and anti-virus tools

- IC CIO Enterprise Architecture compatibility

- Advanced analyst tools

- Complete disaster recover and business continuity capability

Ultimately, TFIN will interact seamlessly within the IC and provide Treasury analysts with the common software tools used throughout the Community to allow timely and efficient collaboration with other intelligence analysts in the IC, other government departments/agencies, and the DoD.

Objective 1: Recruit and hire a high quality workforce.

- Identify the appropriate skills mix to build an agile and highly responsive intelligence analytical unit and intelligence liaison function.

- Develop relationships with outside entities, including universities and other outside experts, to identify potential candidates for recruitment.

- Work with Security to expedite clearance process and get new hires on board.

Objective 2: Retain OIA personnel through career development.

- Develop and implement a training plan for OIA workforce for both analytical training and expertise building, leveraging CIA University, Joint Military Intelligence College, State Department Foreign Affairs Training Center, and other government and non-government education resources.

- Provide opportunities for career development and promotion through expanding variety of assignments, including forward-deployed analysts to the Combatant Commands, National Counterterrorism Center, and details to other agencies.

- Ensure each employee has a career development plan outlining opportunities for training and other assignments.

Objective 3: Recapitalize SCI network and provide analytical tools.

- Provide state-of-the-art analytical environment for OIA personnel and acquire analytical tools such as link analysis and data mining to support the office's ability to conduct in-depth, strategic analysis.

- Develop capability to store, retrieve, and manipulate large quantities of data.

- Rebuild SCI network to provide maximum interoperability with other IC agencies in line with E.O. 13356 and rebuild SCI network to be compatible with the Department of Defense's Defense Messaging System network.

- Develop disaster recovery capability to protect vital electronic records and analytical products.

OIA Human Resources Strategy

OIA is developing a hiring strategy to ensure that it is recruiting a high quality work force with the appropriate skill mix. The addition of the new personnel will enable OIA to take significant steps towards building the robust intelligence and analytic program necessary to fulfill its critical mission.

RECRUIT:

OIA will take advantage of a number of different recruiting fora for its hiring effort. These include:

- IC Job Fairs
- Presidential Management Fellow Job Fairs
- Recruiting fairs at select universities

OIA will also be using a variety of federal recruiting programs, including:

- Presidential Management Fellows Program
- Federal Career Intern Program
- Student Career Experience Program
- Federal Career Fellows

HIRE:

- **Analysts:** OIA will be hiring all source analysts with a variety of experience, ranging from very junior analysts directly out of graduate school to senior analysts with years of relevant experience. OIA will be targeting analysts with prior IC and financial sector experience, as well as relevant regional/area expertise.
- **Economists**: OIA will be targeting economists in its FY 2006 hiring efforts. The Treasury Department has made significant strides over the past several years designating terrorism—and more recently proliferation—targets. Developing a better impact of the economic impact of the sanctions is essential in assessing whether Treasury is focusing on the appropriate types of targets. OIA economists will work closely with the other all source analysts to analyze the likely effect of future designations.
- **Information Officer:** As OIA expands, its IC administrative needs will increase as well. OIA will be hiring an officer, who will facilitate OIA's downgrade/declassification requests. These types of request are essential for Treasury's designations and for its diplomatic outreach efforts.

OIA Hiring Strategy, Continued

TRAIN:

- Develop and implement a training plan for entire OIA workforce.
- Appoint a Point of Contact for all training-related matters.
- Ensure that analysts of all experience levels receive appropriate training, including courses on: analytic tradecraft, analytic briefing/presentation, relevant regional/subject areas, and analytic tools.
- Ensure each employee has a career development plan outlining opportunities for training and other assignments.
- Leverage existing US Government training courses, including CIA University, Joint Military Intelligence College, State Department Foreign Affairs Training Center, as well as non-government education resources.

RETAIN:

- Provide opportunities for career development and promotion through expanding variety of assignments, including at the Combatant Commands, National Counterterrorism Center, CIA, and other agencies.
- Raise promotion potential for both managerial and analytic positions, in light of evaluation of current responsibilities.
- Provide the analysts with opportunities to frequently brief senior level Treasury and IC officials, as well as Congressional oversight committees.
- Provide opportunities for both overseas and domestic travel to continue development of expertise and skills.

Measuring OIA's Performance

- OIA has identified a number of potential metrics, against which we will collect data that will permit us to evaluate our current and future performance. As OIA evolves, we will conduct a continuous internal review to ensure that we are using appropriate performance measures. We may find the need to modify both the baselines and the performance measures themselves as a result of this evolution and evaluation.
- OIA's metrics –which are aligned with the DNI's strategic objectives -- are designed to ensure that OIA is fulfilling the objectives outlined in this plan. They include:
    - Contributions of OIA analysts to IC products
    - Customers' satisfaction with timeliness, accuracy, and relevance of OIA's products
    - Integrating the new analytic hires into OIA by providing them with adequate and appropriate training, mentoring and analytic tools
- We are also in the process of developing additional metrics as well.
- We anticipate that this performance management process will be particularly valuable for OIA in judging our progress in the technological arena. In FY 2006, for the first time, we will be closely tracking the TFIN system's performance to establish a baseline. We plan to measure our progress, in large part, by measuring the system's performance in future years against the baseline we establish this year. We hope to see that our efforts to upgrade the system will result in far fewer system failures than we are currently experien

OIA Goals Closely Aligned with those Established by the DNI

OIA's priorities for FY 2006 are closely aligned with those of the DNI, as outlined in the DNI's October 2005 National Intelligence Strategy.

- **Informed Policymakers:** One of the DNI's top mission objectives is to "anticipate developments of strategic concern and identify opportunities as well as vulnerabilities for decision-makers." OIA's top strategic goal to "provide policymakers with relevant intelligence and expert analysis to support the formulation of policy and execution of Treasury authorities" is consistent with this objective. OIA's increased focus on strategic intelligence analysis in FY 2006 will also help OIA identify emerging issues relevant for policymakers.

- **Analytic Expertise:** Transforming OIA into a center of analytic expertise on financial and other support networks for terrorist groups, proliferators, and other key national security threats, is in line with one of the DNI's top enterprise objectives, which is to "strengthen analytic expertise, methods, and practices; tap expertise wherever it resides; and explore alternative analytic views."

- **WMD Proliferation:** The Treasury Department's ability to target proliferators of weapons of mass destruction was enhanced in June 2005 with the issuance of Presidential Executive Order 13382. This order applies the same tools Treasury has used to successfully block the assets of terrorist supporters to those who aid in the spread of weapons of mass destruction. OIA's increased focus on this issue is aligned with the DNI's objective of preventing and countering the spread of weapons of mass destruction.

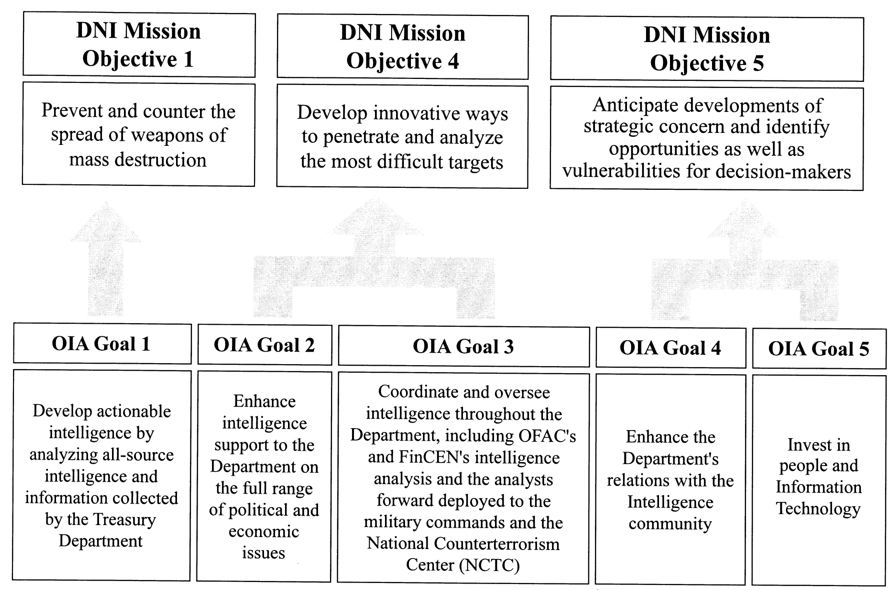
- **Integrated Intelligence Capability:** The DNI's top enterprise objective is to "build an integrated intelligence capability to address threats to the Homeland..." Two of OIA's strategic goals are in line with this DNI objective. OIA's efforts to enhance the Treasury Department's relations with the IC will help the DNI achieve this broader objective. OIA is also responsible for building an integrated intelligence capability within Treasury, with its responsibility for coordinating and overseeing intelligence throughout the Department. Unifying and strengthening Treasury's intelligence efforts will also help the Department build stronger ties to the IC.

OIA Goals Align with Key DNI Enterprise Objectives

DNI Enterprise Objective 1	DNI Enterprise Objective 2	DNI Enterprise Objective 3	DNI Enterprise Objective 4
Build an integrated intelligence capability to address threats to the homeland, consistent with US laws and the protection of privacy and civil liberties	Strengthen analytic expertise, methods and practices; tap expertise where ever it resides; and explore alternative analytic views	Rebalance, integrate, and optimize collection capabilities to meet current and future customer and analytic priorities	Attract, engage, and unify an innovative and results-focused Intelligence Community workforce

OIA Goal 1	OIA Goal 2	OIA Goal 3	OIA Goal 4	OIA Goal 5
Develop actionable intelligence by analyzing all-source intelligence and information collected by the Treasury Department	Enhance intelligence support to the Department on the full range of political and economic issues	Coordinate and oversee intelligence throughout the Department, including OFAC's and FinCEN's intelligence analysis and the analysts forward deployed to the military commands and the National Counterterrorism Center (NCTC)	Enhance the Department's relations with the Intelligence community	Invest in people and Information Technology

OIA Goals Align with Key DNI Mission Objectives



Ms. GARDNER. In addition, it describes the role that OIA plays in the Treasury Department's intelligence activities, and expands on OIA's efforts to better integrate the office with the rest of the Intelligence Community.

As you know, OIA was established by the intelligence authorization bill in 2004, and prior to the creation of OIA, Treasury did not have an in-house dedicated intelligence analytical element. Our mission is to support the formulation of policy and execution of Treasury's authorities, and it is twofold. One is to support TFI in providing expert analysis of intelligence on financial and other support networks for terrorist groups, proliferators, and other key national security threats. But also to provide timely, accurate and focused intelligence on the full range of economic, political, and security issues for the Secretary, the Deputy Secretary, and the Office of International Affairs.

While we are still a fairly new entity, we have taken a number of significant steps in 2005 toward building the robust intelligence and analytical program necessary to fulfill our mission. We are trying to transform Treasury from a passive consumer of analytical and intelligence products, to becoming a full member of the Intelligence Community, and we are building a foundation to become a true center of expertise on material support to terrorist organizations.

The funding allocated by Congress for fiscal year 2006 is allowing us to make significant additional improvements in a number of areas. For example, we have completed a research and production plan for fiscal year 2006 to help guide our activities during the upcoming year. The plan was coordinated with our primary customers including within TFI, but also the entire Intelligence Community and the National Security Council to ensure that our priorities are aligned with the administration.

In particular, we are trying to improve our understanding of insurgency financing in fiscal year 2006 primarily through the Baghdad-based Iraq Threat Finance Cell that you had mentioned, Mr. Chairman, for which Treasury serves as the co-lead with CENTCOM at DOD. ITFC was established to enhance the collection, analysis, and dissemination of intelligence to combat the Iraqi insurgency, and that kind of intelligence is really critical to support and strengthen U.S. and Iraqi coalition efforts to disrupt and eliminate financial and other material support to the insurgency. In fact, the Treasury's presence in Iraq on ITFC is already paying some dividends. More and better detailed information on the insurgency financing issues is becoming available. In addition, the financial intelligence analysts have provided great support to the military in identifying trends and patterns in insurgency financing in the context of a cash-based economy like Iraq.

The funding request for fiscal year 2007 will enable OIA to continue its efforts to build our intelligence capabilities by improving key infrastructure and adding to our analytical breadth and depth on terrorist financing and the financial underpinnings of other national security threats.

Let me just briefly mention the initiatives that we have. The first one was one that you had mentioned, the Treasury Foreign Intelligence Network, which is the sole source of top secret information into the Treasury Department. When TFI was created, our counterterrorism-related responsibilities were expanded dramatically, and the current system has not been modified or updated to keep pace with changes in either intelligence user or technological requirements. The operating system is no longer supported, and our frequent crashes have been preventing senior Treasury officials from receiving intelligence in a timely manner. What we will be doing in response to some of your concerns on the IT management, we have tried to leverage the expertise of the Intelligence Community, so they are helping us so that we are not reinventing the wheel, and we are taking off-the-shelf software and hardware. We are also using the CIA to help do the project management for us, so we have two levels of oversight. We have asked the DNI's office, the Director of National Intelligence, to also take a look. They have a new CIO, and they are coming also to take a look at us to make sure that we are on the right track. So we are ensuring that we do have the proper project management discipline in place that the Secretary has mentioned.

In addition to TFIN, we have an initiative for All Source Analysis Capability. As Under Secretary Levey mentioned, over the past year as OIA has grown, policy makers both at Treasury and at the White House have become more aware of Treasury's capabilities, and OIA has increasingly been tasked with addressing the most pressing national security issues. Given our small size, we have gone from zero analysts in the beginning of fiscal year 2005, to 53 analysts, and will hopefully have 15 more. Bringing these new analysts on board as quickly as possible is essential to our continued success, and these additional positions will allow us to engage in increased analytical exchanges with other national security and Intelligence Community agencies, and this also includes our effort to sustain the effort in Baghdad.

PREPARED STATEMENT

Finally, one more initiative that is important is our secure space. As you know, OFAC also is going to be growing in terms of its terrorism and WMD designation programs, and together we are going to try to make sure that we have the secure space available to house these new analysts.

Thank you very much for your continued support, and for your comments this morning.

[The statement follows:]

PREPARED STATEMENT OF JANICE GARDNER

Chairman Bond, Ranking Member Murray, and members of the subcommittee, I thank you for the opportunity to testify today on the Office of Intelligence and Analysis' 2007 budget request. The Department of the Treasury greatly appreciates the committee's support to this point for our efforts to establish and build the Office of Intelligence and Analysis (OIA).

I request that a copy of OIA's report on its fiscal year 2006–2008 strategic direction be entered into the record. We produced this report for your committee in response to the conference report accompanying the fiscal year 2006 appropriations bill. OIA was required to submit a report that detailed "how OIA will implement the purpose of the Office as intended by the Congress." OIA's report defines its mission, establishes strategic objectives, and outlines OIA's priorities and direction for the next several years. In addition, it describes the role that OIA will play in the Treasury Department's intelligence activities, and expands on OIA's plans to better integrate the office into the Intelligence Community (IC). We hope that the committee members will find the report to be helpful as they consider OIA's 2007 budget request.

I will discuss a number of the themes covered in the OIA report in my prepared remarks today. I will provide some background on our office, provide an overview of the significant progress we made in fiscal year 2005, update you on where we stand with our fiscal year 2006 efforts, and explain how we would plan to use the funds we have requested in fiscal year 2007.

BACKGROUND ON OIA

OIA was established by the Intelligence Authorization Act for fiscal year 2004. The Act specifies that OIA shall be responsible for the receipt, analysis, collation, and dissemination of foreign intelligence and foreign counterintelligence information related to the operation and responsibilities of the Department of the Treasury. Prior to the creation of OIA, Treasury did not have an in-house intelligence analytic element.

On April 28, 2004, Secretary of the Treasury John Snow established the Office of Terrorism and Financial Intelligence (TFI) by Treasury Order, which placed OIA within TFI. As the Assistant Secretary, I report directly to Under Secretary Levey, who heads TFI.

OIA's mission is to support the formulation of policy and execution of Treasury authorities by:

—Producing expert analysis of intelligence on financial and other support networks for terrorist groups, proliferators, and other key national security threats, and

—Providing timely, accurate, and focused intelligence on the full range of economic, political, and security issues.

SIGNIFICANT PROGRESS IN FISCAL YEAR 2005

While OIA is still a fairly new entity, it took a number of significant steps in 2005 towards building the robust intelligence and analytic program necessary to fulfill its critical mission. Moving the OFAC Foreign Terrorist Division (FTD) analysts to OIA was instrumental in transforming Treasury from a passive consumer of analytic and intelligence products to a full contributing member of the IC. OIA has been using the expertise of these analysts—as well as that of the new hires—as a foundation for a true center of expertise on material support to terrorist organizations. As a result, OIA has considerably improved its analytic coverage and capability in priority areas, such as Iraqi insurgency funding.

OIA's top priority, as we mentioned in our report to your committee, is to help translate intelligence into policy. OIA analysts conduct "all source" analysis, regularly reviewing a broad range of information from the IC, including human and signals intelligence reports, other agencies' analytic assessments, as well as open source information. OIA's role in this regard is to then ensure that the current intelligence information and analysis are incorporated into all aspects of policy deliberations. OIA took several steps in 2005 to address this objective.

—Perhaps most significantly, OIA initiated weekly targeting sessions, which are led by Under Secretary Levey and include officials from OIA, OFAC, and FinCEN as well. At these sessions, potential targets are presented and discussed. The participants assess the full range of potential Treasury actions, including designation, and then assign follow up action.

—OIA also began producing analytic papers for Under Secretary Levey, primarily on nongovernmental organizations (NGOs), which may be providing support to terrorists. Under Secretary Levey has passed a number of these papers to the foreign governments where these NGOs are based, asking them to take appropriate action. He has then followed up to ensure that the governments are taking the necessary steps to put a halt to this activity.

In addition to these diplomatic papers, in 2005 Treasury's intelligence office prepared a number of other all source intelligence analytic products on terrorist financing and other national security threats. In fact, OIA has disseminated over 50 cables to the IC over the past year. OIA analysts also participated in the drafting and coordination on a variety of IC analytic products. These include:

—National Intelligence Estimates;

—CIA studies; and

—Articles for senior administration officials, such as the Senior Executive Intelligence Brief.

There were two key reasons why OIA was able to improve its capability to produce all source intelligence analytic products. First, Treasury—through OIA—is becoming far better integrated into the IC than it has been in the past. In 2005, OIA hired its first full time Requirements Officer, who has played a key role in bringing OIA into the IC. This officer is sending in specific questions and inquiries on behalf of all Treasury entities, including OFAC, to the IC. In these "requirements submissions" Treasury includes comprehensive background information as well as a detailed statement of Treasury's intelligence gaps to help focus the IC on Treasury's needs. In response to these detailed requirements, Treasury has received a greatly increased level of tailored support from the IC.

Second, OIA has also built its analytic expertise and improved its access to intelligence information by establishing detail arrangements with various intelligence, law enforcement and military agencies. These detail assignments include:

—*Military*.—OIA has analysts detailed to 3 of the military commands—CENTCOM, PACOM, and EUCOM—and a military officer from CENTCOM is assigned to OIA. OIA also has an established liaison relationship with SOUTCOM. SOCOM is also preparing to assign an officer to OIA.

—*Law Enforcement*.—The FBI has detailed an intelligence analyst to OIA.

—*Intelligence*.—A representative from NSA is assigned to OIA to provide support to senior Treasury officials.

In 2005, OIA also began to build its analytic expertise and coverage in another key area—proliferation financing. The Treasury Department's ability to target proliferators of weapons of mass destruction (WMD) was enhanced in June, 2005 with the issuance of Executive Order 13382. This order applies the same tools Treasury has used to successfully block the assets of terrorist supporters to those who aid in the spread of WMD. OIA analysts were integrally involved in supporting OFAC in developing the designation targets listed in the annex of the Executive Order, and continue to assist OFAC investigators in identifying intelligence reporting that may be useful to support future designations.

BUILDING ANALYTIC COVERAGE AND DEPTH IN FISCAL YEAR 2006

The funding allocated by the Congress for fiscal year 2006 is allowing OIA to make significant additional improvements in a number of areas this year. For example, the additional personnel and the infrastructure improvements funded in fiscal year 2006 are enabling OIA to increase its analytic coverage and to further develop its expertise on the financial aspects of key threats to U.S. national security, including terrorism and WMD proliferation.

In fiscal year 2006, OIA analysts will be completing strategic research papers on high priority terrorist and proliferation financing topics. OIA has completed a research and production plan for fiscal year 2006 to help guide OIA's activities during the upcoming year. The plan was coordinated with OIA's primary customers, including TFFC, OFAC, and FinCEN, and is consistent with IC, NSC, and Treasury priorities.

—*Terrorist Financing*.—Over the past several years, the terrorist threat has become far more decentralized in nature, and many terrorist groups affiliated with al Qaida increasingly pose a serious threat to U.S. national security. In fiscal year 2006, OIA will continue to develop its analytic expertise and expand its analytic coverage on the financial and other support networks of the various terrorist groups and networks bent on attacking the United States and its allies.

—*Insurgency Financing*.—OIA will attempt to improve its understanding of the insurgency financing in fiscal year 2006, primarily through the Baghdad-based Iraq Threat Finance Cell (ITFC) for which Treasury serves as the co-lead with Department of Defense. ITFC was established to enhance the collection, analysis and dissemination of intelligence to combat the Iraqi insurgency. Such intelligence is critical to support and strengthen U.S., Iraqi and Coalition efforts to disrupt and eliminate financial and other material support to the insurgency.

  —In fact, the Treasury presence in Iraq on the ITFC is already paying dividends. More and better detailed information on the insurgency finance issues is becoming available. In addition, the financial intelligence analysts have provided great support to the military in identifying trends and patterns in insurgency financing in the context of a cash-based economy.

—*Rogue Regimes/Proliferation Financing*.—Over the past year, OIA has assumed an increasingly important role in Treasury's effort to combat national security threats, including rogues regimes involved in WMD proliferation, such as Iran, Syria, and North Korea. In fiscal year 2006, OIA is continuing to build on its nascent effort in this critical area.

To accommodate its rapid growth, and to achieve the ambitious goals that have been laid out for OIA, we have developed a hiring strategy to ensure that we are recruiting a high quality work force with the appropriate skill mix. OIA has been taking advantage of a number of different recruiting fora and using a variety of Federal recruiting programs, such as the Presidential Management Fellows Program. In terms of our analytic hires, OIA is hiring all source analysts with a variety of experience, ranging from junior analysts directly out of graduate school to senior analysts with years of relevant experience. OIA is also targeting analysts with prior IC and financial sector experience, as well as relevant regional/area expertise.

OIA is also targeting economists in its fiscal year 2006 hiring efforts. The Treasury Department has made significant strides over the past several years designating terrorism—and more recently proliferation—targets. Developing a better assessment of the economic impact of the sanctions is essential in determining whether Treasury is focusing on the appropriate types of targets. This kind of analysis is extremely valuable not only for Treasury policymakers, but for policymakers elsewhere in the government as well. It can help shed light on what policy tools the U.S. Government should use—and are likely to be effective—against particular countries or targets.

In sum, we believe that we are on track to succeed with our rapid expansion, and that we will make—and are already making—major strides in fiscal year 2006 to continue transforming OIA into a center of analytic expertise on the issue of financial and other support networks for terrorist, proliferators, and other key national security threats.

FISCAL YEAR 2007 BUDGET REQUEST

The funding request for fiscal year 2007 would enable OIA to continue its efforts to build Treasury's intelligence capabilities by improving its key infrastructure and adding to its analytic breadth and expertise.

Our key initiatives in our fiscal year 2007 request include:

TFIN.—The modernization of Treasury's Foreign Intelligence Network (TFIN), the sole information technology system in the Department authorized for Top Secret information. With the creation of Treasury's Office of Terrorism and Financial Intelligence (TFI) and OIA, the Department's counterterrorism-related responsibilities were expanded dramatically. A new information technology architecture was required to support this broader, Congressionally-mandated mission. The current system is unstable and has not been modified or upgraded to keep pace with the changes in intelligence, user, or technological requirements. The operating system is no longer supported and the entire system is at risk of catastrophic failure. The frequent system crashes have been preventing senior Treasury officials from receiving intelligence reporting from other agencies in a timely manner. In addition, the system's performance issues have been hampering the ability of Treasury's intelligence analysts to perform their jobs.

Ultimately, the upgraded TFIN system will allow Treasury to interact seamlessly within the IC and provide Treasury analysts with the common software tools used throughout the Community. It will allow timely and efficient collaboration with other intelligence analysts in the IC, other government departments/agencies, and the Department of Defense.

ITFC.—Our request will allow Treasury to sustain its co-lead role in the Baghdad-based ITFC. Two Treasury officers have already been assigned temporarily to Iraq, where they conducted the initial assessment or "Phase I". "Phase II," which calls for the assignment of Treasury personnel to Iraq on an ongoing basis to bolster the all-source intelligence analysis on the insurgency, is now in progress. Improving the U.S. Government's understanding of the insurgency funding is a key goal for our office, and I as mentioned earlier, this interagency initiative is already paying important dividends.

All Source Analysis Capability.—The additional analysts OIA is requesting in fiscal year 2007 will allow OIA and Treasury to further increase the depth and breadth of its analytic coverage and expertise in priority areas, such as terrorist financing, and proliferation financing. Over the past year, as OIA has grown and policymakers—both at Treasury, in the White House and elsewhere—have become more aware of its capabilities, OIA has been increasingly tasked with addressing the most pressing national security issues. Given its small size and increasing importance, bringing new analysts on board as quickly as possible is essential for OIA's continued success. These additional positions would also allow OIA to engage in increased analyst exchanges with other national security and IC agencies, in accordance with the Intelligence Reform and Terrorist Prevention Act of 2004.

Secure Space.—As the committee is aware, in addition to the proposed OIA growth, the Office of Foreign Assets Control (OFAC) is expanding its terrorism and WMD designations programs. Both OIA and OFAC's expansion is necessary, in part, as a result of the June 2005 Executive Order, giving the Treasury Department additional authority to target proliferators of WMD. The highly classified work of these expanding units can only be accomplished in specially constructed secure areas, known as Sensitive Compartmented Information Facilities (SCIFs). Once the fiscal year 2006 hires have been assigned their work spaces in existing SCIFs, there will be no available SCIF space remaining in the Department. Both OIA and OFAC are requesting additional positions in fiscal year 2007; the Secure Space Initiative is directly linked to that request. Given the lack of remaining available SCIF space in the Treasury Department, we will have to build additional SCIF space to accommodate any fiscal year 2007 OIA and OFAC hires. Adequate security infrastructure is critical to protecting the intelligence and national security functions of the Department. Approval of this initiative will ensure Treasury personnel have the required secure workspaces to support the mission of disrupting and dismantling the financial infrastructure of the terrorists and isolating their support networks.

CONCLUSION

Thanks again for your continued support for OIA and TFI. We appreciate the confidence that your committee has shown in our office to this point. We believe that the resources that we requested in fiscal year 2007 will enable OIA to take the next steps in building the type of robust intelligence capability that Congress envisioned when you created our office.

That concludes my prepared remarks. I would be happy to answer any questions.

TFI AUTHORITIES

Senator BOND. Thank you very much, Ms. Gardner. Mr. Levey, I am delighted to hear that our allies are now saying that we ought to hold financiers to account. You may know I am from Missouri which is called the “Show Me” State. A lot of times I keep thinking about that old country music song, “I Want a Lot Less Talk and a Whole Lot More Action.” Would you please tell us when you start seeing the action? Words are nice.

Let me ask you to explain in a little more detail how TFI has had an impact on combatting terrorist financing and what new powers you have that Treasury could not do before TFI was created, and what additional resources you may need from this committee or from the Intelligence Committee.

Mr. LEVEY. I think maybe we should do that by discussing the initiatives that we have asked for, in addition to the ones that Assistant Secretary Gardner laid out for our Intelligence Office which are critical in order to answer the increased demand. I want to highlight one thing that she said, which is that success breeds demand in this. People are seeing that the actions that we take in terms of looking at the financial system and trying to both make it impervious to illicit activity on the one hand, but also to target illicit activity within it on the other to identify the bad actors and call them out and get financial institutions to say they are going to stop doing business with them. People are seeing that that is really valuable, and so they are asking us to do more and more on different important issues, both with respect to WMD proliferation and terrorism.

In order to do that, one of the most important things we need is the intelligence capability to support it. We need to be able to come up with the analysis, identify the right targets, know the right networks, so that we can exercise our authorities wisely. This is, I think, attributable to the fact that we have this Intelligence Office that Assistant Secretary Gardner leads and that she has been building, but we need to continue to build it, both in terms of personnel and in terms of the infrastructure to support it which is the TFIN network and secure space.

In addition, we need to be able to continue to build up OFAC to follow through on the tactical actions, and so our 2007 budget request includes additional analysts for WMD proliferation and terrorism. On the terrorism issue in particular, what those are for, Mr. Chairman, is to follow up on entities that are already designated, because one thing we know, as you indicated in your opening statement, is that these terrorist entities are very capable and flexible, and we have to be flexible, too. So once we designate someone or an entity, we need to follow up and see how that network is reformulating itself so that we continue to follow up. If we do not do that, then our designation is not nearly as effective. So one of the things we have asked for is support for that.

BANCO DELTA ASIA DESIGNATION

Senator BOND. I think you asked for more time to explain how the impact of the Banco Delta Asia expands. Would you tell us about the follow up on that as well?

Mr. LEVEY. I would love to be able to do that. In fact, we have prepared a diagram. I don't know if you can see that. Do we need to move it closer to you, Senator Murray or Mr. Chairman?

Senator BOND. You don't happen to have it on a little handy cheat sheet, do you?

Mr. LEVEY. Yes, we do.

Senator BOND. That might be a lot easier.

Mr. LEVEY. What this chart shows is how our office works when it works well, and I think this not only a case study, but it is a successful case study.

What we have on the left side with the overlapping circles is TFI, all the different aspects of TFI. You have OFAC, you have the Office of Intelligence Analysis, FinCEN, you have our Policy Office led by Assistant Secretary O'Brien, and you have the IRS which supports us on financial investigations. OIA has the responsibility for pulling all that together through an integrated intelligence analysis. We were looking at North Korean illicit conduct, trying to figure out who were we going to put pressure on North Korean illicit conduct, and through Janice's leadership we were able to pull all of that together and identify what targets we should go after.

We identified a bank in Macau which is a jurisdiction that has money-laundering problems in many ways, but this particular bank was facilitating a wide range of illicit activity on behalf of the government of North Korea, engaged in counterfeiting of U.S. currency, they are engaged in narcotics trafficking, they are engaged in other sorts of criminal conduct, and they were using this bank in order to facilitate that. Not only that, this bank had negotiated a deal with the government of North Korea and these entities that in exchange for fees paid to the bank, they would apply a lower standard of due diligence which is a very tempting thing for someone who is engaged in illicit conduct.

We identified this bank and we designated it under the PATRIOT Act as a primary money-laundering concern. That is the second column. After we all get together and sit down and look at the intelligence analysis. In fact, we have a meeting this afternoon to do this with another target, where we all sit down together and say: "What is the best way to get at this problem?"

In this situation, we identified two things to do to get at the North Korean illicit conduct. The first is the top item, designating the bank under section 311 of the PATRIOT Act. The second one is the Executive order designations below, which is the Executive order that I mentioned in my opening statement that the President issued to give us the power to target and freeze the assets of WMD proliferators. We designated a number. Actually, at this point the President himself designated in the initial Executive order North Korean entities of proliferation concern under that Executive order.

One of those entities that was designated was Tanchon Bank which is a North Korean bank that is the primary financial facilitator for KOMID which is the North Korean military procurement entity, which happened to have a number of accounts and to be a big customer of Banco Delta Asia, so it all came together quite nicely.

Senator BOND. Mr. Levey, we need to get on with the questions. I would say that Banco Delta Asia was what you would call a full-service bank.

Mr. LEVEY. A full-service bank.

Senator BOND. They certainly had it all. I am going to turn now to Senator Murray for questions.

Mr. LEVEY. Thank you, Mr. Chairman.

BSA DIRECT

Senator MURRAY. Thank you very much, Mr. Chairman. I want to go back to some previous discussion about the BSA Direct program very quickly before I ask you some other questions. That program in the past was presented to us as a critical program to combat terrorist financing. Now that this program appears to be kind of on life-support, can you tell us what impact that failure will have on your efforts to monitor compliance with the Bank Security Act?

Mr. LEVEY. Senator Murray, just to preface this, you are right to have all the concerns that you have expressed about the BSA Direct Program, and you are right that we have come to this committee and asked for money for, and support, and we appreciate the support, and what has happened is a disappointment to me as I know it is to you. The new Director of FinCEN, Bob Werner who certainly deserves no blame for this, I want to make sure people understand that. Bob Werner is the new Director who came in to a tough situation, identified these problems, and after consulting with me, took the appropriate action which is to put a temporary work stoppage in place so that we could assess exactly where the project is and make sure that we do not continue to spend money if the project is not going to succeed.

Senator MURRAY. Why did it take the appointment of a new Director to find out that we were way off track?

Mr. LEVEY. The answer to that is that that is an excellent question, and I want to know the answer to that, too. I think as the chairman put it in his opening statement, he is going to ask for people to look at this, and I think that that is appropriate. We need to find out, and I also want to find out the answer to that question, and figure out if there is anything I should have been doing better so that I can make sure that I do not make whatever mistakes I may have made again.

Senator MURRAY. Is this going to move forward now, or are we going to pull the plug?

Mr. LEVEY. What we need to do is, under this temporary stop work order, it gives us 90 days to assess it to determine what is the best next step. The reason we did this now, or the reason that Director Werner recommended that we do this now, and I think it was the right decision, is that by doing this temporary stop work order, we are able to make sure that we do not have a loss of service to our customers in the interim. That is, of course, of the highest priority. We are hopeful that we are going to be able to do this assessment and get through the project without ever losing our customer service. Frankly, we are going to look at the idea I think you mentioned in your opening statement about what benefit we can draw upon and what leverage we can apply to the IRS systems that might be used.

Senator MURRAY. Did I hear you say you are in a 90-day review?

Mr. LEVEY. Yes.

Senator MURRAY. I assume that at the end of that, if you are moving forward, you are going to be able to guarantee to us that you will get all the functionality out of that new system that we were originally promised?

Mr. LEVEY. I will give you a complete briefing on the functionality that will be obtained by the new process and exactly how much it will cost. I think that the chairman's suggestion that we give an action plan on BSA Direct, in whatever time period you think is appropriate, Mr. Chairman, we will do it, is exactly what is called for.

Senator MURRAY. Given all of that, do you still stand behind the request for $12.5 million for this in 2007?

Mr. LEVEY. I think the request is $2.4 million. With your permission, Senator, I would want to refer that question to Director Werner. If it is easier, we can respond in writing and do that promptly.

Senator MURRAY. Is he in the room?

Mr. LEVEY. Yes, he is right here.

Senator MURRAY. If you would not mind, Mr. Chairman.

Senator BOND. I was going to ask Director Werner to come forward. The GAO has raised questions about it and you have raised a very good question.

BSA DIRECT AND THE CROSS-BORDER WIRE INITIATIVE

Senator MURRAY. And with the cross-border wire request as well, it is a $12.5 million request.

Mr. LEVEY. With the cross-border wire it is, yes.

Senator BOND. Mr. Werner, if you will state your full name and title for the record, please.

Mr. WERNER. My name is Robert W. Werner, and I am the Director of Financial Crimes Enforcement Network.

Senator MURRAY. Did you say the new Director?

Mr. WERNER. New Director. Good morning, Mr. Chairman, and Madam Ranking Member. You are correct, the cost is $2.4 million, I think it is $2.473 million, relates to the BSA Direct components. That includes the secure outreach, the BSA electronic filing, and the BSA Direct retrieval and storage component, and then there is $10 million separately requested for the cross-border study.

While the cross-border wire study is related to BSA Direct because ultimately the data would be folded into that program, it is really very distinct at this point. Right now we are in the middle of a feasibility study for the cross-border wire. Given the massive amount of data involved in that, if the Secretary were to approve the feasibility study and decide to go forward with it, that would require tremendous augmentation to existing systems. So the fact of the matter is, we are going to have a retrieval and storage component for BSA Direct, but whether we are able to have the full range of functionality that was originally planned in the current retrieval and storage project, it is too early to say. But we will not have disruption of service to our customers because at this point we are also transitioning to the IRS's Web CBRS system, so we will have a functioning system. Part of what we are reassessing is what exactly the requirement needs are and revalidating those.

Senator MURRAY. This committee will need to know whether you stand by that number or where you are on that fairly soon, so I hope you stay in touch with the committee on that.

Mr. WERNER. We absolutely will, and I can tell you now that the electronic filing component is not involved in the stop work order and is about $1.3 million of that. In addition, the secure outreach which, again, is an operational functioning system and not part of the stop work, is close to about $500,000. So the remainder does relate to the retrieval and storage component, and we will keep you very closely apprised of that.

Senator MURRAY. I appreciate that. Thank you, Mr. Chairman.

Senator BOND. Thank you very much, Senator Murray. The GAO has raised a lot of questions that I know Director Werner is going to have to answer, and we are going to have to answer. So I think this is a work in process, and I think 45 days, if you can make it, is a good timeline to let us know what you found, where you are going to go, and how you can make some chicken salad out of what you have been presented.

Mr. WERNER. We will absolutely keep you briefed. I think at this point we are projecting having a written report hopefully sometime in June, but I think within 45 days we will certainly have a much better idea of where we are and what some of the options are.

TREASURY FOREIGN INTELLIGENCE NETWORK

Senator BOND. Thank you very much, Mr. Werner. Turning to Ms. Gardner, your work I know is extremely important. The DNI has emphasized to us how critical your information is, and we want to know how we can help you get the work done. I do not want to see all of your time taken up as an IT manager because you have very important work to do. So we will look forward to discussing that with you as the process goes forward.

Now I would like to ask, Ms. Gardner, if you can elaborate on the importance of upgrading the Treasury Foreign Intelligence Network, TFIN, especially in terms of how it can help you improve the way that OIA performs its job, and when do you expect TFIN to be complete?

Ms. GARDNER. Thank you, Mr. Chairman. I appreciate the opportunity to talk about TFIN because it is very near and dear to my heart. We do need this capability in order to deliver all of the things that Under Secretary Levey promised that we would be able to do.

The TFIN system was actually built in the 1990's, and it was built in-house, and so it was great at the time, but clearly we need something more now. What we have done is try to take this in two steps. One is, first, to stabilize the current system. That delivery will be on April 18 so that the system crashes that we have been experiencing hopefully will stop. Then the next phase is actually the upgrade to increase capabilities. When the system was built in the mid-1990's, we were just a liaison shop. We did not have analysts doing analytical work. So now we need to be able to put all the bells and whistles of analytical tools, link analysis tools, data retrieval, all those things on there.

I think that we have segmented it in a way so that all the deliveries will be rolling out over the next year. If we do get the budget request in 2007, we are hoping that we will be able to finish all of the phases by the end of the fiscal year with the slight possibility that the Disaster Recovery Site will probably be at initial operating capability, but not at full operating capability until maybe early first quarter 2008.

INTERNATIONAL TERRORIST FINANCING COOPERATION AND THE BANCO DELTA ASIA DESIGNATION

Senator BOND. Thank you. Mr. Levey, I was going to ask you about collaboration with international partners, but I had to cut you off after you just got through the first two columns in your magnificent chart. Let's pick up back on the chart. I would like to know in addition to the particular North Korean Banco Delta Asia, how you are working with the United Nations, the Financial Action Task Force, and other successes, and your challenges, in that area.

Mr. LEVEY. Interestingly, I think right where I stopped is where I was going to get to intelligence cooperation, so I will be able to try to answer two questions at once.

After we took these actions that I described earlier, the next step is to go and talk to our partners around the world and say this is a threat not only to our financial system, it is a threat to the global financial system, and the answer to your question on how that international cooperation is working, Mr. Chairman, is it is working very well. We are getting a huge amount of cooperation internationally when we are able to identify illicit conduct and say this is illicit conduct, it is a threat to our financial system and to yours. And we are getting cooperation not just from governments, but from private financial institutions, and that was the reference I made to UBS in my opening statement.

In the BDA case in particular, I made a trip out to Asia, and then Mr. O'Brien's Deputy also made a trip out to Asia, and we were able to persuade governments in the region that this was a threat to them as well. They took action to put a lot of pressure on this illicit financial network, and they took relevant steps that pushed this North Korean illicit financial activity out of their banking system and left it with no place to go, or searching for a place to go.

Then the last thing is monitoring follow-up, and it comes back to Janice Gardner's work, which is, now we need to see where they are going to try to put their money into the system. What is their next target? They are going to try to access the financial system in another way, and we have to stay on top of it so that we do not just have a temporary victory.

More broadly, Mr. Chairman, the cooperation internationally particularly on terrorist financing has been excellent. We have a growing number of states using the U.N. system on terrorist financing and designating names which is a real important development, and we are continuing to build on that I think through Mr. O'Brien's leadership. He has been doing a lot of good, hard work and spending a lot of time on the road.

TFI REDUNDANCY CONCERNS AND DIFFERENCES BETWEEN TFI COMPONENTS

Senator BOND. One last question. During the early days of TFI there were concerns about the possible redundancy and OIA acting as an operational vice analytical unit. Can you explain how you have addressed these concerns, and explain the differences between FinCEN, OFAC, TFFC, OIA, and any other agencies you have?

Mr. LEVEY. Mr. Chairman, I know that that has been a concern. As you know, when I have come to talk to you in your capacity on the Intelligence Committee, and I have already shown you this in private, this indicates how we work. It is a generalized example of what the North Korean Illicit Finance process is. On the left you see there are particular threats that we feel we need to take action against, and that is where our intelligence function comes in. They are to pull together all the information that we need in order to determine what steps to take. That is not an operational activity, that is classic intelligence analysis, presenting the information to the policy makers so that we can make a choice.

The middle, without going through all the acronyms there, but what that is is a sampling of the tools available to us as an organization, either through OFAC, through FinCEN, through international outreach, through TFFC which is Assistant Secretary O'Brien's organization. We sit down and we go through one of those meetings, we have one this afternoon, as I mentioned, and we will say: "What can we do?" We choose what we think is the right thing to do, and then we go out and do it. We have operational components of what we do in the sense that we are not just developing this information to learn about it, but to act on it, and then we act.

Then the bottom arrow is, after we act, again, just like we are doing with North Korea, the challenge is to see if our action had any effect. To be honest with you, sometimes they are more effective than others. We have to learn not only when we take an action, if it was not as effective as we had hoped, why not, what is the next step so we can learn to do better, and that is, again, where our Intelligence Office comes in.

ADDITIONAL COMMITTEE QUESTIONS

Senator BOND. As followers of the Senate know, all those bells and whistles means that a vote has started. In closing, I appreciate all the hard work and time you and your good leadership team have put in to combatting terrorist financing and other illicit financing efforts. I support and recognize the importance of the 2007 budget request, but I need your help to make sure you succeed, especially in making sure that TFIN does not experience the same problems that BSA Direct has experienced.

[The following questions were not asked at the hearing, but were submitted to the Department for response subsequent to the hearing:]

QUESTIONS SUBMITTED BY SENATOR CHRISTOPHER S. BOND

MANAGEMENT

Question. As I noted in my opening statement, I remain concerned about the Department's management especially since the OIG continues to cite management as their No. 1 concern in their annual challenges report and due to the recent information technology failure with BSA Direct.

How are you addressing this concern, especially on the need for effective corporate leadership in resolving serious deficiencies at the bureau level? Please include specific examples in your response.

Answer. The Department is committed to exercising strong corporate leadership over all components of the Treasury Department—through the policy offices' supervisory and oversight relationships with our bureaus, as well as through the discipline of the traditional management functions such as human resources, information technology (IT), procurement, budget, strategic planning, and financial management. With nearly a full complement of senior officials now in office at Treasury, our ability to emphasize corporate management has been greatly enhanced.

In describing Treasury's corporate management challenge, the Inspector General emphasized the need to provide IRS and bureau oversight and "ensure consistency, cohesiveness, and economy among all bureaus in achieving Treasury's goals and objectives." Over the past 9 months, the Assistant Secretary for Management and Chief Financial Officer (ASM/CFO) has instituted a better process for coordinating Department-wide management issues. The Bureau Heads' Council has been restructured to serve as one of the primary tools of this coordinated management effort. The Council has become an arena for discussing best practices, cohesive policies and strategic priorities based on the President's Management Agenda (PMA), Treasury goals, and bureau goals. Participation is now limited to bureau principals, the ASM/CFO, and the Deputy Secretary to ensure vigorous discussion and extensive exchanges between participants in order to provide thoughtful recommendations to the appropriate Department officials. This reinvigorated Council has addressed operations, management, Homeland Security Presidential Directive-12 (HSPD–12), OMB Circular A–123, the Working Capital Fund, annual budget submissions, the Department's strategic plan, and Emergency Preparedness. These discussions have led to the creation of sub-groups, comprised of a bureau head "champion" as chairman and other interested bureau heads as members. These sub-groups are addressing issues raised during the Council meetings and providing monthly updates upon which they make recommendations to the appropriate officials.

Other examples of how Treasury provides effective corporate oversight and leadership across management functions include:

—The majority of Treasury IT projects are succeeding, including most of the systems mentioned at the April 6, 2006, Senate Appropriations Committee hearing. For example, Treasury's HR Connect system was recently named a Federal Human Resources Management Line of Business (HR LoB) Shared Service Center (SSC) by the Office of Personnel Management and the Office of Management and Budget (OMB). The HR LoB is one of the Presidential E-Government lines of business, which designates agency centers of excellence to provide government-wide servicing for core functions. Currently, the Department's HR Connect program services Treasury, the Department of Housing and Urban Development (HUD) and components of the Departments of Justice and Homeland Security.

—Treasury migrated HUD to HR Connect last year on time and within budget, adding an estimated 10,000 employees to the system. Both HUD and industry recognized Treasury for the cost-effective and smooth transition. Treasury clearly has addressed its past problems with the HR Connect program and continues to drive towards enhanced performance and operating efficiency.

—Treasury has made significant improvement across the core IT management areas measured under the Expanding E-Government (E-Gov) Initiative of the President's Management Agenda. For the first time since the establishment of the PMA in 2002, Treasury improved its overall E-Gov status from Red to Yellow in the first quarter of fiscal year 2006. The improved PMA score was based on Treasury's meeting key requirements and performance metrics. These key requirements and performance metrics included developing Treasury-wide IT capital planning policy, maturing the Departmental Enterprise Architecture, and meeting quarterly milestones for Presidential E-Gov Initiative implementation. This was accomplished in large measure by the efforts of all bureaus through the Treasury Chief Information Officers' Council and its sub-councils.

—The Alcohol and Tobacco Tax and Trade Bureau's (TTB) recent successful migration from the Bureau of Alcohol, Tobacco and Firearms and Explosives (ATF) infrastructure is an example of proper oversight and assistance between the Department and a Treasury bureau. When ATF was divided into two organizations in 2003 (ATF became part of the Department of Justice while TTB remained a Treasury bureau), all IT resources remained with ATF. These IT resources included 100 percent of all capital assets, infrastructure, IT support personnel, and resources to continue development of core business applications. Treasury's senior management team worked closely with TTB bureau executives in developing and implementing smart sourcing strategies. TTB accomplished the migration of its entire IT infrastructure off of ATF in 6 months, which is an extremely aggressive schedule for a migration of this scale. In fact, the migration was completed well ahead of schedule and within an extremely tight budget.

—With respect to the Treasury Communications Enterprise (TCE) procurement, Treasury senior management is engaged in the procurement and the issues raised by the Government Accountability Office (GAO) were resolved. The Department is working closely with Treasury's Inspector General and Treasury senior management to improve documentation for the program.

—To address the new requirements in the Office of Management and Budget (OMB) Circular A–123, "Management's Responsibility for Internal Control," the Treasury Chief Financial Officers' Council formed a cross-bureau and office working group that developed a comprehensive methodology to identify, document, test, and assess internal controls. The work group, established in November 2004, includes permanent participation from 22 of Treasury's 24 financial reporting entities involving 8 bureaus and 6 offices, including advisory participation from the Office of the Inspector General. As a result, Treasury has devised collective financial reporting internal controls, established uniform documentation methods, developed comprehensive test approaches and test plans, and completed over 70 percent of the required testing to date.

Part of the corporate leadership response for improving management at the bureau level is to institute a Program Contract Review (Review). This Review will be added to the quarterly Capital Planning and Investment Control (CPIC) process, and will require Contracting Officers to certify that high impact contracts and contracts related to high impact programs are on target with respect to performance (schedule and quality), budget (cost or price), and the required qualifications of the Program Manager, Contracting Officer, and Contracting Officer's Technical Representative. The goal of the Review will be to ensure improved communication and coordination among the bureau-level professionals responsible for different functional aspects of contract management and mission delivery, and to provide a mechanism for early problem visibility and resolution at the bureau and corporate levels, as needed. Initially, the Review will focus on high impact information technology programs and related contracts already in the CPIC database, and will expand to include a review of all high impact acquisitions, including non-IT acquisitions.

This approach will support the introduction of Earned Value Management (EVM) techniques into our contract portfolio, and will help ensure that Treasury managers follow the sound business practices associated with EVM. It builds on the management platform to strengthen cross-disciplinary support and oversight within two already-established governance processes, CPIC and the Office of Procurement Executive's (OPE) Evaluate & Monitor Program, designed to ensure that Treasury's procurement organizations are in compliance with the law, good practice, and are promoting continuous improvement.

The Evaluate and Monitor Program, managed by the Office of the Procurement Executive, will provide improved corporate oversight of and support to Treasury's operational acquisition organizations, including high impact acquisitions. An Acquisition Bulletin, AB 06–04, http://www.treas.gov/offices/management/dcfo/procurement/policy/ab06-04.pdf, was recently issued requiring all bureaus to identify ongoing, planned, or anticipated procurement actions, defined by the following criteria:

—Acquisitions with an estimated value of more than $10 million;

—Acquisitions with an estimated value more than $1 million if the proposed acquisitions involve more than one bureau, excluding Administrative Resource Center (ARC) support of other Treasury bureaus;

—Acquisitions that require a review by the Treasury Technical Investment Review Board (TIRB);

—Competitive sourcing actions under OMB Circular A–76;

—Acquisition actions that may be controversial or otherwise sensitive such that they warrant the attention of the Senior Procurement Executive, for example, relevant protests or claims, or acquisitions in which interest or inquiries have been expressed by either the White House or Congress, Inspector General (OIG or TIGTA) or Government Accountability Office (GAO).

The Evaluate & Monitor Program is increasing its staffing to improve oversight. Current staffing is 6 FTE, and oversight and support have been improving commensurately.

—The Program/Contract Review, AB 06–04, and the Evaluate & Monitor Program have been reviewed and approved by the Treasury Acquisition Council (TAC). The Office of the Procurement Executive chartered the TAC in April 2005 to improve governance of the acquisition function. The TAC is comprised of the bureau Chief Procurement Officers, the Treasury CIO, and the Deputy CFO. It is chartered to coordinate cross-cutting policy and management issues, develop and implement innovative acquisition approaches, share best practices and lessons learned, oversee and track progress against improvement goals, and make other decisions on issues that have a potential for Treasury-wide impact on acquisition and financial management programs.

The Department also remains focused on enhancing project management capability by establishing a Treasury-wide training program. In line with OPM and OMB guidance, Treasury's existing IT capital planning policy outlines the skills and competencies required for project managers based on project scope and complexity. Currently, bureau CIOs are required to certify that project managers for major investments are qualified according to these guidelines. This initiative, which supplements bureau training programs, will include a project management course focused on Treasury-specific policy and procedures to ensure consistent implementation across the Department.

BSA DIRECT/TFIN

Question. The recent problems exposed with the Financial Crimes Enforcement Network's new system called "BSA Direct" raises serious questions about the Treasury's ability to procure, manage, and oversee information technology projects.

How can I be confident that other high-risk projects such as the "Treasury Foreign Intelligence Network" system (TFIN) will not experience the same problems as BSA Direct? Are you personally committed to providing the necessary support and resources for TFIN and other IT projects and that you will ensure that the lessons learned from BSA Direct will be applied to TFIN and other IT projects?

Answer. The Treasury Foreign Intelligence Network (TFIN) is the sole source of Top Secret/Sensitive Compartmented Information intelligence at the Department of the Treasury. Stabilizing and modernizing the TFIN system is one of the Department's highest priorities.

From a system development view, BSA Direct involves the design and development of a new and complex database application and data warehouse, while the TFIN concept and design is based on best practices already in use within the Intelligence Community.

An effective governance structure has been in place for TFIN since the inception of the project to ensure mission, business, and technical objectives are achieved. This governance structure consists of the: (1) TFIN Executive Board comprised of senior officials from the Office of Terrorism and Financial Intelligence and the Office of the Chief Information Officer (OCIO), and (2) TFIN Steering Committee comprised of project management and technical leads from stakeholder offices. These governance structures facilitate coordination, track project status, and support executive decision-making. OCIO hired a dedicated project manager to oversee the TFIN project.

Treasury has established additional oversight as well. The Assistant Secretary for Management and Chief Financial Officer (ASM/CFO), the Chief Information Officer (CIO), and the Assistant Secretary for Intelligence and Analysis (OIA) are committed to ensuring the project's successful completion. The ASM/CFO and CIO are engaged fully with the Assistant Secretary for Intelligence and Analysis, the system's major stakeholder. These officials and their staffs are working closely together to manage the development of TFIN, meeting regularly to resolve quickly problems that might affect the cost and schedule of the system. Treasury also is working closely with and receiving direct support and assistance from the Intelligence Community.

This executive level engagement will continue throughout the project and we expect Treasury to complete the system on time and within budget. For example, the TFIN platform was stabilized successfully according to schedule and budget. Treasury and the Intelligence Community have identified TFIN as a critical investment. As such, the TFIN investment is subject to additional reporting requirements beyond the quarterly "Control" review conducted as part of the IT capital planning and investment control processes.

The Department also is implementing specific initiatives to improve IT investment and contract management. These actions are focused on promoting greater accountability for IT management in the bureaus at the project management level, improving the reliability of information being reported by the bureaus, and establishing additional processes through which to assess and validate project performance. To highlight a number of the key initiatives, the Department is: (1) requiring bureau CIOs to certify the qualifications of their project managers and the accuracy of investment reporting; (2) establishing a more rigorous process for justification and reporting is established when bureaus request baseline change requests for their major investments; (3) implementing a program for reviewing the top 50 investments and contracts within the Department; and (4) expanding the independent verification and validation program at the corporate level to assess the accuracy of bureau project and investment reporting.

RESPONSE TO GAO REPORT ON BSA DIRECT

Question. Two days ago, the GAO issued a review of FinCEN's fiscal year 2007 budget request. GAO asserted that "FinCEN has experienced cost, schedule, and performance issues while developing the retrieval and sharing component of the BSA Direct project, which raise questions about the project's future. Therefore, the assumptions made by FinCEN when developing the request for new BSA Direct initiatives may no longer be valid, calling into question the need for this funding." I agree with GAO that the BSA Direct problems raise some serious questions about FinCEN's ability to spend effectively the $12.5 million in additional funding in the budget request. Providing these new funds appears to be "throwing good money after bad."

What is your response? If BSA Direct cannot be salvaged, do you intend to recommend to the Congress that the "Cross-Border Wire Transfer System Initiative" is not feasible and should not be funded for fiscal year 2007?

Answer. The $12.5 million in requested additional funding referenced in the GAO report includes $2.5 million for BSA Direct and $10 million for a separate, but related, Cross-Border Wire Transfer System.

BSA Direct is an overall umbrella project composed of three components: electronic filing (e-filing), secure access, and retrieval and sharing. Of the $2.5 million requested for the BSA Direct umbrella components, $1.3 million is for enhancements to the e-filing component, $0.5 million is to meet the customer base of the secure access system, and $0.7 million is for the retrieval and sharing component.

The electronic filing and the secure access components have been operational for a number of years. Electronic filing reduces the cost to collect BSA data from a range of $0.76–$7.15 per paper form to an average of $0.21 per electronic form submitted. The system is used by more than 300 of the largest financial institutions in the United States. Planned upgrades to the e-file system in fiscal year 2007 will allow: direct input of the BSA filings into the collection system; added features such as reference number assignment, error notification and other correspondence; improved editing of certain types of filing errors; and options for single form filing.

The secure access component serves as a gateway to FinCEN's services, including access to BSA data, analytical products, and online training and support for Federal, State and local law enforcement and regulatory users through secure electronic communication. In fiscal year 2007, FinCEN anticipates a significant increase in the user base for this system, regardless of the status the retrieval and sharing component.

The retrieval and sharing component is being developed by EDS and it alone is the subject of the recent stop work order. This component was designed to provide a data warehouse with 10 years of enhanced BSA data and additional analytical tools.

The fiscal year 2007 budget request of $10 million for a Cross-Border Wire Transfer reporting system allows upfront discussions with Congress in the event the Treasury Secretary approves the collection of cross-border wire transfer data. The authorizing language (Section 6302 of the Intelligence Reform Act of 2004 (S. 2845 Public Law 108–458)) charges FinCEN with two tasks: (1) a feasibility study to be completed as soon as practicable; and (2) the implementation of enabling regulations and a technological system for receiving, storing, analyzing, and disseminating the reports, to be completed by December 2007. This request does not represent an assumption that the Treasury Secretary or Congress will authorize the development of the system, but was submitted out of an abundance of caution and the concern that, if approved, resources would be needed for an implementation that would begin during fiscal year 2007.

The technical alternatives analysis that FinCEN will present in the feasibility study rests on the premise that any conceptual system must be flexible enough to incorporate existing, planned, and future data sources—this includes BSA Direct. FinCEN's study will consider whether and how to create a new system to accommodate the cross-border funds transfer data and other BSA data. The criteria applied by FinCEN in its study of the collection and storage of electronic funds transfer reporting are that the system must:

—integrate multiple data sources, including existing BSA data systems;

—require minimum or no alteration to existing BSA data sources;

—enable the concurrent query of the multiple data systems by the users in a transparent fashion; and

—accommodate the addition of future data sources with minimum or no alteration to the existing or planned BSA data sources.

FinCEN currently is working to complete its feasibility study and anticipates submitting a report to the Secretary of the Treasury in the coming weeks. The feasibility study will outline alternative approaches to developing the system and will provide order of magnitude estimates of the costs involved. These alternatives will address the risks and our concerns if we attempt to implement this system by December 2007, as required in the legislation.

While the study still is underway, a preliminary conclusion is that it is not feasible to complete the development and implementation of the system by December 2007. Due to the complexities of implementing a cross-border wire transfer reporting requirement, which would involve developing and issuing new regulations as well as developing the necessary information technology infrastructure to receive, warehouse and analyze the data received, FinCEN will need the time and resources to develop its project management capabilities before it can undertake this effort. The study will outline the organizational resources that FinCEN will need to manage successfully the development of this project.

CIO AND CFO OVERSIGHT

Question. The Department of the Treasury spends over $2 billion annually on information technology. What percentage of this investment portfolio does the Treasury CIO directly oversee?

Answer. The ASM/CFO and CIO oversee Treasury's entire investment portfolio through formal and informal channels.

Formally, the ASM/CFO meets monthly with the bureau heads to review corporate management issues, including IT management concerns, and agree upon enterprise directions and implementation approaches. As an example, the Department's HSPD–12 initiative, which will meet the requirements of the whole Treasury Department, is being led at this level.

From an IT perspective, the Treasury CIO oversees the entire Treasury Information Technology (IT) investment portfolio. As Chair of Treasury's Technical Investment Review Board (TIRB), which is comprised of bureau CIOs, oversight is provided through a formal Capital Planning and Investment Control (CPIC) process, which we have developed over the last 2 years. The process is multi-layered with both quarterly and annual reporting.

The CPIC process for each fiscal year includes a review of proposed new investments (Pre-Select), decisions regarding the composition of the IT portfolio to be submitted to OMB (Select), quarterly reviews of the portfolio's health (Control), and assessments of steady state investments (Evaluate).

As part of the Control phase of the CPIC process at Treasury, all IT investments are reviewed quarterly to ensure compliance with cost, schedule, security, risk management, and project manager requirements and guidelines. For non-performing investments, where cost, schedule, or performance fails planned targets by 10 percent, the project managers must submit corrective action plans to the CIO. In addition, Treasury has established a formal baseline change request process to oversee all changes to established IT investment baselines. Finally, we now are asking bureau CIOs to certify cost and schedule performance information provided to the TIRB on quarterly basis.

Informally, both the ASM/CFO and the CIO work directly with their bureau counterparts on a day-to-day basis to ensure that the Department's high priority projects succeed. For example, the ASM/CFO, CIO, and the rest of the Treasury management team work directly with bureau stakeholders to implement the President's Management Agenda. Within the E-Government area, this has included the implementation of government-wide payroll, grants, and recruitment systems across Treasury.

Question. How specifically does this oversight occur?

Answer. The Treasury CIO reports directly to the Assistant Secretary for Management and Chief Financial Officer (ASM/CFO).

Question. How does the CFO ensure adequate performance and accountability by the CIO? What specific criteria does the CFO use to measure the performance of the CIO?

Answer. The ASM/CFO ensures performance and accountability by the CIO through a rigorous performance planning process for the CIO's individual performance plan. The CIO's specific performance commitments include: strengthening corporate management for the Department, including addressing control weaknesses and management challenges identified by the OIG and TIGTA, progress in meeting President's Management Agenda requirements for the Expanding E-Gov initiative, and improving enterprise IT operations. The CIO must meet specific performance metrics agreed upon in each of these areas.

IT BUSINESS CASE DOCUMENTATION

Question. The Government Accountability Office (GAO) recently reported that the business case documentation required for major IT investments is unreliable based on a review of five agencies, including the Department of the Treasury. GAO subsequently recommended that agencies improve the reliability of these business cases.

What specific actions is the Treasury CIO taking to improve the accuracy and reliability of the Department's IT business cases?

Answer. Treasury is taking actions to promote greater accountability across the Department's IT management, including steps to improve the reliability of information being reported, and establishing additional processes to assess and validate program performance and reporting.

We are developing, updating, and institutionalizing Treasury-wide policies and guides to improve documentation for major IT investments. For example, over the past year Treasury has issued formal guidance on Treasury Capital Planning and Investment Control Policy, Earned Value Management, Alternatives Analysis, and Baseline Change Request Policy. We are revising overall Treasury IT policy to incorporate minimum life cycle documentation requirements for all major IT projects. This documentation will ensure project managers are developing and maintaining the detailed background records required for effective program management.

In addition, we now are integrating the efforts of the Office of the CIO and the Senior Procurement Executive in overseeing IT projects and establishing an ongoing capability for independent validation and verification of IT investments, as discussed in more detail in response to Senator Bond's first question.

CIO'S OVERSIGHT OF BUREAU PROJECT MANAGEMENT TEAMS AND CIOS

Question. The Treasury CIO told committee staff that his responsibilities include reviewing and certifying the qualifications of every Treasury bureau CIO and their project management teams and that he has the authority to remove a CIO or project management team if they do meet his qualifications.

How often does the CIO review and certify the qualifications of each bureau CIO and project management team? What criteria does he use to determine their qualifications? Has the CIO ever removed a bureau CIO or project management team? If so, please provide specific information on when this occurred and the reasons for the removal.

Answer. To clarify, the Treasury CIO does not have the independent authority to remove a bureau CIO or project team, nor does he certify the qualifications of each bureau CIO.

In January 2006, the Treasury CIO established a policy pursuant to which each bureau CIO must certify to corporate management the qualifications of its project managers for major investments. The policy was based on guidance issued by the Office of Personnel Management and Office of Management and Budget (OMB M–04–19) that requires requesting agency CIOs to ensure that major investments are managed by qualified project managers. This certification is required each time there is a new investment added to the IT portfolio or when there is a change in the project manager for a major project. Treasury Capital Planning and Investment Control guidelines require major IT investment project managers to be qualified in accordance with the Federal CIO Council Workforce and Human Capital for IT Committee's Federal IT Project Manager Guidance Matrix. Project managers must document the knowledge, skills, abilities, and experience that qualify them to manage a major IT investment.

The Treasury CIO is continuing to strengthen project management within the Department. A formal Treasury-wide training program is being established to provide project managers with critical skills and competencies in terms of best practices and earned value management concepts. This program will enhance bureau training initiatives. For example, the program will include a course focused on Treasury-specific policy and procedures to ensure consistent implementation across the Department.

The Treasury CIO also is working with FinCEN and the IRS to address specifically a number of critical investments within those bureaus. Treasury CIO management is participating in the selection of new bureau CIOs, including advising the FinCEN Director on the selection of a new FinCEN CIO, as well as participating in the selection of a new CIO for the Bureau of Engraving and Printing (BEP). Where issues or concerns arise with bureau IT performance, the ASM/CFO and the Treasury CIO directly engage bureau heads.

ROLES AND RESPONSIBILITIES OF THE CIO

Question. Please describe for the record, the roles and responsibilities of the Treasury CIO and specifically how these roles and responsibilities aligned with each requirement specified in the Clinger Cohen Act, E-Gov Act, and Paperwork Reduction Act.

Answer. As outlined by the Government Accountability Office, the Chief Information Officer has 13 major areas of responsibility. The Treasury CIO is responsible for:

—Information Technology/Information Resources Management (IT/IRM) strategic planning [44 U.S.C. 3506(b)(2)]
—IT capital planning and investment management [44 U.S.C. 3506(h) and 40 U.S.C. 11312 & 11313]
—Information security [44 U.S.C. 3506(g) and 3544(a)(3)]
—IT/IRM human capital [44 U.S.C. 3506(b) and 40 U.S.C. 11315(c)]
—Information collection/paperwork reduction [44 U.S.C. 3506(c)]
—Information dissemination [44 U.S.C. 3506(d)]
—Records management [44 U.S.C. 3506(f)]
—Privacy [44 U.S.C. 3506(g)]
—Statistical policy and coordination [44 U.S.C. 3506(e)]
—Information disclosure [44 U.S.C. 3506(g)]
—Enterprise architecture [40 U.S.C. 1401(3)]
—Systems acquisition, development, and integration [44 U.S.C. 3506(h)(5) and 40 U.S.C. 11312]
—E-Government initiatives [44 U.S.C. 3506(h)(3) and the E-Government Act of 2002]

The following table lists a selection of the major requirements within the Clinger-Cohen Act, the E-Gov Act, the Paperwork Reduction Act, and the corresponding role and responsibility of the Treasury CIO.

Requirement	Treasury CIO
Clinger-Cohen Act:	
Provide IT related advice and other assistance to the agency head and other senior management personnel.	Reports to ASM/CFO. Advises and consults with ASM/CFO and other Treasury leadership regarding IT management. Oversees Treasury-wide IT capital planning process.
Develop, maintain, and facilitate implementation of a sound and integrated IT architecture.	Leads the development and implementation of the Treasury Enterprise Architecture.
Promote effective and efficient design and operation of all major information resources management processes.	Chairs the Treasury CIO Council and Treasury Technical Investment Review Board. Promotes policy and process improvements to enhance Departmental IT oversight and management.

Requirement	Treasury CIO
E-Gov Act:	
Participate in the functions of the Federal CIO Council	Participates in the Federal CIO Council and is co-chair of the IT Workforce Committee.
Monitor the implementation of IT standards . . . including common standards for interconnectivity and interoperability, categorization of Government electronic information, and computer system efficiency and security.	Leads E-Government program which incorporates Enterprise Architecture, Enterprise Solutions, and Presidential E-Government functions.
. . . Develop citizen and productivity-related performance measures for use of E-Government and IT in meeting agency objectives, strategic goals, and statutory mandates.	Manages and oversees Treasury performance of E-Government requirements as outlined in the President's Management Agenda and the Department's IT strategic planning process.
. . . Comply with OMB E-Guidance, particular emphasis on agency head communicating guidance to key agency executives.	Oversees compliance and dissemination of OMB guidance and policy regarding IT.
. . . Establish and operate IT training programs.	Assesses and determines the strategy for ensuring adequate IT workforce capabilities; develops and promotes IT training programs for the Department.
Agencies must conduct Privacy Impact Assessments for new IT investments and on-line information collections.	Serves as the Department's Chief Privacy Official; manages the Department's Privacy Impact Assessments and information collection functions.
Requires each agency to develop, document, and implement an agency-wide information security program to provide information security for the information and information systems that support operations and assets (FISMA).	Leads Treasury computer security program, including overall FISMA compliance. In this role, develops, maintains, and facilitates implementation of Departmental IT guidance, including policies, procedures, manuals, and/or guidelines relative to the Department of the Treasury's unclassified computer security programs of all Departmental elements and classified and sensitive but unclassified telecommunications security.
Paperwork Reduction Act:	
Overall responsibility for information resources management.	Leads comprehensive IT management organization comprised of IT capital planning, IT strategic planning, enterprise architecture, E-Government, Cyber Security, Information Management, Telecommunications, and Enterprise Solutions.
Establish an effective information collection and records management program.	Serves as the senior official managing the Department's comprehensive information collection and records management functions. Certifies all Treasury information collection requests and prepares the Department's annual Information Collection budget.

CFIUS

Question. The Committee on Foreign Investment in the United States or CFIUS has become a controversial issue over the past year with the Unocal and DPW deals. Even though both deals ended up collapsing due to political pressure, I believe that there are some lessons learned from these two experiences that need to be addressed.

Senator Shelby has taken the lead in reforming the legislation governing CFIUS. However, I believe the Treasury and the administration could take some steps outside of legislation that could improve the process. For example, I think that the Office of Intelligence and Analysis is uniquely positioned to provide intelligence support for the CFIUS process.

What steps is Treasury taking to avoid some of the mistakes from the past year? In particular, how are you improving communication with the Congress so that we learn about these potentially controversial deals prior to the media learning about them?

Answer. The administration supports reform of the CFIUS process and has already begun to take steps to address the concerns expressed by members of Congress. First, the administration is committed to improving communication with Congress concerning CFIUS matters and shares the view that Congress should receive timely information to help meet its oversight responsibilities. Treasury is now promptly notifying Congress of every review upon its completion, and the administration is working hard to be responsive to Congressional inquiries. The administration also has offered to conduct quarterly briefings for Congress on CFIUS matters.

These quarterly briefings were scheduled to begin before the issues with respect to the DP World transaction became the subject of Congressional and media attention. I look forward to your suggestions on how to foster better communication.

Second, the administration supports a high level of political accountability for CFIUS decisions and is committed to ensuring that senior, Senate-confirmed officials play an integral role in examining every transaction notified to the committee. Improvements to the CFIUS process should also ensure that senior U.S. officials are focused on national security issues. CFIUS agencies are briefing at the highest levels in their respective agencies. On-going, high-level engagement occurs regularly on CFIUS issues at Treasury and other CFIUS agencies.

Third, the administration and the Treasury Department also agree that the committee can carry out its role more effectively by strengthening the role of the intelligence community in the CFIUS process, which is essential in a complex and changing national security environment. The Director of National Intelligence (DNI) has begun to do so by assigning an all-threat assessment responsibility to the National Intelligence Council and ensuring that all relevant intelligence community agencies and activities participate in the development of final intelligence assessments provided to the committee, including Treasury's Office of Intelligence Analysis. The committee recently formalized the role of the Office of the DNI, which plays a key role in all CFIUS reviews and investigations by participating in CFIUS meetings, examining every transaction notified to the committee, and providing broad and comprehensive threat assessments. The DNI already contributed greatly to the CFIUS process through reports by the Intelligence Community Acquisition Risk Center concerning transactions notified to the committee, but formalizing its place in the process—and strengthening the threat assessments provided to the committee—represent an enhancement of the intelligence community's role. The DNI does not vote on CFIUS matters and should not, because the role of the DNI is to provide intelligence support and not to make policy judgments based upon that intelligence.

IRS BSM

Question. The budget request proposes a major increase in funding for BSA Direct of some $12.5 million but proposes a major cut to the IRS's Business Systems Modernization program of some $30 million. The GAO just issued a report noting the problems with BSA Direct and the Treasury OIG just issued a report praising the IRS's management of its IT contractors.

Given what we now know about the problems at FinCEN and BSA Direct and the improvement at the IRS, do you agree that the budget request for FinCEN is a case of rewarding bad behavior while the request for IRS is a case of punishing good behavior? How do you reconcile these contradictions? Are you still committed to BSM?

Answer. The $12.5 million in requested additional funding for BSA Direct referenced in the GAO report includes $2.5 million for BSA Direct and $10 million for a separate, but related, Cross-Border Wire Transfer System.

Of the $2.5 million requested for BSA Direct, $1.8 million is for enhancements to meet the needs of the expanding user base for the e-filing and secure access components, both of which have been operational and successful for a number of years, with the remaining $0.7 million for continued development of the retrieval and sharing component.

The problems noted in GAO's report have come to light and are being addressed. FinCEN Director Werner proactively has initiated an assessment of the BSA Direct retrieval and sharing component, presently scheduled to be completed in July, to determine the extent of the problems with the project and the next steps that need to be taken with regard to BSA Direct. The Office of the CIO is working closely with FinCEN on this effort.

The $10 million requested in fiscal year 2007 for the Cross-Border Wire Transfer System is submitted in accordance with Section 6302 of the Intelligence Reform Act of 2004 (S. 2845, Public Law 108–458), which charges FinCEN with two tasks: (1) a feasibility study to be completed as soon as practicable; and (2) the implementation of enabling regulations and a technological system for receiving, storing, analyzing, and disseminating the reports, to be completed by December 2007. FinCEN will submit a report on the results of the feasibility study to the Secretary in the coming weeks, and has included this funding request to allow development of the system to begin in 2007, should the Secretary recommend and Congress authorize doing so.

The administration continues to be committed to the IRS Business Systems Modernization program. We are pleased with the Treasury Inspector General for Tax Administration's recognition of the progress that the IRS BSM program has made over the past 2 years to improve its performance on delivering projects and releases on time and on budget, while meeting or exceeding scope expectations. In fiscal year 2006 and continuing into fiscal year 2007, BSM is revising its modernization strategy to emphasize the incremental release of projects to deliver business value sooner and at a lower risk. The President's budget request for BSM for fiscal year 2007 aligns with this revised strategy and provides the level of resources the administration believes necessary to deliver the fiscal year 2007 BSM program requirements.

DYNAMIC ANALYSIS OFFICE OF TAX POLICY

Question. The budget request proposes some $500,000 to create a new "dynamic analysis office" within the Treasury.

What types of analysis would this office conduct that is not being conducted at Treasury or other Federal agencies? What is the long-term plan for this office in terms of funding and staffing?

Answer. The administration has very limited capabilities to conduct dynamic analyses of tax policy changes. The budget request would create a new Dynamic Analysis Division within the Treasury Department's Office of Tax Policy to conduct dynamic analyses of major tax policy changes. The dynamic analyses would focus on the macroeconomic effects of tax policy changes. The new Division would not, at least initially, conduct dynamic scoring of tax policy changes, which would take dynamic analysis one step further and estimate how the macroeconomic changes affect government revenues.

While the fiscal year 2007 budget request for $513,000 is for the upcoming fiscal year, Assistant Secretary Pack sent a letter on June 8, 2006 to Chairman Bond and Ranking Member Murray proposing that this initiative be accelerated into this fiscal year. The acceleration of this new Division into fiscal year 2006 would be funded within the existing appropriation for this fiscal year. The request for fiscal year 2007 would remain unchanged, funding three full-time positions for 1 full year rather than the estimated six positions for 6 months.

TREASURY COMMUNICATIONS ENTERPRISE (TCE)

Question. Have the deficient items identified in the TCE bid protest been addressed and corrected? In particular, what measures are being taken to ensure the reasonableness of the price evaluation?

Is the Treasury's office of the Chief Information Officer properly structured and staffed to provide adequate oversight to major systems acquisitions such as TCE?

Answer. The issues raised on the TCE bid protest have been addressed fully. In October 2005, Treasury released an amended Request for Proposal, which clarified what is required of vendor price proposals. Furthermore, in evaluating vendor proposals, the evaluation team is working in close concert with both Internal Revenue Service (IRS) legal counsel as well as Treasury's Office of the General Counsel (OGC) to ensure that they are following all appropriate rules and regulations.

The Office of the Chief Information Officer (OCIO) is qualified fully to provide effective oversight to major acquisitions such as TCE. The TCE procurement is being executed through the IRS Office of Procurement, which has extensive experience in conducting acquisitions the size and scope of TCE. The OCIO senior management works in close concert with IRS Procurement, IRS legal counsel, Treasury OGC, and Treasury senior management to provide adequate oversight and management of the acquisition. This collective leadership team meets weekly to monitor the status of the TCE procurement.

The ASM/CFO also established a focused leadership group to provide advice and recommendations on the business case documentation and on the strategy for TCE. This group includes the Treasury CIO, Senior Procurement Executive, Deputy Chief Financial Officer, Assistant General Counsel, and ASM/CFO senior advisors.

IRS OVERSIGHT BOARD NOMINATIONS

Question. There are currently three vacancies on the IRS Oversight Board. I fully support Chairman Wagner and believe that these vacancies must be filled quickly to ensure that the Board has a quorum to meet and conduct its legislatively-mandated oversight responsibilities.

Has the administration identified individuals to fill these vacancies? When can we expect these nominations to be formally submitted to the Senate?

Answer. On May 1, 2006, the President nominated 4 outstanding individuals to fill the vacant or expired seats on the IRS Oversight Board. They are:

—Paul Cherecwich, Jr., of Utah, to be a Member of the Internal Revenue Service Oversight Board for a term expiring September 14, 2009, vice Charles L. Kolbe, term expired;

—Donald V. Hammond, of Virginia, to be a Member of the Internal Revenue Service Oversight Board for a term expiring September 21, 2010, vice Robert M. Tobias, term expired;
—Catherine G. West, of the District of Columbia, to be a Member of the Internal Revenue Service Oversight Board for a term expiring September 14, 2008, vice Karen Hastie Williams, term expired; and
—Deborah L. Wince-Smith, of Virginia, to be a Member of the Internal Revenue Service Oversight Board for a term expiring September 14, 2010, vice Larry L. Levitan, term expired.

STANDING UP TFI

Question. During the early days of TFI, there were concerns about possible redundancy and OIA acting as an operational vice analytical unit.

Please explain how you have addressed these concerns and explain the differences today between FinCEN, OFAC, TFFC, OIA, etc.

Answer. The four components of TFI—the Financial Crimes Enforcement Network (FinCEN), the Office of Foreign Assets Control (OFAC), the Office of Intelligence and Analysis (OIA), and the Office of Terrorist Financing and Financial Crime (TFFC)—play distinct but complementary roles in fulfilling the overall mission of safeguarding the financial system from criminal abuse and applying measures to combat key national security threats, including terrorism, the proliferation of weapons of mass destruction, and money laundering. FinCEN is the U.S. Financial Intelligence Unit (FIU). Its mission is to administer and enforce the Bank Secrecy Act (BSA) and to receive, analyze, and disseminate, both domestically and internationally, financial intelligence, including suspicious activity reports, to detect criminal activity so that it can be prevented and prosecuted criminal activity. OFAC administers and enforces economic and trade sanctions, which are based on U.S. foreign policy and national security goals against targeted foreign countries, terrorists, international narcotics traffickers, and those engaged in activities related to the proliferation of weapons of mass destruction. In putting together packages for designation under Treasury's various sanctions authorities, OFAC engages in investigations, analysis, and research involving intelligence, law enforcement, and open source information and, as appropriate, extensive field work. As the policy development and outreach office for TFI, TFFC works with the Treasury Department, the U.S. Government interagency community, and its counterparts in Finance Ministries around the world, as well as directly with the private sector to develop and advance policy and specific actions to combat terrorist financing, WMD proliferation, money laundering, and other criminal activities. TFFC leads and coordinates U.S. representation at international bodies dedicated to fighting terrorist financing and financial crime such as the Financial Action Task Force (FATF) and increases our multilateral and bilateral efforts in this field. TFFC also promotes the development of effective targeted financial sanction regimes and the use of other targeted financial authorities through the G7, G20, FATF, United Nations, European Union, and bilaterally with countries of strategic importance.

OIA is Treasury's in-house intelligence analytic unit, focusing on counterterrorism, counterproliferation, and other national security threats. OIA's mission is to support the formulation of policy and execution of Treasury authorities by providing: (1) expert analysis and intelligence production on networks that provide financial and other support to terrorist groups, proliferators, and other key national security threats; and (2) timely, accurate and focused intelligence support on the full range of economic, political, and security issues. We envision that as OIA evolves, it will be widely viewed as a center of analytic expertise on such networks. The TFI components' counterterrorism efforts are closely coordinated, both at daily senior staff meetings, and perhaps even more importantly, at weekly targeting meetings. The targeting meetings, which are led by TFI's Under Secretary, include senior officials from all of the TFI components. At these sessions, based on a review of the relevant intelligence, potential targets are presented and discussed. The participants assess the full range of potential Treasury actions, including designation, and decide on follow up direction and assignments. OIA will continue to host and participate in these sessions in the future, which have proved to be an effective mechanism for translating intelligence information into policy action.

COORDINATION WITH OTHER AGENCIES

Question. With the establishment of TFI, I am curious to know how this new office is coordinating its intelligence activities with other Federal agencies and the Office of the Director of National Intelligence.

How are you working and communicating with the intelligence community, especially with the Office of the Director of National Intelligence and other key intelligence agencies such as the Department of Homeland Security, the Department of Justice and the Federal Bureau of Investigation to make sure that efforts are not being duplicated?

Answer. OIA is the primary Treasury office responsible for ensuring that the Department is fully integrated with the Intelligence Community (IC). Our recently completed report on OIA's fiscal year 2006–2008 strategic direction makes clear that enhancing Treasury's integration into the IC has been—and will remain—one of OIA's top priorities. OIA has been working closely with the Office of the Director of National Intelligence since it was created. The DNI has been very supportive of OIA, and has been of great assistance to OIA at a number of key junctures. OIA has aligned its priorities with those set forth by the Director of National Intelligence in the National Intelligence Strategy. OIA's goals and direction align with key DNI objectives in a number of areas, including: strengthening analysis, WMD proliferation, keeping policymakers informed, and building an integrated intelligence capability. During its short tenure, OIA has already made great strides in integrating TFI specifically, and Treasury more generally, into the IC, and it will continue to build on these efforts. As a result of its improved integration into the IC, OIA analysts are now participating in the drafting and coordination of a variety of IC analytic products. These include: National Intelligence Estimates, CIA studies, Senior Executive Intelligence Briefs and Presidential Daily Briefs. OIA has also initiated both formal and informal analytic exchanges with its intelligence and law enforcement partners. The FBI and OIA, for example, are now working on a joint analytic project, which they intend to complete this year. The additional personnel OIA is now hiring—and those it is requesting in fiscal year 2007—will allow OIA to further increase its contributions to IC products, and to produce additional finished intelligence pieces for dissemination to the IC.

OFAC DESIGNATIONS

Question. Pursuant to the Treasury's new designation authority to sanction proliferators of weapons of mass destruction, please provide the committee an explanation of the Office of Foreign Assets Control's designation process.

Answer. OFAC follows a three-step process in pursuing designations, which consists of: identifying the target; constructing and de-conflicting an evidentiary package; and publicly announcing the designation. Like its colleagues in law enforcement and the intelligence community, OFAC follows leads. If the initial investigation of a lead shows promise, then OFAC investigators move into the second stage of the designation process—the evidentiary process.

In the WMD proliferation context, as well as in OFAC's other programs, such as the successful counter-narcotics programs, OFAC engages in investigation and research using intelligence, law enforcement and open source information and, as appropriate, field work. Once this evidence is collected, OFAC's investigators draft an evidentiary document analyzing and summarizing the information acquired through their research. This "summary" document describes how the information provides OFAC reason to believe that the target meets the specific criteria for designation. After an evidentiary package has been thoroughly reviewed within OFAC, it is reviewed by Treasury's attorneys to ensure that OFAC has met its evidentiary threshold, and by the Department of Justice's Civil Division, which represents OFAC in court if its designations are challenged.

The next formal stage of OFAC's process involves interagency coordination. In most cases, OFAC engages informally with colleagues in a variety of agencies throughout the investigation process. In fact, initial targets are suggested through an interagency working group, and closely coordinated and vetted within appropriate agencies in the early stages of development. OFAC also works closely with colleagues in OIA and from elsewhere in the Intelligence Community. Nonetheless, OFAC goes through a more formal coordination phase designed to de-conflict its proposed designations with the operational and policy interests of other agencies and to ensure that the targets are consistent with and further the strategic national security and foreign policy goals of the United States. Executive Order 13382 specifically directs that designations by Treasury or State be undertaken in consultation with one another, as well as in consultation with Justice and other relevant agencies.

Once this thorough interagency review process has been completed, the final evidentiary package is presented for signature by the Director of OFAC. At the same time that the package is provided to the Director of OFAC for consideration, two other important processes are in motion. First, OFAC's team of compliance officers and information technology professionals work closely with OFAC investigators to prepare the information about a target for possible public dissemination through OFAC's List of Specially Designated Nationals and Blocked Persons (SDN list). The SDN list is used by thousands of companies around the country and around the world to screen real-time transactions and accounts for the possible involvement of an OFAC target. The second process occurs if and when OFAC investigators become aware that a designation target has a presence in the United States. At that point, OFAC investigators from both the Designation Investigations Division and the Enforcement Division prepare an operation to block any property that can be identified.

BIGGEST CHALLENGES

Question. What are the three most immediate challenges for TFI?

Answer. The three most immediate challenges for TFI are: (1) the need for additional resources to more aggressively pursue core objectives, including combating the financial underpinnings of weapons of mass destruction (WMD) proliferation; (2) leveraging our authorities most effectively to deal with terrorist-sponsoring regimes Iran and Syria, and working in partnership with governments and the private sector to do so; and (3) building the information technology systems necessary to effectively and efficiently carry out our mission.

First, with respect to resources, Treasury has continued—with the support of your subcommittee—to build the new Office of Terrorism and Financial Intelligence. As TFI has grown in size, the demand for our expertise and capabilities has expanded as well. The President's budget for fiscal year 2007 includes funding for the component offices of TFI to meet this demand. For example, it provides OFAC with additional positions to implement and administer the WMD sanctions program, as well as to monitor and update existing terrorism designations. It provides funding for OIA to continue its efforts to build Treasury's intelligence capabilities by improving its key infrastructure and adding to its analytic breadth and expertise. And it provides FinCEN with additional resources to streamline data processing and enhance its e-filing capabilities to increase the ease of compliance with regulations and improve its abilities to track users' needs.

Second, TFI continues to be challenged to leverage its capabilities to deal with terrorist-sponsoring regimes Iran and Syria. TFI has at its disposal a broad range of tools to pressure obstructionist regimes and freeze the assets of terrorists, proliferators, and other wrongdoers. We have regulatory authorities to help banks and other institutions implement systems to detect and halt corrupt money flows. And, we continue to work with other governments and international institutions to achieve collective action against threats and to take critical steps to stem the flow of illicit finances. The combination of these various measures contributes to the U.S. Government's overall ability to deter and defend against key threats. The dynamic situation in the Middle East requires close and sustained attention and careful coordination across the interagency and the international community to ensure that these capabilities, or, in some cases, the threat to take certain measures, are exercised most efficiently and effectively.

Finally, TFI continues to be challenged to meet its internal information technology requirements, and the fiscal year 2007 budget request, if approved, will move us toward being able to do so. For example, Treasury's Foreign Intelligence Network (TFIN), the sole information technology system in the Department authorized for top secret information has not been modified or upgraded to keep pace with the changes in intelligence, user, or technological requirements. TFIN lacks appropriate analytical tools and a robust disaster recovery capability. The fiscal year 2007 budget provides funding to upgrade this critical system. Additionally, OFAC has a demonstrated need for an Enterprise Content Management (ECM) system to provide electronic document, records and case management functions. The fiscal year 2007 budget request of $627,000 will assist OFAC and Treasury's Office of the Chief Information Officer (OCIO) in continuing their joint efforts to develop a pilot approach to an ECM system within the context of a government-wide/department-wide enterprise solution.

QUESTIONS SUBMITTED BY SENATOR THAD COCHRAN

Question. The New Markets Tax Credit (NMTC) Program relies upon the decennial census to qualify areas as eligible for NMTC financing. Employing 2000 Census Bureau data, only a few census tracts along Mississippi's devastated coast line qualify as "Low-Income Communities". A re-measurement, not contemplated in the current statute would likely qualify them under the program's guidelines. In addition, I understand that Secretary Snow has the discretion under the Job Creation Act of 2004 to designate "targeted populations" as a group to be treated as a "Low-Income Community".

Will the Community Development Financial Institutions Fund, with the Secretary of the Treasury, designate the census tracts or targeted population of the most heavily damaged areas as "Low-Income Communities" by conducting either a re-measurement of census tracts in the Katrina-affected areas or employing the targeted population discretionary tool which currently exists?

Answer. The CDFI Fund, the Internal Revenue Service (IRS) and NMTC Program participants rely upon Census Bureau data to determine whether projects are located in NMTC-qualifying Low-Income Communities (LICs). To our knowledge, the Census Bureau has not announced plans to re-assess the areas damaged by Hurricane Katrina and provide updated census information. Absent new data from the Census Bureau, the CDFI Fund does not have any means available to provide a remeasurement of these areas.

Although new census data won't be available, the Secretary may designate "Targeted Populations" as LICs. Pursuant to The American Jobs Creation Act of 2004, Targeted Populations may include low-income persons as well as other persons that "otherwise lack adequate access to loans or equity investments" (i.e., persons who have historically been denied access to loans, equity investments or financial services due to factors that are unrelated to their investment or credit worthiness such as gender, race, ethnicity, national origin and creed).

The CDFI Fund, in conjunction with the IRS, is developing guidance to implement this new Targeted Populations provision. As part of this process, we are considering whether and under what circumstances residents of the Hurricane Katrina Gulf Opportunity (GO) Zone could potentially be included as a Targeted Population. We hope to publish guidance on this matter before the end of June 2006.

Question. Of the $8 billion of NMTC Allocations made to date, a very small amount of NMTC allocation ($15 million of the total $8 billion) has been made to Community Development Entities ("CDEs") based in Mississippi, and little other NMTC allocation has made its way into the State from allocatees based outside Mississippi. The residents of Mississippi suffered much devastation from the Katrina Hurricane.

Instead of allocating $1 billion of NMTCs to the entire GO Zone, will the Community Development Financial Institution Fund (CDFI) and Secretary of the Treasury consider designating a pro-rata (based on pro rata storm population in the Katrina affected areas) amount to be spent in each State?

Answer. The NMTC, unlike other credits such as the Low-Income Housing Tax Credit, is a non-apportioned Federal tax credit. That is to say, NMTCs are not apportioned to States on a pro-rata basis. Rather, they are awarded to intermediary entities known as Community Development Entities (CDEs) throughout the country that apply to the CDFI Fund under annual competitive allocation rounds. While the GO Zone Act of 2005 provided an additional allocation of $1 billion for use in the recovery and redevelopment of the Hurricane Katrina GO Zone, it did not specifically authorize or otherwise instruct the CDFI Fund to convert the allocation authority into an apportioned Federal tax credit to be issued by the affected States.

Question. Six hundred million dollars of the supplemental $1 billion allocation created for the benefit of the GO Zone is being allocated under rules which do not open the opportunity for interested groups in Mississippi to participate in its redevelopment through this incentive. In March 2006, some of my constituents learned that to be considered for the $600 million, an entity would have had to have submitted an application for NMTCs in September 2005, 3 months before the $1 billion supplemental was signed into law. To submit an application for NMTCs, an entity would have had to file to become a CDE 1 week before Hurricane Katrina landed onshore. This implementation of the program disadvantaged participants inside the State of Mississippi who would like to be involved in its rebuilding.

For Mississippi CDEs that did apply for NMTCs in this round, will the CDFI Fund and Secretary of the Treasury work with applicants to make revisions necessary to their applications to ensure that they receive minimum threshold scores, qualifying them for allocations?

How will the CDFI Fund and Secretary of the Treasury open this process to those in Mississippi who would like to compete for the $600 million of NMTCs? Will it hold a special competition (either completely open or with limitations) for the $600 million? Will the $600 million be allocated pro rata among the governors of the three States for State-created CDEs, allocations of which could then be allocated to other CDEs in the State?

Answer. The process for allocating the $600 million of GO Zone allocation authority through the 2006 allocation round was described in a revised Notice of Allocation

Availability (NOAA) published on March 10, 2006. The Treasury Department has no plans to amend these procedures.

The GO Zone Act of 2005 made available $1 billion of additional allocation authority to be allocated as follows: $300 million through the 2005 NMTC allocation authority; $300 million through the 2006 allocation authority; and $400 million through the 2007 allocation authority. As you are aware, this legislation was enacted in late December 2005—approximately 6 months after the 2005 NMTC award decisions had been finalized. The $300 million of additional 2005 GO Zone allocation authority was therefore added to the $300 million of 2006 GO Zone allocation authority, thus enabling the CDFI Fund to allocate up to $600 million of allocation authority through the 2006 allocation round. This is an addition to the $3.5 billion of allocation authority that was already available through that round.

When the GO Zone Act was passed in December 2005, the application deadline for the 2006 round of NMTC allocation authority had expired. The Treasury Department decided not to re-open the round to accept additional applications, as this would likely lead to delays of 6 months or more in making available the allocation authority to the GO Zone applicants. The Treasury Department felt that it was critical that these resources be made available as soon as possible in the affected areas.

In determining not to accept additional applications, the Treasury Department took into account the make-up of the 2006 round applicant pool. The CDFI Fund received a total of 254 applications, including 65 that were submitted by organizations that indicated their intent to serve the GO Zone as part of their principal markets. This included 16 applicants (requesting a total of $2.59 billion in allocation authority) that were headquartered in the GO Zone, 13 of which had received deadline extensions (some as long as 12 weeks) in the wake of Hurricane Katrina. Based on this data, the Treasury Department was confident that there would be a high number of qualified CDEs headquartered both inside and outside of the GO Zone that would be able to make effective use of the credits.

Finally, we believe the GO Zone legislation addresses your concern that local entities be involved in the redevelopment process. The legislation requires that, in making the GO Zone allocation determinations, CDEs must demonstrate that they have a significant mission of recovery and redevelopment in the GO Zone. The CDFI Fund will consider each applicant's track record of redevelopment in the GO Zone, as well as the extent to which it has resources (physical resources as well as personnel) deployed in the GO Zone and/or is partnering with local entities in the GO Zone.

Question. There is some evidence that a preponderance of NMTC financing, both loans and investments, have been directed to real estate businesses. There also seems to be less NMTC financing being directed to small business lending and venture capital investing. Both venture capital and small business lending would be helped if regulations governing the reinvestments of capital could be made more flexible—both in terms of the substantially all threshold for reinvestment and in terms of the eligible uses of reinvested funds in terms of geographic area and investments activity.

What regulatory changes are you contemplating to ensure more use of the NMTC for small business and venture capital projects?

Answer. The CDFI Fund has collected NMTC transaction level data on transactions completed in 2004 through its Community Investment Impact System. Data on 2005 transactions is due June 30, 2006. The 2004 data indicates that of the 280 transactions reported in 2004, 28 percent were business investments and 72 percent were real estate transactions.

The Treasury Department is aware of the desire to see more use of the NMTC Program to support small business lending and venture fund investing. The NMTC statute does not prioritize allocations among the various types of potential uses such as real estate development, business loans or venture investing. However, the NMTC statute does require that substantially all of a qualified equity investment be used to make qualified low-income community investments throughout a 7-year period. We are told that investors prefer the certainty of real estate transactions both as a matter of mitigating economic risk and as a matter of compliance with the 7-year investment period rule.

The CDFI Fund will award a contract to evaluate the use of the NMTC Program, including evaluating its use in financing small business and venture fund investments. One element of the evaluation will include an assessment of investor behavior and preferences in the NMTC Program. The Fund expects to have information late this fall or early in 2007. The CDFI Fund anticipates that subsequent to the issuance of this assessment and the statutorily-mandated GAO study due in 2007, the CDFI Fund will work collaboratively with the Office of Tax Policy and the Internal Revenue Service to study appropriate statutory and/or regulatory improvements to the program, if the program is extended.

Question. It is my understanding that urban areas claim approximately two-thirds focus of the NMTC program's resources, in terms of percentage of allocations and actual funds. The one-quarter share of funds first devoted to rural geographies has shifted to suburban areas. Only one-sixth of resources were targeted to rural communities in the last round.

What can you do to ensure that more of the credit reaches rural communities?

Answer. At the time of application submission, applicants are asked to estimate the percentage of activities that will be undertaken in rural areas. Through three allocation rounds, awardees have estimated that approximately 17 percent of their transactions would be undertaken in rural areas, which is consistent with the percentage of the U.S. population that resides in rural areas (17.4 percent, according to 2000 census data).

In addition, the CDFI Fund has completed an analysis of transactions undertaken by awardees as of fiscal year end 2004, and has determined that approximately 19 percent of the $1.3 billion of investments closed that year were undertaken in rural communities. The CDFI Fund has also analyzed the application trends in the 2005 application round, and determined that there is no selection bias against applications submitted by organizations serving rural areas. In other words, CDEs focusing activities primarily in rural markets received awards in a rate consistent with their application rate.

That being said, the CDFI Fund will continue its efforts to provide more outreach in markets that do not appear to be benefiting from NMTC investments.

Question. I have constituents who are concerned about the use of credit to subsidize transactions that would otherwise move forward without the credit. NMTC should drive capital into new deals not feasible in conventional markets.

What is being done to make sure that the NMTC is being used to subsidize transactions that would not occur without the credit?

Answer. Historically we know that low-income communities have not been able to access capital on the terms needed to finance businesses and real estate developments. Based upon preliminary transaction data provided by allocatees through the CDFI Fund's Community Investment Impact System (CIIS), which is required as a matter of compliance with the Fund's allocation agreement, as well as anecdotal accounts of the use of the credits, the CDFI Fund believes that the NMTCs have been very effective at bringing capital into transactions that would not otherwise be financed.

To obtain an allocation through what has been a very competitive application process in each of the four rounds conducted to-date, the CDFI Fund gives each applicant the opportunity to commit that it will go above and beyond minimal program requirements. For instance, while all allocatees are required to invest substantially all (generally 85 percent) of the qualified equity investments they receive in low-income communities, most applicants have committed to invest NMTC proceeds in areas characterized by severe economic distress (i.e., areas that have significantly higher poverty rates and lower median family incomes than those minimally required under the NMTC Program; areas that have unemployment rates at least 1.5 times the national average; and/or areas that have been designated for economic development through other governmental programs such as Brownfields, Empowerment Zones and Renewal Communities). Of the 41 allocatees that received awards under the 2005 round, 37 indicated that at least 75 percent of their activities will be provided in these areas of severe economic distress, and 21 indicated that 100 percent of their activities will be provided in such areas. The CDFI Fund will require these allocatees, through their allocation agreements, to meet the benchmarks identified in their applications.

Similarly, the CDFI Fund requires its allocatees to provide products with non-conventional features, even though this would not otherwise be required under the program regulations. Such features include, among other things: equity and equity-equivalent terms and conditions; subordinated debt; below market interest rates; and reduced origination fees. In the 2005 allocation round, all 41 allocatees indicated that at least 75 percent of their loans and investments will have particularly flexible or non-traditional features, and 36 of the 41 allocatees indicated that 100 percent of their loans and investments will have particularly flexible or non-traditional features. Thus, the CDFI Fund ensures that the commitments made in the applications will be kept through the allocation agreements.

We believe these requirements help ensure that the investments being made through the NMTC Program are not in the locations or not on the terms and conditions that the marketplace would normally finance. Additionally, the CDFI Fund is about to engage an independent contractor in a long-term, longitudinal evaluation of the NMTC Program. This evaluation will enable the CDFI Fund and Congress to more fully understand and measure the benefits of the tax credit in low-income communities throughout the country.

Question. The Internal Revenue Service (IRS) regulations implementing the New Markets Tax Credit Program place an onerous regulatory burden on allocatees seeking to use their credits to make investments in CDEs or intermediary activities. Specifically, the regulations require the "direct tracing" of tax credit investor proceeds to specific activities or projects; thus, making it difficult to use as loan or equity capital. Most CDEs that are CDFIs are small and already have significant reporting burdens required to maintain their CDE/CDFI certification status. The reporting burden has a disproportionate impact on rural or other communities that are typically served only by small- or medium-sized CDE/CDFIs and has effectively locked them out of accessing these important Federal resources.

What can the Treasury Department or IRS do to eliminate the direct tracing requirements for allocatees seeking to use their credits to make investments in Community Development Entities (CDEs) that are also CDFIs?

Answer. The NMTC statute requires that for an equity investment to be qualified, substantially all of the cash must be used to make qualified low-income community investments throughout a 7-year period. The tracing requirements are necessary to ensure that the statutory requirements are met. Recognizing the difficulty in such tracing, a safe harbor is provided for determining the use of the cash.

QUESTIONS SUBMITTED BY SENATOR PATTY MURRAY

TREASURY COMMUNICATIONS ENTERPRISE (TCE)

Question. In 2004, the Treasury Department launched the procurement of a new Treasury Communications Enterprise—or "TCE". TCE was envisioned to allow data, voice, and video technologies in a single network. Your budget told us that it would be worth $10 billion over a 10-year period.

Every aspect of this procurement appears to have been botched by your Department. You awarded the contract to AT&T but shortly thereafter, several unsuccessful bidders won a bid protest before the GAO because your Department altered the basis upon which the bidders prepared their proposals. Your Department was also found to have understated the cost of the winning bid and failed to fairly evaluate the prices of the competing bids.

In response to GAO's decision, you decided to terminate the contract with AT&T and acquire the services through the GSA. Then, late last year, you reversed course again and announced that you would proceed with your own independent procurement. For some reason, having failed once with an independent procurement, you are now going forward with one even though the GSA is in the midst of its own similar procurement for much of the rest of the government. The GSA maintains that all the services you will need will be provided by their system.

When the Treasury Inspector General looked into this program, he found that poor planning and execution of TCE resulted in numerous delays and increased costs. They also found little evidence of adequate senior management oversight of the project.

Mr. Secretary, what explains all the problems that have plagued this program? Why did you reverse course and decide not to proceed with the GSA procurement? What critical capabilities will your system have that the GSA's system will not?

Answer. The contract award for TCE in December 2004 was protested by the losing bidders. Due to the considerable interest in Treasury's ability to use GSA's Networx program, Treasury and GSA entered into a Memorandum of Understanding (MOU) on December 2, 2004. The MOU stated that Treasury would evaluate the GSA's Networx services 3 years after the award of TCE. The losing bidders argued that this MOU materially altered the basis under which option years would be awarded. The protest was upheld by GAO in March 2005. Treasury did not intend nor did it believe the MOU impacted the procurement, as the Department already intended to seek the best value for the government by evaluating other service for the option years. Consistent with effective IT management and procurement principles, the goal was to evaluate the TCE contract and determine the most cost-effective long term strategy.

Subsequent to the sustained protest, Treasury conducted a second Acquisition Alternatives Analysis in consultation and cooperation with GSA. Treasury once again considered government-wide contract alternatives and scrutinized carefully these options in light of the protest decision. Treasury and GSA worked to refine the alternatives analysis and reach consensus on the best approach to move forward with the replacement for the expiring contract, Treasury Communications System (TCS). The Treasury and GSA post-protest analysis confirmed Treasury's conclusions of the initial analysis. Based on the estimated schedule for the award of Networx and a review of other GSA options to serve as a bridge between TCS and Networx, the finding was that a Treasury-led full and open competition was the most reasonable decision based on contract structure, cost, and most importantly, transition risk.

Existing GSA contracting vehicles could not accommodate easily the managed service requirements for TCE. To support the managed services model, the GSA contracts would have required modifications, which would have increased time, cost, and complexity to support a managed services solution. The near-term expiration of GSA contracting vehicles would have required an additional competition and a second transition once the new contracting vehicle—GSA's planned Networx program—was awarded. Two transitions within a 2-year timeframe represented unacceptable risks of potential service interruptions and threat to Treasury's ability to fulfill its mission responsibilities. Using a GSA contract vehicle also was a significantly more expensive option due to GSA overhead and the costs associated with waiting for Networx.

Concurrently, the Office of the Inspector General completed an audit of the TCE procurement, which found that planning documentation was not cohesive or comprehensive. While the project had the full support of Treasury senior officials, who were briefed regularly on TCE, we recognize that the supporting documentation did not reflect consistently and clearly senior management decisions to the extent necessary for management review and audit. Treasury subsequently has undertaken specific actions to address the audit findings.

Question. Why hasn't your CIO done a better job of managing this project and all the other troubled IT projects in your agency?

Answer. Treasury is taking the necessary steps to address the Inspector General's (IG's) findings and recommendations. Upon receipt of the report, the ASM/CFO directed a team of IT, procurement, and legal executives to develop corrective actions that address all of the IG's findings and recommendations. Specifically, the Department has greatly improved the TCE documentation, and also is strengthening documentation requirements for all major Treasury IT projects.

Department-wide efforts are underway to strengthen IT investment oversight for the Treasury IT portfolio as a whole. Over the past 2 years, the Treasury CIO has been leading efforts to mature the IT capital planning process within the Department. Treasury has made demonstrated progress in: (1) formalizing and standardizing the quarterly review process of the health of the IT portfolio, (2) establishing Department-wide Capital Planning and Investment Control (CPIC) process and Contract Earned Value Management policy guidance, and (3) instituting the use of a common investment portfolio management tool.

Other examples of how Treasury is providing effective corporate oversight and leadership of IT management include:

—The majority of Treasury IT projects are succeeding, including most of the systems mentioned at the April 6, 2006, Senate Appropriations Committee hearing. For example, Treasury's HR Connect system was recently named a Federal Human Resources Management Line of Business (HR LoB) Shared Service Center (SSC) by the Office of Personnel Management and the Office of Management and Budget (OMB). The HR LoB is one of the Presidential E-Government lines of business, which designates agency centers of excellence to provide government-wide servicing for core functions. Currently, the Department's HR Connect program services Treasury, the Department of Housing and Urban Development (HUD) and components of the Departments of Justice and Homeland Security.

—Treasury migrated HUD to HR Connect last year on time and within budget, adding an estimated 10,000 employees to the system. Both HUD and industry recognized Treasury for the cost-effective and smooth transition. Treasury clearly has addressed its past problems with the HR Connect program and continues to drive towards enhanced performance and operating efficiency.

—Treasury has made significant improvement across the core IT management areas measured under the Expanding E-Government (E-Gov) Initiative of the President's Management Agenda (PMA). For the first time since the establishment of the PMA in 2002, Treasury improved its overall E-Gov status from Red to Yellow in the first quarter of fiscal year 2006. The improved PMA score was based on Treasury's meeting key requirements and performance metrics. These key requirements and performance metrics included developing Treasury-wide IT capital planning policy, maturing the Departmental Enterprise Architecture, and meeting quarterly milestones for Presidential E-Gov Initiative implementation. This was accomplished in large measure by the efforts of all bureaus through the Treasury Chief Information Officers' Council and its sub-councils.

—The Alcohol and Tobacco Tax and Trade Bureau's (TTB) recent successful migration from the Bureau of Alcohol, Tobacco and Firearms and Explosives (ATF) infrastructure is an example of proper oversight and assistance between the Department and a Treasury bureau. When ATF was divided into two organizations in 2003 (ATF became part of the Department of Justice while TTB remained a Treasury bureau), all IT resources remained with ATF. These IT resources included 100 percent of all capital assets, infrastructure, IT support personnel, and resources to continue development of core business applications. Treasury's senior management team worked closely with TTB bureau executives in developing and implementing smart sourcing strategies. TTB accomplished the migration of its entire IT infrastructure off of ATF in 6 months, which is an extremely aggressive schedule for a migration of this scale. In fact, the migration was completed well ahead of schedule and within an extremely tight budget.

The Department also remains focused on enhancing project management capability by establishing a Treasury-wide training program. In line with OPM and OMB guidance, Treasury's existing IT capital planning policy outlines the skills and competencies required for project managers based on project scope and complexity. Currently, bureau CIOs are required to certify that project managers for major investments are qualified according to these guidelines. This initiative, which supplements bureau training programs, will include a project management course focused on Treasury-specific policy and procedures to ensure consistent implementation across the Department.

However, it is clear that there still remains work to be done. Treasury is implementing specific actions to promote greater accountability across the Department's IT management, improve the reliability of information being reported, and establish additional processes through which to assess and validate program performance and reporting. These efforts are being undertaken Treasury-wide, with engagement of the leadership across the senior management, IT, and procurement communities.

Question. Mr. Secretary, last year in a question for the record, I asked whom you held responsible for this botched procurement. The answer never identified anyone. So, now I want to ask you in person.

Who in your department is to be held responsible for this waste of taxpayer dollars?

Answer. Ultimately, as Secretary, I am responsible for the use of all Treasury resources. I rely on the ASM/CFO and the CIO to execute this responsibility related to major IT investments. I am confident that they are taking the necessary steps to provide a solution that is cost effective and meets Treasury's business needs.

The Treasury Department's telecommunications infrastructure is critical to many functions such as: online tax filing and processing, the auction and purchase of Treasury securities, toll-free telephone taxpayer assistance, the disbursement of social security and veterans' benefits, and the collection of payments and delinquent debt owed to the U.S. Government.

A Treasury-led full and open competition represents the most cost-effective use of taxpayer dollars, as well as the most responsible approach in mitigating the risk of service interruption that would impair Treasury's ability to carry out its mission.

Given that no GSA alternative was available at the time it was needed, Treasury had to use a sole-source justification to continue to receive telecommunications services. In addition, GSA delayed the Networx contract awards multiple times, which now are scheduled for March and May of 2007. After those awards, there will be an additional delay before any agency can receive services under Networx in order for the agency, including Treasury, to conduct a competition among vendors in the Networx program.

If TCE were shut down, Treasury would face a potential gap in service from the time the current contract expires, i.e., September 2007, to the time the final Treasury site is transitioned to Networx. To avoid this gap, Treasury would need to use a second sole-source justification to extend the current contract long enough to bridge to services under Networx, possibly until the first or second quarter of fiscal year 2009. This is a best-case estimate assuming: (1) no Networx protests and (2) that Treasury is the first agency in line for competition and transition needed to obtain services from a winning Networx vendor.

Treasury's extension of its current telecommunications contract also would pose the risks: (1) a protest of a second sole-source justification and a significant cost increase by the current provider; (2) termination of service, should the current provider decide to shutdown the existing telecommunications infrastructure for its own business reasons; or (3) considerable time and cost to move sites that already have been transitioned to the TCE vendor back to the current telecommunications provider.

If TCE were shut down, Treasury would be required to end the TCE contract under the contract's "Termination for Convenience" clause. That would make Treasury liable to the contractor for termination costs, such as equipment investment, minimum order costs, work in progress costs, and other costs allowed under a termination for convenience. Treasury also might be liable for the significant sunk investment to build the infrastructure necessary to provide TCE services.

In addition, Treasury currently is spending an estimated $3.3 million per month for telecommunications services above the estimated TCE monthly costs. The Department will continue to incur this additional cost until it completes the transition to TCE or Networx.

BSA DIRECT—WHY DID NO ONE SPOT THE PROBLEMS?

Question. Mr. Secretary, you heard me discuss the recent problems discovered with the BSA Direct program. That program was supposed to be the key tool for your agency to combat terrorist financing by ensuring compliance with the Bank Secrecy Act.

In our appropriations bill last year, our committee directed you to report to us if there were to be any significant delays with this program. On February 17 of this year, your agency listed the continued development of BSA Direct as a major accomplishment of the agency. Your staff told us that the project was on track and would start functioning at the end of April.

Less than 1 month later, the new director of the Financial Crimes Enforcement Network issued a "stop work" order for BSA Direct and required a top-to-bottom review because the project had failed to meet major performance milestones.

How did this happen and who are you holding responsible for this failure?

Answer. In February 2006, as the various commercial software products were integrated and tested, a number of system performance issues surfaced. Due to these performance issues, the system still was not fully tested by mid-March, and so a contingency plan had to be implemented to ensure continued access by our customers to the BSA data.

FinCEN Director Robert Werner issued a 90-day "stop work" order directing FinCEN to perform an assessment of the BSA Direct Retrieval and Sharing component in order to ensure that the best product is developed at the best price, while also taking advantage of already developed technology. An assessment team chaired by the FinCEN BSA Direct project manager and including representatives from the Treasury CIO's office, FinCEN's Acting CIO, subject matter and information technology experts from FinCEN, as well as three support contractors on the BSA Direct project was created in March 2006. This assessment team will assess and refine core requirements for BSA information retrieval, dissemination, sharing, and analysis; determine if this component of BSA Direct can be salvaged and/or leveraged by other alternatives; and define the path to ensure business continuity. The team expects to deliver a report to the FinCEN Director by July 2006, following a recent 30-day extension of the "stop work" order. This time frame will allow the assessment team to offer specific recommendations based on detailed conclusions that are supported by clear, concise and credible evidence.

Throughout this assessment period, FinCEN will be working with the IRS to ensure that there is no disruption of service to its customers in the law enforcement community. BSA Direct users will continue to have access to BSA data via the current FinCEN Secure Outreach web site, and will use the IRS WebCBRS (Currency and Banking Retrieval System) for retrieval and online analysis of information.

OVERALL MANAGEMENT OF TREASURY PROJECTS

Question. Mr. Secretary, at last year's hearing, when we discussed the mismanagement of major procurements in your Department, I thought that part of the problem might have been the many vacancies that you had in senior positions at the Department. Now, it's a year later and many of those vacancies have been filled.

Looking forward, can we expect to see these costly, wasteful mistakes come to a stop?

Answer. The Department has experienced a number of organizational changes and vacancies over the past few years. This turnover, indeed, has precipitated questions regarding the management of major procurements by the Department. With the new team recently put in place, we are working diligently to implement Treasury-wide IT capital planning and contract management policies consistently throughout the Department. These efforts are focused on promoting greater accountability across the Department's IT management, instituting standards for documentation for major projects, and establishing additional processes through which to assess and validate program performance and reporting. The Treasury CIO is working closely with the Office of the Inspector General to address the Management Challenges identified in the fiscal year 2005 Performance and Accountability Report. Actions include strengthening Treasury-wide IT capital planning policy and guidance, establishing minimum documentation requirements for major projects, and improving the reliability of investment reporting through an expanded independent verification and validation program. We believe these efforts will address key areas for improvement across the full life cycle of IT investments from acquisition, to steady state, to project closure.

Question. In particular, your agency is telling us that its new Treasury Foreign Intelligence Network will have a total cost of $30 million.

Can you guarantee us that the cost will not grow dramatically for this program like it has for so many others?

Answer. The President's fiscal year 2007 budget requests $21.2 million to implement an accelerated deployment schedule to strengthen quickly Treasury's ability to fulfill its expanded intelligence role and to operate as a full partner in Intelligence Community activities. The $21.2 million will fully fund the needed upgrades to TFIN, which is scheduled to be completed by the end of fiscal year 2007. This brings the total cost of developing the TFIN core network and disaster recovery capabilities to $37 million.

An effective governance structure has been in place for TFIN since the inception of the project to ensure mission, business, and technical objectives are achieved. This governance structure includes the: (1) TFIN Executive Board comprised of senior officials from the Office of Terrorism and Financial Intelligence and the Office of the Chief Information Officer (OCIO), and (2) TFIN Steering Committee comprised of project management and technical leads from stakeholder offices. These governance structures facilitate coordination, track project status, and support executive decision-making. OCIO hired a dedicated project manager to oversee the TFIN project.

Treasury has established additional oversight as well. The Assistant Secretary for Management and Chief Financial Officer (ASM/CFO), the Chief Information Officer (CIO), and the Assistant Secretary for Intelligence and Analysis (OIA) are committed to ensuring the project's successful completion. The ASM/CFO and CIO are engaged fully with the Assistant Secretary for Intelligence and Analysis, the system's major stakeholder. These officials and their staffs are working closely together in managing the development of TFIN, meeting regularly to resolve quickly problems that might affect the cost and schedule of the system. For example, on April 24, we implemented successfully the new stabilized TFIN platform. This executive level engagement will continue throughout the project. We expect Treasury to complete the system on time and within budget. Treasury also is working closely with and receiving direct support and assistance from the Intelligence Community.

From a Departmental IT investment management perspective, Treasury has identified TFIN as a critical investment internally, as has the Intelligence Community. As such, the TFIN investment is subject to additional reporting requirements beyond the quarterly "Control" review conducted as part of the IT capital planning and investment control.

The Department also is implementing specific initiatives to improve IT investment management, including the expansion of independent verification and validation resources to assess accuracy of project and investment reporting. We do not anticipate requesting additional funds from the Congress for the development of the TFIN system.

STOP THE WINE TAX!!

Question. Last year, your Department proposed almost $30 million in new and increased user fees on the wine and alcohol industry. We, in our wisdom, did not adopt your recommendation. Yet, again, this year, you are proposing those same user fees.

These don't appear to be new fees to provide new services to the industry. Rather, they are just new taxes proposed so you can eliminate some appropriated funding in your Department.

Why are you proposing these fees again when you know they are not likely to be approved?

Answer. The user fees proposed for TTB are intended to recover the costs in providing regulatory services to the alcohol industry. TTB issues permits to industry members engaged in the business of producing, importing, or wholesaling alcohol. Additionally, TTB must pre-approve all labels for alcohol products bottled, sold, or imported in interstate commerce. TTB must also approve certain formulas and statements of process for alcohol products, and may perform certain laboratory tests.

These services ultimately protect both the general public and industry against misleading labels, adulterated alcohol, and dishonest persons entering the alcohol business, and promote fair competition among industry members. Since these regulatory efforts provide value to the industry, the industry should pay for the benefits it receives.

Charging fees for services to industry can also provide incentives that lead to increased efficiency. For example, in calendar year 2005, 71 percent of applications for approval of alcoholic beverage labels were filed on paper instead of electronically. Fees will encourage industry to file electronically and reduce unnecessary Certificate of Label Approval submissions.

Question. Washington State is home to more than 400 wineries and 350 wine grape growers—which is more than California's Napa Valley. They play an ever-increasing role in the Washington State economy—especially in rural communities throughout the State. I believe these increased fees will severely hinder growth of the wine industry here in the United States.

Can you outline for this committee what new benefits these user fees will provide the industry? Isn't it true that, once these new fees are assessed, the wineries will not be getting any new services above the ones they are getting today?

Answer. Industry members will not receive any new services under this proposal. However, industry is currently receiving benefits from the services TTB provides and should pay for those benefits.

ESTABLISHMENT OF A DYNAMIC TAX OFFICE AT TREASURY

Question. Your fiscal year 2007 budget request includes an additional $513,000 and 3 FTE for a Dynamic Analysis Division within the Office of Tax Policy at Treasury.

What resources are you dedicating towards this effort this year—do you plan to reprogram any resources to stand it up sooner?

Answer. We would like to accelerate this initiative into fiscal year 2006 and Assistant Secretary Pack sent a letter to this effect to Chairman Bond and Ranking Member Murray on June 8, 2006. Establishing this new Division now will enhance and facilitate our capabilities to perform dynamic analyses of the macroeconomic effects of major tax policy changes, which, as you know, are particularly important to the work currently underway at the Treasury Department on tax reform. The acceleration of the new Division into fiscal year 2006 would be accomplished with no impact on our fiscal year 2006 funding; that is, it will be funded within the Office of Tax Policy's existing appropriation. The funding that we requested in the fiscal year 2007 budget also would be unaffected.

Question. Is it your intention should you receive this funding in fiscal year 2007 that dynamic scoring would be instituted into the government's budgeting?

Answer. This dynamic analysis initiative will allow us to examine the effect that tax policy changes have on the size of the economy and major macroeconomic variables, such as GDP, the size of the capital stock, and total compensation. Dynamic scoring would take this one step further and estimate how the change in the size of the economy translates into higher or lower tax revenues. We envision that the initiative will, at least initially, focus on dynamic analysis, not dynamic scoring. Conventional revenue estimates, which do not take into account changes in the size of the economy, will continue to be produced. The Department needs to develop the capability for and experience with dynamic analysis before it can consider dynamic scoring of tax policy changes.

HYPOCRISY OF CHINA VS. CUBA POLICY

Question. Mr. Secretary, do you believe that our Nation's policy of constructive engagement with China, and particularly our trade relationship with them, has helped us press our case for democracy, open markets and human rights?

If you believe that our Nation's policy of constructive engagement with China has been a positive force change in that country, why is this administration doing exactly the opposite with Cuba?

Answer. When formulating U.S. foreign policy, different considerations come into play; and sanctions regimes are designed to respond to country-specific concerns.

While the United States remains concerned about the democracy and human rights record in China, we must also recognize that China is in the midst of an historic transformation from a centrally-planned economy to a market economy. Increasing openness to trade and foreign investment is central to this process, as is the integration of China into the institutions (and the responsibilities) that govern the global trading system. Chinese leaders at the highest level have stressed their commitment to financial sector reform and openness, a major focus in Treasury's engagement with China. On his visit to Washington last month, President Hu stated that his country will not only "continue to advance the reform of the RMB exchange rate regime," but also "take positive steps in expanding market access, increasing imports, and strengthening the protection of intellectual property rights." We will continue to leverage our trade relationship to work towards open markets in China, which is in both our interests. There is still a long way to go.

Cuba has a brutal dictatorship that is increasing pressure on opposition groups. In addition to engaging in political repression, the Cuban government is actually reducing the limited economic openings for small-scale entrepreneurs in Cuba. U.S. policy towards Cuba remains to hasten the rapid transition to democracy and a free-market economy. As set forth in the Libertad Act, U.S. policy is to take steps to remove the economic embargo of Cuba when the President determines that a transition to a democratically elected government in Cuba has begun. The State Department is best placed to respond specifically to questions about the administration's policy toward Cuba.

ARE THE RUSSIANS ALLIES WHEN IT COMES TO COMBATING TERRORISM?

Question. A senior official in Russia's Foreign Ministry said last week that, as chair of the G–8, Russia will put forward a number of new initiatives to combat international terrorist financing.

Have you been in contact with the Russian government to help shape this agenda, and if so, what new initiatives should we expect out of the Russians in this area?

Answer. Yes, Treasury has been in contact with Russian counterparts regarding the G–8 Anti-Money Laundering/Combating the Financing of Terrorism (AML/CFT) agenda. For example, AML/CFT issues were discussed in the most recent G–8 Finance Sous Sherpas on May 11. Russia will be hosting an experts meeting from May 31 through June 1, 2006, which will focus on working with the Financial Action Task Force (FATF) style Regional Bodies (FSRBs) to implement AML/CFT standards. Russian proposals in this area are consistent with ongoing bilateral and multilateral AML/CFT initiatives. In particular, Russia has stressed the importance of enhancing the effectiveness of the FSRBs by increasing IMF and World Bank coordination with the regional bodies and by increasing support for their mutual efforts.

The United States and Russia agree that it is crucial for countries to continue to develop strong AML/CFT programs. We agree that the work of the FSRBs to promote implementation of the FATF AML/CFT standards is instrumental to these efforts, as is the support of the International Financial Institutions. We see merit in Russia's proposals to enhance cooperation between these groups.

Question. On a related matter, Russia, as you know, does not officially consider Hamas a terrorist organization. In fact, Russia was one of the first countries to invite Hamas on an official visit following the terrorist group's victory in the Palestinian legislative elections.

How do disagreements between nations in the definition of who is a "terrorist" affect our efforts to stop the flow of terrorist-related finances?

Do you worry that the Russians' efforts in this area might undermine our own efforts and those of other allies?

Answer. United Nations Security Council Resolution (UNSCR) 1267 requires all countries to freeze the assets of individuals and entities related to Usama Bin Laden, Al Qaeda and the Taliban. UNSCR 1373 requires all countries to freeze the assets of individuals and entities that support global terrorism, but leaves it to member states to determine which groups fall within its scope. Many countries, including the United States and members of the European Union, have designated Hamas as a terrorist organization. Unfortunately, not all countries have followed this lead.

As with any sanctions program, the extent to which a terrorist designation is multilateralized renders it more or less effective. This certainly applies to Hamas. We will continue to work, both bilaterally and multilaterally, to ensure that terrorist organizations find no financial safe haven and that these organizations are to the greatest extent possible deprived of access to the international financial system.

DISRUPTING TERRORIST FINANCING NETWORKS

Question. Treasury now has at its disposal, increased resources to disrupt terrorists' financial support networks and you continue to seek more such resources. In fact, the majority of the fiscal year 2007 requested increases go for these purposes.

What kind of progress have you been able to make on cross-border currency transactions, wire transfers, and effective oversight of alternative payment systems such as "hawalas" with other countries?

Answer. In the area of traditional wire transfers, we believe that every major bank in the United States has access to the tools necessary to implement a robust compliance program to interdict transactions potentially violative of OFAC regulations. OFAC has also made considerable progress in the area of cross-border Automated Clearing House (ACH), actively working with industry and with the Federal Reserve's Gateway to develop new standards to increase the transparency of the parties involved in such transactions. OFAC, along with FinCEN, is coordinating with both Federal and State regulators to address money laundering issues within informal value transfer systems. It has, for example, pursued a number of cases, both criminally and civilly, with regard to hawalas acting illegally in sending funds to sanctioned countries, particularly Iran.

FinCEN continues to oversee and better ensure compliance with the Bank Secrecy Act with respect to cross-border currency transactions, wire transfers and transactions conducted in the United States by, for, or on behalf of alternative payment systems such as hawalas. All of these types of transactions are subject to certain reporting, and record-keeping requirements under the Bank Secrecy Act. FinCEN also will continue to evaluate the need for further rule making under the Bank Secrecy Act to better safe guard our financial system from criminal abuse.

Additionally, we have been addressing actively these issues with other countries through our membership in the Financial Action Task Force (FATF) and its network of FATF-Style Regional Bodies (FSRBs). FATF and its FSRBs include approximately 150 countries that have agreed to implement the FATF Forty Recommendations on Money Laundering and Nine Special Recommendations on Terrorist Financing.

Last year, TFI led the effort within the FATF to adopt Special Recommendation (SR) IX. SR IX requires FATF/FSRB members to take steps to detect the physical cross-border transportation of currency and negotiable instruments and to stop or restrain funds that are suspected to be related to terrorist financing or money laundering. FATF/FSRB member countries also are required under Special Recommendation (SR) VI to implement measures to ensure that money remitters are licensed or registered, apply appropriate AML/CFT controls (including customer identification, recordkeeping, and Suspicious Activity Report (SAR) reporting), and to take administrative, civil or criminal action against violators. In the United States, money transmitters (including alternate payment systems such as hawaladars) are required to register with the Financial Crimes Enforcement Network (FinCEN); adopt AML programmatic policies, procedures and controls; identify customers; and report suspicious activity.

With respect to wire transfers, SR VII requires countries to transmit full originator information with cross-border wires, providing law enforcement authorities with ready access to information needed to track illicit funds. These requirements complement those contained in the Travel and Recordkeeping Rules that govern wire transfers in the United States.

As co-chair of the FATF's Working Group on Terrorist Financing, the U.S. Government plays a key role in the implementation of these Special Recommendations. TFI also works within the interagency to provide assistance to other jurisdictions in implementing the FATF 40 + 9.

HOW MUCH CAN REALISTICALLY BE ACCOMPLISHED?

Question. Terrorist cells are increasingly self-financing through criminal activity such as drug trafficking, counterfeiting intellectual property, insurance claim fraud to name a few, as opposed to wire transfers. There are strong indications that terrorist operations do not require exorbitant sums of money. The bombings of the U.S.S. *Cole* and those in Bali, Madrid and London, are all estimated to have cost $50,000 or less, and the 9/11 bombings were estimated to cost $500,000. Experts in terrorist financing have said that the cost of terrorist attacks is decreasing exponentially.

Are we reaching a point of diminishing returns because terrorists are avoiding the transfer mechanisms that we are good at tracking?

Answer. Treasury's approach to combating terrorist financing is two-fold: first, we seek to identify and close vulnerabilities in the international financial system; second, we seek to identify, disrupt and dismantle the financial networks that support terrorist organizations.

We are meeting this responsibility through a number of initiatives involving various sectors. For example, we are working through organizations such as the FATF and the IMF and World Bank to ensure that all countries are taking effective measures to prevent terrorist abuse of such mechanisms as charities, cash couriers, wire remitters, and informal funds transfer providers.

The imposition of sanctions by the United States and its international partners against terrorists, terrorist organizations and their support structures is a powerful tool with far-reaching effects that goes beyond the blocking of terrorist assets. Designating individuals or organizations as SDGTs (Specially Designated Global Terrorists), SDTs (Specially Designated Terrorists), or FTOs (Foreign Terrorist Organizations) notifies the U.S. public and the world that these parties are either actively engaged in or supporting terrorism or that they are being used by terrorists and their organizations to support the terrorist agenda. Notification also serves to expose and isolate these individuals and organizations and denies them access to the U.S. financial system, and in the case of a United Nations (U.N.) designation, the global financial system. In addition, the imposition of economic sanctions can assist or complement the law enforcement actions of other U.S. agencies and/or other governments.

As long as terrorists, terrorist organizations and their support structures continue to target the United States and its allies, we must make every effort to combat them; targeted sanctions are one of the tools employed by the United States. Terrorists are becoming more sophisticated at attempting to evade sanctions. Such activity necessitates our continuing efforts to identify, expose and target morphed or reformed terrorist organizations, front companies, and agency relationships that may be developed to evade sanctions and allow them access to the United States and international financial systems. Unless the United States and its allies apply constant and unrelenting pressure, terrorists will immediately exploit any opportunities that become available. Denying terrorists, especially their financial supporters, the convenience and benefits of using traditional legitimate economic and financial systems has created another barrier to their activities and has impeded their support networks. Removing those hurdles to the funding of their infrastructures will not produce a benefit because they will be able to revert to using unprotected traditional systems. Keeping those barriers in place requires undiminished commitment by Treasury at the same time that the alternative systems that terrorists and their supporters may choose to use become another target set for action by the U.S. Government. It gains us nothing in the war on terrorism to remove security from the front gate because the terrorists have started trying to tunnel beneath the fence. Consequently, in the War on Terror, there are arguably no diminishing returns, because stopping or impeding even one terrorist act saves lives and adds to the national and economic security of the United States and its allies.

PROGRESS WITH CHARITABLE ORGANIZATIONS

Question. Charitable organizations can be exploited by terrorists because there is little government oversight, donations are largely anonymous, and these funds are collected by both charitable groups and the government in lieu of taxes for religious, social, and humanitarian purposes. The financial and operating structures of charitable organizations are not easily understood.

How have you been able to deal with this and are you considering measures that will produce transparency in charities?

Answer. Treasury has taken an active role in preventing widespread abuse of the charitable sector by terrorists to raise and move funds and provide logistical support. Curtailing such abuse is a critical element in the U.S. Government's national and international strategy to combat terrorist financing generally, as underscored in the 2002 and 2003 National Money Laundering Strategies, numerous U.S. Government counter-terrorist financing strategies, and various international resolutions and standards.

The U.S. Government has developed a comprehensive strategic approach to combat the risk of terrorist financing in the charitable sector. Collectively, these measures include: a coordinated oversight system comprised of Federal, State, and private elements; targeted investigations, prosecutions, and designations; international engagement; and extensive outreach engagements with the private sector.

Under the coordinated oversight prong, Treasury has promulgated effective measures for monitoring charitable organizations' compliance with U.S. law through its terrorist-related designations pursuant to Executive Orders (EO) 13224 and 12947. As of May 2006, the United States has designated 41 charities under EO 13224 and EO 12947 because of their support for terrorist activity. This includes five U.S.-based charities and 36 additional international charities (two of which have branch offices located in the United States). On February 19, 2006, the United States blocked the assets of a sixth U.S.-based charity pending further investigation, which has the effect of freezing all assets located within U.S. jurisdiction and prohibiting U.S. nationals from transacting with the charity. These designations serve a multitude of purposes aside from blocking the flow of funds to terrorist organizations or purposes, including putting other charities and donors on notice of the designation, deterring donors or charities that may otherwise have funded terrorist organizations, and forcing terrorist organizations to use alternative, riskier financing mechanisms.

To increase awareness of the risk of terrorist financing in the U.S. charitable sector and to provide charities with measures they can take to protect themselves, Treasury's Office of Terrorist Financing and Financial Crime (TFFC) has undertaken an extensive outreach program. In response to numerous dialogues with the sector on how they might better adopt practices to protect themselves from such abuse, and protect the integrity of charitable giving and the confidence of donors, in November 2002, the Treasury Department released the Anti-Terrorist Financing Guidelines: Voluntary Best Practices for U.S.-Based Charities (Guidelines), which were revised and released in draft form to solicit public comment in December 2005. The Guidelines provide measures for charities to take in order to protect themselves against the risks of terrorist financing.

The Guidelines follow a risk-based approach that balances the demands of applying these protective measures with the particular operational risks of each charity and with an understanding that terrorist financing risks vary between charities. They encourage charities to enact and practice sound governance and fiscal policies, which includes detailed record-keeping, as well as to collect information on and vet key employees, members of the governing body, and potential grantees. There is also guidance on the adoption of specific practices that help better facilitate compliance with OFAC sanctions programs, including those that address terrorist financing, and provide information on directing inquiries and/or suspicions and referrals to the appropriate State and Federal law enforcement authorities. Moreover, the issuance of the Guidelines initiated a strong, ongoing dialogue with the sector, which reinforced the sector's awareness of the risks of terrorist abuse it faced, and led to a greater understanding of the available resources and measures that could help to protect against such risk.

The Guidelines also led to a strong engagement with the American Muslim charitable community, which often faces heightened risks due to the high-risk regions in which many American Muslim charities operate. TFFC has facilitated meetings with other watchdog and intermediary organizations (such as ECFA and BBB–WGA, etc.) in an effort to facilitate the creation of the National Council for American Muslim Non-profits (NCAMN). Launched in March of 2004, NCAMN is a proactive initiative of the American Muslim charitable community and is working to create standards of transparency and accountability similar to other intermediaries that it can apply to organizations under its purview, including relief organizations, mosques, Islamic schools, etc. TFFC's parallel engagement with the American Muslim charitable sub-sector and the larger charitable sector have resulted in charities adopting more proactive approaches to protect their assets and the integrity of their operations.

TFFC has also acted as an integral component of overall U.S. engagement with the international community. Specifically, TFFC has helped to shape international policy on charities through its work with the FATF. It recently took part in negotiations for the FATF's Interpretive Note to Special Recommendation VIII on non-profits, which is the practical application of the international standard to curb terrorist abuse of non-profit organizations. This Interpretive Note was adopted by the FATF member countries at the February 2006 Plenary. TFFC will continue to engage with the FATF, its regional-style bodies, and individual member countries to encourage implementation of national standards that encourage transparency and accountability in the charitable sectors of those jurisdictions.

Finally, OFAC has a section of its website dedicated to charitable organizations and will shortly be publishing suggestions for analyzing sanctions risk with regard to both donations and grant-making.

IS TREASURY TARGETING NON-CONVENTIONAL FUNDING SOURCES?

Question. GAO has recommended that the administration pay closer attention to non-financial mechanisms used by terrorist financiers to generate and distribute funds.

To what extent is the Treasury Department, and its Office of Terrorism and Financial Intelligence (TFI) in particular, interested in and able to concentrate on non-conventional money-generating and money-moving networks such as the trade in commodities—gold, diamonds, cigarettes, and gemstones?

Answer. TFI examines all forms of financial networks that support terrorist, WMD and other illicit activity, including trade-based money laundering and potentially illicit trade in commodities.

FinCEN recently issued an interim final rule that requires dealers in precious metals, stones or jewels to establish and maintain anti-money laundering programs to prevent and detect money laundering and terrorist financing. In addition, the Bank Secrecy Act requires all trades and businesses in the United States to report the receipt of cash, or cash equivalents, in excess of $10,000 to FinCEN. This information is captured on the FinCEN/IRS 8300 form which also provides a "suspicious transaction" box to alert law enforcement and regulatory agencies to the possibility of criminal activity. Perhaps most importantly, the Bank Secrecy Act has many reporting and recordkeeping requirements on banks, money service businesses, broker dealers and other financial institutions in the United States including, but not limited to, the reporting of cash and suspicious transactions by customers. Since all types of non-conventional money-generating or money-moving networks use banks or other types of financial institutions to place and move funds, financial activities by these entities are reported, or otherwise available to, law enforcement, intelligence and regulatory authorities. Attempts to evade the Bank Secrecy Act by way of "structuring" or bulk-cash transportation also make criminals vulnerable to detection by law enforcement.

Additionally, TFFC is working with the relevant FATF-style Regional Bodies (FSRBs) to examine trade-based money laundering and to craft innovative solutions. TFFC has worked extensively with the interagency community, particularly Immigration and Customs Enforcement (ICE) at the Department of Homeland Security, to understand and counteract the trade-based money laundering employed by Colombian narcotics groups through the Black Market Peso Exchange. TFFC and ICE have worked through international organizations such as the FATF to develop typologies of trade-based money laundering and continue to collaborate with international partners and exchange trade-based data as a means of identifying trade-based money laundering networks and taking appropriate responsive action.

Finally, OFAC focuses on any entities that meet the criteria for designation under Executive Orders and statutes it implements. Insofar as such entities include non-conventional money generating/moving entities, OFAC investigates the ways in which such entities are moving money in connection with individuals and entities on OFAC's List of Specially Designated Nationals and Blocked Persons (SDN list). Thus, OFAC's focus is not on any one kind of entity, but rather on any entity moving value for the benefit of a narcotics trafficker's or terrorist's or WMD proliferator's organization.

WHAT ABOUT ADDRESSING OFFSHORE BANKS, ETC.?

Question. It has been suggested that the U.S. Government is neglecting the role played by offshore banks, shell companies, and business fronts in funding terrorism. Do you agree?

Answer. No. FinCEN requires financial institutions to establish and maintain adequate anti-money laundering programs with systems and controls, training, testing and designated personnel to detect and report suspicious activity, including terrorist financing. Offshore banks, shell companies and business fronts have long been acknowledged as high risk entities. As such, these entities are subject to elevated due diligence standards by financial institutions to ensure compliance with the suspicious activity reporting requirement of the Bank Secrecy Act. Failure to develop an adequate anti-money laundering program and failure to report suspicious activity involving offshore banks, shell companies and business fronts has resulted in very significant civil money penalties by FinCEN. See http://www.fincen.gov/reg_enforcement.html.

Title III of the USA PATRIOT Act provides the U.S. Government with powerful tools to prevent these entities from being utilized by terrorists to raise and move funds. Section 312 requires financial institutions to apply enhanced due diligence policies and procedures to correspondent accounts maintained for certain foreign banks operating under offshore banking licenses. Section 313(a) prohibits U.S. financial institutions from providing correspondent accounts in the United States to foreign banks that do not have a physical presence in any country. It also requires these financial institutions to take reasonable steps to ensure that correspondent accounts provided to foreign banks are not being used to provide banking services indirectly to foreign shell banks and financial institutions are required to obtain certification to this effect.

The U.S. Government has also taken action against jurisdictions with respect to their offshore sectors. Under the provisions of Section 311, the U.S. Government determined Nauru to be a jurisdiction of primary money laundering concern and proposed instituting special measures against it in 2002 for its failure, among other things, to adequately supervise its offshore banking sector. The U.S. Government has also been pursuing cases where offshore banks have attempted to manipulate U.S. branches, affiliates, and correspondents by using the U.S. financial system to route transactions in violation of our sanctions. We are working diligently with the banking community and with international regulators to ensure transparency in transfers such as cover payments where there is little information about underlying transactions. We also have extensive outreach and educational programs in place to address manipulation of check-clearing and trade finance mechanisms.

The U.S. Government participates actively in international bodies such as the Financial Action Task Force (FATF) and the Offshore Group of Banking Supervisors (OGBS) that promote effective implementation of international anti-money laundering and counter-terrorist financing standards in offshore financial centers.

OFAC has been pursuing cases where offshore banks have attempted to manipulate U.S. branches, affiliates, and correspondents by using the U.S. financial system to route transactions in violation of our sanctions. We are working diligently with the banking community and with international regulators to assure transparency in transfers such as cover payments where there is little information about underlying transactions. We also have extensive outreach and educational programs in place to address manipulation of check clearing and trade finance mechanisms.

Question. Can Treasury play an expanded role in this area?

Answer. Treasury continues to monitor jurisdictions and institutions overseas to identify offshore sectors and activities that could pose potential threats to the U.S. financial system. We will utilize the authorities made available to us by Congress under the Bank Secrecy Act (BSA) as amended by the USA PATRIOT Act including section 311, the International Emergency Economic Powers Act (IEEPA) and other statutes to address these specific threats through targeted economic and financial sanctions, rulemaking and the issuance of advisories, alerts and reports to industry.

TREASURY'S OFFICE OF INTELLIGENCE ANALYSIS

Question. Ms. Gardner, the 9/11 Commission stated that terrorist financing had not been a priority for either domestic or international intelligence collection and, as a result, intelligence reporting on the issue was not up to par.

How has Treasury's relatively new Office of Intelligence Analysis contributed to overall intelligence collection?

Answer. While Treasury's Office of Intelligence and Analysis (OIA) is primarily an analytical unit, it has already begun to play a role in improving the Intelligence Community's (IC) collection efforts on terrorist financing. In 2005, OIA hired a full-time Requirements Officer, who submits requirements and evaluations on behalf of all Treasury entities, including OFAC and FinCEN, to the IC. In these requirements submissions, Treasury includes comprehensive background information as well as a detailed statement of Treasury's intelligence gaps to help focus the IC on Treasury's needs. In response to these detailed requirements, Treasury has received a greatly increased level of tailored support from the IC. OIA is in the process of hiring another Requirements Officer to help with its growing responsibilities in this area. OIA has played a particularly significant role in improving IC collection on the Iraqi insurgency. OIA is serving as the co-lead with the Department of Defense on the Baghdad-based Iraq Threat Finance Cell (ITFC). The Treasury presence in Iraq on the ITFC is already paying dividends. More and better detailed information on insurgency finance issues is becoming available, due in part to the increased analytic focus on this issue. In addition, the financial intelligence analysts have provided great support to the military in identifying trends and patterns in insurgency financing in the context of a cash-based economy.

WHERE DO WE GO FROM HERE?

Question. Mr. Levey and Mrs. Gardner, the 9/11 Commission report suggests that the strategy for terrorist financing should shift from seizing assets to gathering intelligence since it may not be achievable or cost effective to attempt to deny terrorists funding. Terrorists are increasing seeking more informal ways of moving money and terrorist networks themselves are becoming more decentralized and self-supporting.

What, do you believe, is the appropriate combination of goals to address terrorist financing?

Answer. The imposition of sanctions by the United States and its international partners against terrorists, terrorist organizations and their support structures is a powerful tool with far-reaching effects that goes beyond the blocking of terrorist assets. Designating individuals or organizations as SDGTs (Specially Designated Global Terrorists), SDTs (Specially Designated Terrorists), or FTOs (Foreign Terrorist Organizations) notifies the U.S. public and the world that these parties are either actively engaged in or supporting terrorism or that they are being used by terrorists and their organizations to support the terrorist agenda. Notification also serves to expose and isolate these individuals and organizations and denies them access to the U.S. financial system, and in the case of a U.N. designation, the global financial system. In addition, the imposition of economic sanctions can assist or complement the law enforcement actions of other U.S. agencies and/or other governments.

As long as terrorists, terrorist organizations and their support structures continue to target the United States and its allies, we must make every effort to combat them and targeted sanctions is one of the tools employed by the United States. Terrorists are becoming more sophisticated at attempting to evade sanctions. Such activity necessitates our continuing efforts to identify, expose and target morphed or reformed terrorist organizations, front companies, and agency relationships that may be developed to evade sanctions and allow them access to the United States and international financial systems. Unless the United States and its allies apply constant and unrelenting pressure, terrorists will immediately exploit any opportunities that become available.

Denying terrorists, especially their financial supporters, the convenience and benefits of using traditional legitimate economic and financial systems has created another barrier to their activities and has impeded their support networks. Removing those hurdles to the funding of their infrastructures will not produce a benefit because they will be able to revert to using unprotected traditional systems. Keeping those barriers in place requires undiminished commitment by Treasury at the same time that the alternative systems that terrorists and their supporters may choose to use become another target set for action by the U.S. Government. It gains us nothing in the war on terrorism to remove security from the front gate because the terrorists have started trying to tunnel beneath the fence. Subsequently, in the War on Terror, there are arguably no diminishing returns because even stopping or impeding only one terrorist act saves lives and adds to the national and economic security of the United States and its allies.

Question. Given these trends and given the fact that we don't have unlimited dollars, how can we get the most for the money spent?

Answer. Treasury focuses on two goals regarding terrorist financing: to identify and close vulnerabilities in the international financial system and to identify, disrupt and dismantle the financial networks that support terrorist organizations. The overall impact of these effects is to make it costlier, riskier, and less efficient for terrorists to move their funds through the international financial system. Treasury gets the most for the money spent by focusing on these two strategic priorities. Therefore, the extent to which terrorists are forced to rely on more cumbersome and less reliable methods of funds movement is a measure of success. The response to this development, however, is to redouble our efforts to target all financial channels, both formal and informal.

Treasury will continue to apply its authority, in coordination with the inter-agency national security infrastructure, to disrupt the financing of terrorism and deter terrorist operations.

DO BANKING AGENCIES COMPLY WITH FINCEN'S BANK SECRECY REQUIREMENTS?

Question. Last year, I asked how regulatory agencies can seriously comply with the required exchange of bank secrecy data when there is no penalty if they don't comply. The Department's answer was to say that an unprecedented level of cooperation has been reached with the banking agencies and that including a penalty provision would have undermined this cooperation.

So, can you say that up through today, since the enforcement action against Riggs National Bank, all the banking agencies have been fully cooperative?

Answer. Yes. The Riggs National Bank matter served notice of the problems that can arise with respect to an absence of cooperation, unintentional or otherwise, among Federal agencies with parallel or overlapping jurisdiction. Based partly on the Riggs matter, FinCEN entered into Memoranda of Understanding (MOU) with the Federal banking agencies in October 2004. FinCEN has and will continue to enter into MOU with other Federal and State agencies, as appropriate. The MOU ensure that FinCEN receives timely notice of all significant Bank Secrecy Act (BSA) related findings, and ensure cooperation among the stakeholder agencies with respect to compliance with, and enforcement of, the anti-money laws of the United States.

In accordance with Memoranda of Understanding with FinCEN, all Federal and State law enforcement and regulatory agencies are required to safeguard BSA data acquired from FinCEN from unauthorized disclosures. In order to ensure the effectiveness of the safeguards, FinCEN conducts inspections of agencies that receive BSA data.

In regard to information flowing to FinCEN from the Federal banking agencies, we have instituted systems and controls to ensure the data is not disseminated to unauthorized personnel. In fact, the Memoranda of Understanding with the Federal banking agencies of October 2004 contain an explicit provision prohibiting the unauthorized disclosure of BSA and other "confidential supervisory information" by FinCEN to unauthorized parties.

In addition, 31 U.S.C. 5318(g)(2) prohibits any director, officer, employee or agent of a financial institution to notify any person reported on a suspicious activity report that such a report has been filed with FinCEN. This same section prohibits any officer or employee of any Federal, State or local government from doing the same, other than as necessary to fulfill official duties. Furthermore, government employees are subject to a host of legal and administrative sanctions for unauthorized disclosures of protected information, including BSA information.

Question. FinCEN recently stood-up its Office of Compliance, among other things, to analyze Bank Secrecy Act examination data provided by regulators.

What is your assessment of how successful FinCEN has been with its analysis of bank secrecy data and have results been demonstrated?

Answer. FinCEN provides a broad range of analyses of Bank Secrecy Act (BSA) data to Federal, State, local and foreign law enforcement and regulatory customers. These analyses play an important role in safeguarding the financial system from the abuse of financial crime, including money laundering, terrorist financing, and other illicit activity. Specifically, FinCEN analysis of BSA data identifies relationships among targets of law enforcement investigations, identifies patterns of funds movement, and identifies the locations of suspects and their assets. FinCEN analysts also enhance BSA data with all-source information in providing findings and options to customers. FinCEN has developed a suite of analytical tools that enable analysts to conduct complex mining of BSA data, and to depict results with graphic displays of data relationships and financial flows.

In fiscal year 2005, FinCEN provided BSA data analysis in response to 1,436 requests from domestic and foreign law enforcement, regulatory and intelligence customers. For the first half of fiscal year 2006, FinCEN provided analysis in response to 742 customer requests. FinCEN's customers for this work also include foreign financial intelligence units (FIUs) that are members of the Egmont Group of FIUs, comprising 101 participating countries. The Egmont Group is committed to a global effort to combating money laundering and terrorist financing through FIU cooperation and information exchange. During the past 5 years, Egmont FIU case requests to FinCEN have grown 32 percent annually on average. FinCEN also works with financial regulators, including FinCEN's own regulatory component (FinCEN's Regulatory Policy and Programs Division), the Federal banking supervisory authorities, the Internal Revenue Service, and 41 State banking supervisory agencies. FinCEN's BSA data analysis in response to these requests supports pending enforcement actions against particular non-compliant institutions, and also supports possible Bank Secrecy Act policy enhancements. This type of analysis has identified compliance issues previously undetected in certain depository institutions and money services businesses and, since August 2005, has supported at least six significant enforcement actions against three banks, one broker-dealer firm, a casino and a money services business.

FinCEN's BSA data analysis for regulatory customers also provided filing trends and patterns and identified vulnerabilities in certain financial industry segments. For example, information gleaned from the study of Suspicious Activity Reports (SARs) relating to the insurance industry was used in developing new insurance regulations. FinCEN's BSA data analysis also supports guidance to the private sector, including "The SAR Activity Review—Trends, Tips & Issues", as well as the biannual publication of "The SAR Activity Review—By the Numbers", a compilation of numerical data gathered from Suspicious Activity Reports filed by all institutions with mandatory suspicious activity reporting requirements. Financial industries members widely use both analytical publications.

The large volume of customer requests to FinCEN for analysis is one important measure of the effectiveness of FinCEN's BSA data analysis. Another important measure is customer satisfaction. FinCEN's most recent survey of customer satisfaction, which was conducted by an independent evaluator from August to October 2005, included a statistically valid sample of the FinCEN customers of four types of analysis products (investigative target reports, investigative case reports, SAR activity review, and strategic analysis products). The survey results indicated 73 percent of FinCEN's customers found FinCEN's analytic support valuable.

The effectiveness of FinCEN's analysis of BSA data also is highlighted in the outcomes of specific cases. Recent examples of effective outcomes include the following:

—FinCEN completed a proactive targeting case initiated based on a Suspicious Activity Report that alleged possible terrorist financing based on suspicious wire transfers. The bank referred to numerous instances of the company being identified as a front or shell company for Hezbollah. The report explored potential connections between Islamic terrorism fund-raising and narcotics money laundering through an examination and analysis of Bank Secrecy Act information on a company located in South America, and a company believed to be affiliated in Central America.

—A geographic threat assessment was completed on the Southwest Border based on analysis of all BSA data forms for counties bordering Mexico. The threat assessment was requested by the Texas Department of Public Safety's (DPS) Directed Intelligence Group in an effort to identify money laundering hot spots. The DPS is working toward intelligence-driven operations and investigations, and with this threat assessment of money laundering hotspots will be able to direct and train their intelligence collection efforts much more effectively. Recently, criminal investigators in Texas noted that debriefings of suspects in the southwest border region indicated suspects were under pressure to find crossing points other than Laredo, Texas, and El Paso, Texas, because of the increased observation that those locations have been receiving as a result of the FinCEN assessment.

—FinCEN examined SARs through one of its BSA search and analysis tools to identify activity associated with the suspicious remittance of U.S. dollars to Colombia via Automated Teller Machines (ATMs). Research identified a cluster of 11 interrelated SARs associated with a man and a woman located in the United States who were depositing and transferring funds into or through 36 accounts at 8 U.S. banks. SARs indicated that a large percentage of the funds were subsequently remitted back to Colombia through ATMs at the rate of 57 to 157 withdrawals per day. Currency Transaction Reports (CTR) and Currency and Monetary Instrument Reports (CMIR) verified statements made by the man that the funds were derived from cash imported from Colombia. This activity, initially provided to law enforcement as an investigative referral, provided only a snapshot of what could be a much larger pattern of activity.

—FinCEN supported an Immigration and Customs Enforcement (ICE) field office effort to identify unlicensed/unregistered remittance businesses in a specific geographic area of Virginia. FinCEN found no viable targets through the SAR targeting method of querying key words in the SAR narratives, e.g., "wire transfer," "remittance," "hawala," etc. As a result, FinCEN downloaded CTRs filed by banks in the specified area, and after conducting analysis of the CTRs through an ad hoc database, was able to identify seven targets.

—FinCEN utilized CTR targeting in support of an ICE investigation into alleged willful negligence by a large bank. The investigation was initiated after it was discovered that the bank had not filed SARs on large, suspicious cash deposits by a convicted heroin money launderer. FinCEN focused its efforts on finding other individuals or businesses that had conducted similar activity through the same and other banks in the geographic area. Through the use of CTRs, FinCEN profiled the activity of the heroin money launderer then identified similar activity by downloading all CTRs where the number and amount of CTR activity was similar to that of the money launderer. The effort resulted in an extensive list of targets that resulted in a number of "spin-off" investigations by ICE and IRS–CI.

FINCEN'S REGISTRATION OF MONEY SERVICE BUSINESSES (MSBS)

Question. The Treasury IG has found that a little over 1 year ago, only a small number of the Money Service Businesses (MSBs) such as Western Union and post offices that do money orders, had registered with FinCEN as required by the Money Laundering Suppression Act of 1994. As of a few months ago, FinCEN's published list of MSBs had only increased a little bit, not much of an improvement.

What is being done to improve this registration effort?

Answer. Since the implementation date of the registration requirement for money services businesses on December 31, 2001, it is clear that identifying the universe of businesses subject to our money services businesses-anti-money laundering regulatory regime is one of the greatest challenges we face as an agency. Finding ways to enhance compliance with the registration requirement has been one of our focuses since the inception of the registration concept.

FinCEN developed and is implementing a comprehensive strategy in fiscal year 2006 for addressing the challenges posed by the identification and registration of money services businesses. The success of our efforts to increase registration, and therefore establish transparency in this segment of the financial services industry, will depend in large part upon our approach to communications, education, and industry outreach. We are in the process of upgrading our money services business internet website, translating the current instructional brochures into various foreign languages, fully implementing the Bank Secrecy Act resource center, and developing and implementing a comprehensive education program for the Internal Revenue Service examiners, our State regulatory partners and the industry.

Over the past several years, we have devoted considerable resources to conduct aggressive outreach and education campaigns concerning Bank Secrecy Act (BSA) requirements. Despite those efforts, some in the industry, particularly those that offer these services only as an ancillary component of their primary business, appear to be unfamiliar with or unaware of their obligations under the BSA. At the same time, as indicated by the volume of requests for administrative rulings and numerous questions received at industry conferences, it is apparent that the current regulatory framework would benefit by more clarity that can be provided through the development and issuance of guidance, such as advisories, frequently asked questions, and the like.

Therefore, we have stepped up our efforts to clarify the expectations that accompany these requirements. For example, on April 26, 2005, FinCEN published guidance to the money services business industry which clearly established the expectations for compliance with the registration, anti-money laundering program, recordkeeping and reporting requirements of the Bank Secrecy Act. On the same date, FinCEN and the Federal banking agencies published joint guidance to banking organizations that explained these expectations to entities providing banking services to money services businesses. On February 3, 2006, we published guidance to reinforce and clarify the registration requirements for money services businesses.

Question. Now that more than 4 years have passed since the registration requirement became effective, how many MSBs have been penalized for non-registration or failure to register?

Answer. To date, we have not penalized a money services business for failure to register under the Bank Secrecy Act. However, we have supported efforts by the Internal Revenue Service (IRS) to upgrade its Bank Secrecy Act (BSA) examination capabilities by providing revisions to the IRS examination manual for non-bank financial institutions, and by providing instruction on risk-based examination procedures at IRS examiner training programs. We believe that these efforts are beginning to show positive results. During fiscal year 2005, the IRS conducted examinations of 3,700 entities for compliance with the BSA, including registration. Furthermore, since July 28, 2005, the Office of Compliance at FinCEN referred 27 suspected unregistered money services businesses to the IRS's Small Business/Self-Employed Division for possible examination.

FinCEN has, however, recently penalized a money services business for violating various provisions of the Bank Secrecy Act. On May 9, 2006, FinCEN issued a civil money penalty in the amount of $10,000 against a money services business located in Tampa, Florida. FinCEN determined that this money services business failed to develop and implement a written anti-money laundering program reasonably designed to ensure compliance with the Bank Secrecy Act which led, in turn, to a failure to file 80 currency transaction reports. In fact, the money services business had a zero currency transaction reporting compliance rate during the period of the BSA deficiencies.

Question. How has the registration program for MSBs enhanced FinCEN's ability to identify potential terrorist financing, money laundering, and other financial crimes?

Answer. The registration requirement is one of many Bank Secrecy Act (BSA) requirements that enables FinCEN to further its mission of safeguarding the financial system from abuses of financial crime, including terrorist financing, money laundering and other illicit activity. The registration requirement facilitates transparency and critical identifying information about the thousands of money services businesses operating in the United States, including readily available information on agent outlets of the major money service business companies. In cases involving non-compliant money services businesses, we can compel immediate corrective action with registration. In cases involving egregious or willful failure to register under the BSA, we can seek and impose appropriate remedies.

As a natural by-product, the registration requirement also enables banks, which money services businesses must eventually use, to gauge the level of knowledge and compliance with the anti-money laundering and terrorist financing provisions of the

BSA. Upon discovery of suspected criminal activity or non-compliance with the BSA by money services business customers, banks can file suspicious activity reports to enable law enforcement and regulatory agencies to respond appropriately.

CAN THE PRESIDENT'S NEW COMMUNITY DEVELOPMENT PROGRAM FILL THE ROLE OF CDFI FUND?

Question. Secretary Snow, you mention in your opening statement that the President is only requesting $7.8 million for the Community Development Financial Institutions (CDFI) Fund, which was funded at $55 million last year. The funding that the President is requesting will only support the New Markets Tax Credit program. The other CDFI Fund activities he proposes to consolidate with other community development programs as part of the Strengthening America's Communities Initiative (SACI). As you know, the President made a similar proposal last year, which the Congress rejected.

The other programs within the CDFI Fund are critical in bringing financial services and private investment into underserved communities. For every dollar that the Federal Government spends, these CDFIs are able to attract $20 in private sector investment. These funds are used to support programs that help support the creation of small businesses, assist with homeownership, even bring ATMs to communities. In my home State of Washington, one CDFI, the Cascadia Revolving Loan Fund has used grant money to increase its capacity and support innovative programs like their Child Care Fund which offers financing and technical assistance to child care providers so that they can open their own child care centers and bring quality child care to these communities.

Since the CDFI Fund helps to bring capital and financial services to communities and individuals that traditional banks view as too risky, how will the President's proposed community development program specifically address this need for access to financial institutions in underserved communities?

Answer. The proposed Strengthening America's Communities Initiative (SACI) for fiscal year 2007 differs substantially from the fiscal year 2006 SACI envisioned model. Last year, 18 community and economic development programs, which included three of the CDFI Fund's monetary award programs and the Department of Housing and Urban Development's Community Development Block Grant (CDBG) Program, among others, were to be consolidated under the aegis of the Department of Commerce. This proposal was rejected by Congress.

The fiscal year 2007 SACI proposal has the CDBG Program remaining at HUD with revised eligibility criteria; with the exception of the Economic Development Administration, all of the other community and economic development programs have been zeroed out with no new program funding (or substantially reduced funding) and no planned program transfers to HUD or the Department of Commerce.

Thus, the President's proposed fiscal year 2007 budget eliminates the Fund's three monetary award programs and provides $7.8 million to administer only the NMTC Program and the portfolio of existing awards.

Question. Instead of developing a new program to serve this purpose, wouldn't it make more sense to continue one that is successful in meeting these needs?

Answer. While there are numerous community development programs, we believe a more focused SACI program would provide better results to individuals and communities.

QUESTIONS SUBMITTED BY SENATOR RICHARD J. DURBIN

THE NATIONAL DEBT

Question. In my opening statement, I talked briefly about the ramifications of the massive amount of our national debt that is currently held by foreign governments. I alluded to the fact that I wanted to talk a bit more about China in particular. Here's why: according the Associated Press, earlier this week a vice chairman of China's parliament suggested that China should stop buying U.S. Treasuries and should take steps to reduce its holdings in those bonds.

Mr. Secretary, if foreign governments start dumping our debt, won't that destabilize our economy? Won't that destabilize the whole international financial system, which for years now has relied upon American demand to fuel economic growth? What do you think will happen if China starts selling?

Answer. The market for Treasury securities is large, liquid, and deep. China could reduce its rate of accumulating Treasury securities, even substantially, without significantly affecting U.S. financial markets. Despite recent large purchases, China's holdings of Treasury securities are still modest relative to the size of the market.

China's holdings of Treasury securities are estimated to be 7.8 percent of the $4.1 trillion in Treasury securities not held by U.S. Government and Federal Reserve accounts at the end of March.

Chinese investors bought around $98 billion in Treasury securities to their portfolios in the 12 months through March 2006. This is around $400 million per trading day. The daily turnover in the Treasury market is over $500 billion. The Chinese authorities have subsequently stated that they do not plan to change the proportion of U.S. Treasury securities purchased for or held in their foreign reserves.

In this regard, it is notable that net purchases of U.S. securities by all foreign official institutions have declined substantially from the peak year 2004 without exerting a significant influence on U.S. financial markets. Foreign official purchases of long-term reached $236 billion in 2004, before falling to $111 billion in 2005.

THE TAX GAP

Question. Mr. Secretary, it's tax time. As my constituents in Illinois are racing to get their taxes filed before the deadline in a couple of weeks, good people assume that they should pay their taxes because it is the right thing to do, because everyone needs to do their part. But in 2001, an estimated $353 billion in Federal revenues has been lost because some people decided not to pay or to underpay their taxes. That works out to $16 out of every $100 owed. This so-called "tax gap" has likely gotten even worse since 2001.

I don't think that Treasury should make it their mission to track down every last dollar owed to the government, because that is too expensive for the government to do that and would lead to unnecessary hassling of good, honest families that are trying their best to pay their taxes correctly. But $353 billion is a big, big number. We simply have too much debt outstanding to ignore this problem.

What is Treasury going to do to close this gap?

Answer. Our tax gap estimates are derived from a National Research Program (NRP) study of Tax Year 2001 individual income tax returns. The final estimates from that study showed that the gross tax gap was $345 billion while the net tax gap, what's left after enforcement and late payment collection, is $290 billion. This is a voluntary compliance rate of 83.7 percent.

The IRS is committed to increasing the voluntary compliance rate to 85 percent by 2009 and is taking several steps to achieve this goal. First, and perhaps most importantly, the IRS must continue the balanced approach of emphasizing both service and enforcement as the best means to achieve compliance. From a service perspective, the IRS is increasing its focus on electronic tax administration. Large businesses and large tax exempt organizations are already required to e-file. In the most recent filing season, over 70 million individual taxpayers filed their returns electronically. This number rises every year. E-filing is a win-win for both the taxpayer and the IRS. For the taxpayer, there is less chance of error on a return prepared and filed electronically. Plus, the taxpayer receives a quicker refund and a notice that the return has been received. For the IRS, the marginal cost for an e-file return is $0.28 as compared to $2.65 for paper returns. This cost savings allows the IRS to re-direct resources to other areas.

IRS is also putting in place a Taxpayer Assistance Blueprint, an ambitious program designed to improve the overall level of service provided to taxpayers.

From an enforcement perspective, IRS is making good use of the additional $442 million included in the fiscal year 2006 IRS budget for enforcement. It is focusing those resources to maximize the use of each dollar dedicated to enforcement. Specifically, the IRS is:

- —Increasing the coverage of high-risk compliance issues to address the largest portion of the tax gap—the underreporting of tax—across all major compliance programs;
- —Looking at complex high-risk issues in abusive tax avoidance transactions, promoter activities, corporate fraud and aggressive transactions, all resulting in increased corporate and high income audit coverage;
- —Improving our ability to identify compliance risks within the tax exempt communities; and
- —Leveraging our resources with those of the States to address common tax gap issues such as more timely data matching, increased use of State data for IRS enforcement actions and the development of complementary Federal/State enforcement strategies based on the NRP data.

Second, the IRS is trying to find ways to increase third party information reporting. This will allow the IRS to match what a third party reports with what the taxpayer reports on his or her income tax return. The NRP study showed that there is a high correlation between items subject to information reporting systems and taxpayers' reporting of such items on their tax return. Where there is no third party reporting, the compliance rate drops dramatically. As a result, it is incumbent on us to find ways to increase information reporting that will not overly burden either the taxpayer or the entity that is required to report. A good example of this is the proposal in the President's fiscal year 2007 budget to require reporting of aggregate payment card reimbursements made to retail merchants each year. This will allow the IRS to match payments made to retail merchants by a payment card issuer to what the merchant reports as income on his or her income taxes.

Third, we must become more efficient in resource utilization. One of the benefits of the NRP study is that it will allow us to refine our audit selection formulas for several examination classes. In addition, these formulas will help us better calibrate the resources in our various business units so they can operate more efficiently and impose less of a burden on compliant taxpayers. We do not have the resources to return to the high audit rates of the past, but we are using the NRP results to manage our compliance programs more effectively and to design pre-filing activities that help taxpayers comply with the law.

Fourth, we need to change the law in several critical areas. I have already mentioned the legislative proposal in the President's fiscal year 2007 proposed budget to require payment card issuers to report aggregate payments made to retail merchants. There are four other specific legislative proposals included in the President's fiscal year 2007 proposed budget designed to reduce the tax gap also included. They are:

—Clarify the circumstances in which employee leasing companies and their clients can be held jointly liable for Federal employment taxes;
—Expand information reporting to certain payments made by Federal, State and local governments to procure property and services;
—Amend Collection Due Process procedures for employment tax liabilities; and
—Expand to non-income tax returns the requirement that paid return preparers identify themselves on such returns and expand the related penalty provision.

In conclusion, it is safe to say that substantial reductions in the tax gap will only be achieved through fundamental reform and simplification of the tax laws. Achieving significant reductions, absent such reform, would necessitate draconian measures that would involve the IRS in the lives of taxpayers in ways that they would never accept. But we can and will make improvements in the mean time as embodied in our goal of 85 percent compliance by 2009.

WORKER MISCLASSIFICATION

Question. Mr. Secretary, I am concerned with how many contractors currently misclassify their workers as independent contractors rather than employees. Contractors do this so they have no responsibility for the withholding of State, Federal, and social security taxes from employee's paychecks, as that responsibility rests on the worker. These contractors gain an additional competitive advantage in that they avoid all the insurance costs of having employees.

Workers are then paid in cash by the contractor, and all too often, the worker does not declare any income, and does not pay any of the required taxes. The loss of tax revenues has been estimated at over $400 billion per year.

Not only is this misclassification issue shortchanging various State and Federal agencies, and therefore the general public who relies on programs such as social security and Medicare, but it is putting honest contractors and honest workers out of business. The cheating contractors can do business at 24 percent less cost than honest contractors, and honest contractors and workers have a hard time competing for jobs.

In my home State of Illinois, this is a growing problem that has to be addressed immediately. From the years 2001–2004, State of Illinois Audits found that 17.3 percent of Illinois employers audited had misclassified workers as independent contractors. In 2004 alone, the rate of misclassification was 21 percent—67,745 employers statewide and 7,478 in construction. This results in $158 million in lost income tax in Illinois alone in 2004, $18 million of which is lost from the construction sector.

Are you aware of this misclassification issue? If so, are you planning on stepping up enforcement efforts to catch the cheats who game the system at the cost of the general public and honest contractors?

Answer. Misclassification of workers has been a long-standing issue for the Internal Revenue Service (IRS).

There is currently no estimate for the portion of the tax gap attributable to misclassification of workers, however, we believe it is significant. The portion of the tax gap attributable to employment taxes is estimated to be $54 billion. Of the Federal tax gap, $109 billion is attributable to underreporting of business income. Schedule C income, which is subject to little or no third-party reporting or withholding, has a net misreporting percentage of 57.1 percent. This includes the misclassification of workers. As you can surmise, noncompliance with Federal employment tax laws also affects State budgets, State unemployment compensations funds, and Workman's Compensation pools.

It is important to note that the misclassification of workers can run the gamut from employers who are just not aware of their employment tax requirements to intentional noncompliance.

We are planning on stepping up enforcement in this area. The IRS has increased its efforts over the past few years to address the employment tax gap. In fiscal year 2005, 33,748 employment tax returns were examined, an increase of 85 percent compared to fiscal year 2004. Worker classification issues were raised in approximately 2,400 of these examinations. Our work plans for fiscal year 2006 called for increasing employment tax examinations of which approximately 5,800 will address worker classification issues. We are currently increasing our Employment Tax staff which will allow us to perform additional work in the future.

The most egregious worker classification issues are identified through the Employment Tax Worker Classification Examination Program which identifies employers who may be misclassifying workers based on filing of Forms 1099.

Additionally, several other initiatives are in process to address the misclassification issue including:

—The Social Security Administration (SSA) processes corrections to individual earnings records (including situations where earnings are missing from the record). Each week, SSA refers a listing of workers whose earnings have been corrected to the IRS. Some of the employers identified did not file income tax or employment tax returns, and further investigation often reveals the employers paid the workers in cash and also did not file Forms 1099–MISC.

—As the Administrator of the Bank Secrecy Act (BSA), the Financial Crimes Enforcement Network (FinCEN) requires depository institutions and other industries vulnerable to money laundering to file Currency Transaction Reports (CTRs) which report cash transactions of $10,000 or more. Acting as FinCEN's agent under the BSA, these reports are transferred to the IRS Detroit Computer Center and entered into a database called the Currency and Banking Retrieval System (CBRS) which is accessed by FinCEN's law enforcement customers. The IRS also uses FinCEN's BSA data to identify employers who cash large checks in a pattern consistent with using the money to fund employee cash payrolls or pay incorrectly classified workers in cash with little or no accounting thereof. We are increasing the number of audits we conduct based on this information in fiscal year 2007.

We have also used IRS databases to compare wage and labor deductions on business returns with corresponding employment tax return filings. Where the appropriate employment tax returns are not filed, an employment tax examination is considered with a potential worker classification issue. We are planning an increase in these audits in fiscal year 2007 as well.

Workers who feel they should be classified as employees can file Form SS–8, Determination of Worker Status, with the IRS. After an exchange of information with the employer, the IRS makes a determination of worker status and refers the more egregious employers to the field for possible examination. In the past 3 years, workers filed more than 17,000 Forms SS–8. This is a source of worker misclassification cases that we use to identify employers for examination.

We also have misclassification cases under investigation as part of our emphasis on abusive transactions and abusive schemes. As an example, we have identified a corporation that targets other client companies and assists them, for a fee, in converting all their employees to independent contractors.

ENFORCEMENT PRIORITIES

Question. Mr. Secretary, let's discuss the law enforcement that Treasury conducts for a moment. I'm told that a professor and a graduate student from Southern Illinois University were recently targeted for scrutiny by your Office of Foreign Assets Control because they were going to travel to Cuba. I presume that these two individuals were singled out for scrutiny because they also happen to be public officeholders in Illinois, but they were traveling under the Cuba license that SIU has held since 2000.

I don't expect you to have intimate knowledge of every case that Treasury investigates, but I do want to ask you about your enforcement priorities.

Shouldn't Treasury and all of its offices be focusing more on chasing terrorists, and focusing less on harassing pre-approved university travelers to Cuba? Do you believe that Treasury's enforcement resources are being allocated properly right now?

Answer. Please be assured that Treasury allocates its investigatory and enforcement resources according to national security priorities established by the administration. Terrorism is, by everyone's measure, the No. 1 priority. Although OFAC does not comment on open investigations, it is important to keep in mind that each license carries with it specific requirements including who may and may not be included on delegations traveling to Cuba. When OFAC becomes aware of potential violations, it investigates and, if warranted, takes appropriate action to address the situation.

FinCEN's administration of the Bank Secrecy Act also ensures the proactive filing of suspicious activity reports involving potential terrorist financing. As evidenced by FinCEN's $24 million civil money penalty against Arab Bank in August 2005, financial institutions that fail to report suspicious transactions involving potential terrorist financing, which can be so critical to assisting authorities in their efforts to identify and prevent terrorist acts and disrupt terrorist networks, are subject to severe sanctions.

PERFORMANCE MEASURES

Question. I've been interested for quite some time in making sure that we are doing everything we can to stop the flow of financial support that terrorists rely upon in order to wreak their havoc. As you know, last year the GAO completed a report which Senate Finance Committee Chairman Grassley and I requested, along with Senate Homeland Security and Governmental Affairs Chairman Susan Collins, to analyze the effectiveness of U.S. Government efforts to combat these terrorism financial networks. The GAO report made several strong recommendations for where the government should try to improve. I'd like to discuss two of those recommendations today.

First, I think that if we can measure success appropriately then we will target our efforts more efficiently. The GAO report recommended that strong performance measures be put in place so that we can better assess how well we are doing in disrupting terror financing. I recognize that this is not an easy thing to measure, but nonetheless we need some benchmarks by which we can judge our progress in rooting out these money networks.

After I wrote to the Treasury to ask about this last fall, I received a response from an Assistant Secretary a couple of weeks ago that stated that the Office of Foreign Assets Control had finished developing performance measures . . . but then he gave no indication of what those measures were.

How do you plan to measure your success in disrupting the financing of terrorism?

Answer. OFAC will measure the impact of Terrorism, Proliferators of Weapons of Mass Destruction, and Narco-Trafficking sanctions programs as high, medium or low impact. For this outcome performance measure, developed in conjunction with Treasury's Office of Strategic Planning and submitted in connection with the Performance and Accountability Report, impact is measured by their effectiveness in identifying, exposing, isolating, impeding, and/or incapacitating the targets (micro and macro) of the sanctions program as demonstrated by, but not limited to, the presence or absence of the following, types of actions:

—Facilitation of law enforcement activity (domestic or foreign);
—Facilitation of intelligence collection by intelligence community;
—Response by the international financial community—voluntary compliance;
—Response by the international business community—voluntary compliance;
—Response by the targets (e.g. attempts to evade sanctions, attempts to restructure organization, etc.);
—Response by foreign governments;
—Response by other government agencies;
—Effectiveness of public exposure;
—Deterrent effect of threat of further action; and
—Impact on targeted network.

AGENCY COOPERATION

Question. The GAO report also criticized Treasury, State, Justice, and other governmental departments for not working in a more coordinated fashion to fight terrorism funding. The report suggested that Treasury does not accept the idea that the State Department should lead this fight, nor does Treasury accept the procedures recommended by the State-led Terrorist Finance Working Group in delivering training and technical assistance abroad.

In the departmental responses to the GAO, Treasury, State, and the other agencies seemed to reject the idea that there was a problem in coordinating our efforts to monitor, track, and eliminate sources of terrorist financing. Please explain to me how Treasury and the other agencies have improved their coordination in these areas and in implementing the procedures recommended by the State-led Terrorist Finance Working Group in delivering training and technical assistance abroad.

Answer. The fight against terrorist financing is among Treasury's highest priorities. Treasury works closely with our partners in the interagency community and our counterparts abroad to ensure that vulnerabilities in the international financial system are closed to terrorists and terrorist financing networks are disrupted and dismantled. Though there is always more that can and must be accomplished, we believe that the U.S. Government's achievements in the fight against terrorist financing have been considerable, as reflected by the "A−" issued to the U.S. Government in the area of terrorist financing in the 9/11 Commission's "Final Report Card on 9/11 Commission Recommendations." The positive assessment is the result of all agencies within the U.S. Government working together and cooperating closely.

The referenced GAO report does not focus on the fight against terrorism funding broadly, but rather is limited to an examination of interagency coordination on the provision of technical assistance related to terrorist financing to certain priority countries. This is a small, though vitally important, component of the U.S. Government's broad counter-terrorist financing efforts. The GAO correctly notes that there can be improvement in the way that the State Department—which has the lead in the provision of technical assistance—and agencies such as the Treasury Department—which has technical expertise in this area—interact and coordinate with each other. Since the publication of the GAO report, considerable effort is underway, both within Treasury and throughout the interagency community, to improve this process. For example, under State Department leadership, the Training and Assistance Sub Group (TASG)—a senior-level interagency group dedicated to overseeing the provision of counterterrorism technical assistance—has been reinvigorated in order to provide enhanced oversight and guidance to the State-led Terrorist Finance Working Group (TFWG). Moreover, more senior representatives have been assigned to the TFWG itself to ensure that it is functioning efficiently. We will continue to work both within Treasury and through the interagency community to improve the coordination and delivery of technical assistance in this vital area.

SUBCOMMITTEE RECESS

Senator BOND. I thank you for coming here today, and you can be sure that we will be continuing to work with you, following your activities, helping where we can, and commenting where needed.

With that, my sincere thanks to the witnesses. The hearing is recessed.

Mr. LEVEY. Thank you, Mr. Chairman.

[Whereupon, at 11:03 a.m., Thursday, April 6, the subcommittee was recessed, to reconvene subject to the call of the Chair.]