



REPORT BY THE U.S.

General Accounting Office

Costs Of FBI Undercover Operations

During fiscal years 1979 through 1981, the FBI spent about \$10.8 million for identified undercover operation expenses. This amount excludes the costs of salaries for undercover agents which could not be determined from available records. It also excludes the costs, still being incurred, of litigating and settling claims and lawsuits resulting from undercover operations. Six lawsuits involving claims of \$18.4 million had been settled for about \$1.1 million as of December 31, 1982. At that date, 16 claims for about \$333.4 million were pending.

with the Subcommittee on Civil
Constitutional Rights, House Committee
Member, GAO did not pursue access
to undercover cost and investigative data
because officials considered sensitive.
Presently, GAO could neither determine
the cost of undercover operations, nor
presently verify the accuracy of the
information provided by the FBI.

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WASHINGTON, D.C. 20548

GENERAL GOVERNMENT
DIVISION

B-210744

The Honorable Don Edwards
Chairman, Subcommittee on
Civil and Constitutional
Rights
Committee on the Judiciary
House of Representatives

NCJRS

JUN 20 1983

ACQUISITIONS

Dear Mr. Chairman:

This report is in response to your June 10, 1982, request that we determine the costs, both direct and indirect, associated with the Federal Bureau of Investigation's (FBI's) undercover operations. As agreed with you and your staff, we did not pursue access to certain undercover cost and investigative data that FBI officials considered sensitive. Consequently, we could not determine the total cost of undercover operations, nor could we independently verify the accuracy of the cost data provided by the FBI.

Even with complete access to FBI data, determining the total cost of undercover operations would have been difficult. During fiscal years 1979 through 1981, the FBI spent about \$10.8 million which is identifiable as undercover operation expenses. However, personnel salaries and the costs of litigation and settlement of lawsuits resulting from undercover operations are not included in this figure. Personnel salaries are accumulated by the type of crime being investigated, such as white collar or organized crime, not by undercover operation. Litigation and settlement costs are still being incurred and their total will not be known for several years. As of December 31, 1982, the Government had to pay settlements on only one operation--Frontload--and these totalled about \$1.1 million.

The settlement costs from operation Frontload resulted from an agreement between the Attorney General and a third-party corporation which was completed after the undercover operation was over. Under the agreement, the Department of Justice assumed responsibility for the litigation and settlement of several lawsuits that had already been filed against the corporation by advising the corporation to implead the United States as a defendant. The Department also advised the corporation that adverse judgments or compromise settlements could be paid by the United States, absent improper or illegal conduct by the corporation's employees.

The FBI also has entered into agreements during undercover operations which contained provisions describing the liability of the parties involved. FBI officials told us that these agreements are used infrequently and usually to help obtain a third party's cooperation for the operation. In some of the agreements the FBI assumed liability for actions other than the negligent acts of its employees, which the Government normally would be liable for under existing law. One of these did not contain language to limit the amount of the Government's liability as required by Supreme Court and Comptroller General decisions, as well as current FBI policies and procedures. This agreement covered one of the FBI's first undercover operations, but FBI officials told us they did not know why the agreement omitted a limit on the amount of the Government's liability. They also told us that no costs have been incurred as a result of the agreement, and none are anticipated. All similar subsequent agreements that the FBI provided us contained language limiting the amount of the Government's liability. However, because of this exception, we are recommending in a separate letter to the Director, FBI, that he ensure that all future agreements contain such language.

We also attempted to evaluate the effectiveness of FBI controls over the expenditure of funds in undercover operations. The guidelines the FBI has established to control funding for undercover operations appear to conform to its GAO-approved accounting system design. However, our limited access to detailed cost information prevented us from assessing how effectively the guidelines were being implemented. In any case, the propriety of undercover operation expenses usually will depend on the integrity of the undercover agent.

Additional details are provided below.

OBJECTIVES, SCOPE, AND METHODOLGY

As requested, we collected information on the funding of FBI undercover operations for fiscal years 1979, 1980, and 1981. Specifically, to the extent feasible, we

--determined the costs of FBI undercover operations including both direct and indirect costs;

--determined the costs of specific Group I undercover operations which were completed and did not have litigation pending;

- identified the nature and extent of legal claims and settlements resulting from FBI undercover operations;
- determined the nature and extent of agreements describing liability in certain undercover operations;
- traced the financial arrangements of five undercover operations; and
- reviewed the FBI's guidelines for funding undercover operations.

We interviewed FBI officials and obtained and reviewed various documents provided by them concerning the above objectives. As stated earlier, we did not pursue access to certain undercover cost and investigative data that FBI officials considered sensitive.

TYPES AND EXTENT OF UNDERCOVER OPERATIONS

FBI officials told us that an undercover operation is one of many techniques that can be used to investigate a specific type of crime. In an undercover operation, FBI agents might assume a personal or business identity in order to obtain evidence of illegal acts. FBI officials have testified that undercover operations are usually targeted at exposing white collar crime, public corruption, and organized crime--types of crime that are more difficult to detect using other investigative techniques. FBI officials characterized these crimes as being rarely documented or witnessed by outsiders; both parties to a transaction may have a criminal interest in concealing the relationship. In each case they said the general public is the unknowing victim.

The FBI classifies undercover operations into two categories--Group I and Group II. Group I operations are the larger, more complex ones, and all Group I expenditures are controlled by FBI headquarters. Group II operations are usually small, more localized operations and are controlled by one of the 59 FBI field offices nationwide. Total expenses for Group II operations cannot exceed \$1,500 without approval from headquarters.

Funding for undercover operations has grown from \$3.0 million in fiscal year 1978 to \$6.6 million for fiscal year 1983. As mentioned previously, these amounts do not include the salary costs of personnel involved in the operations or the costs to litigate and settle claims and lawsuits resulting from the operations. For fiscal years 1979 through 1981, the FBI ran 187 Group I undercover operations and 612 Group II's.

THE COSTS OF MOST UNDERCOVER
ACTIVITIES ARE IDENTIFIABLE

For fiscal years 1979 through 1981, FBI officials told us that about \$10.8 million was spent for undercover operations. A breakdown of these expenditures by group of undercover operation was unavailable for 1979. For fiscal years 1980 and 1981 combined, Group I operations cost about \$6.4 million and Group II operations cost about \$0.4 million. The amount of funds spent for selected Group I operations is shown in appendix I.

These funds cover most aspects of undercover operations. The activities funded include travel, services of informants, the display of a large amount of cash (show money) to reinforce an agent's role, enticement buys to establish an agent's credibility or to encourage a subject to supply additional property or information, rental of equipment, rental of apartments or offices, and entertainment expenses. Also included are indirect expenses, such as transportation and lodging costs incurred by agents during the selection process for potential undercover operation participants. FBI officials told us that expenditures for these indirect activities were \$40,000 or less annually for fiscal years 1979 through 1981.

Costs for specific undercover activities are not accumulated by the FBI. However, they can be derived from existing records. For example, the FBI is required by its authorizing legislation to audit those undercover operations that result in revenues in excess of \$50,000. When these audits are performed, a breakdown of costs incurred is prepared by specific activity. The FBI provided us eight reports on audits completed as of September 30, 1982. These audits included operations with expenses of about \$1.3 million. A combined schedule of the costs for the eight operations showed that three activities resulted in about 80 percent of the expenditures: (1) funding of business operations, such as cost of goods sold and bad debts; (2) payments to informants and payoffs; and (3) daily expenses for

travel, food, lodging, and entertainment. Appendix II shows the composite percentage of total costs represented by each activity for the eight audits. Without complete access to detailed cost records, however, we could not determine the extent to which these costs may be representative of all undercover operations.

PERSONNEL COSTS UNKNOWN

Salaries paid to personnel involved in undercover operations are not accounted for by undercover operation. FBI officials told us that because undercover work is an investigative technique that can be applied to many criminal case situations, the FBI does not attempt to account for undercover personnel costs separately.

The FBI tracks personnel time by type of crime being investigated, such as white collar or organized crime, rather than by the techniques used during the investigation, such as a wiretap or an undercover operation. Thus, the amount of personnel salaries expended for undercover operations was not readily available. Without access to the complete investigative files we could not determine whether staff time devoted to a particular undercover operation could be estimated. FBI officials told us that making such estimates would be difficult.

LITIGATION AND SETTLEMENT
COSTS YET TO BE DETERMINED

As of December 31, 1982, 29 lawsuits with claims of about \$424.3 million had been filed against the Federal Government involving eight FBI undercover operations, including ABSCAM. The Government had settled six of these lawsuits, all involving operation Frontload, at a total cost of about \$1.1 million. The original claims for these suits totalled about \$18.4 million. In addition, seven other lawsuits with claims totalling about \$72.6 million were dismissed. Thus, as of December 31, 1982, 16 claims for about \$333.4 million were pending. The Department of Justice's Civil Division is representing the Government in these lawsuits. The number of claims and settlements arising from FBI undercover activities is summarized below:

<u>Name of operation</u>	<u>Number and status of civil suits</u>	<u>Monetary damages claimed</u>	<u>Settlements</u>
ABSCAM	6 pending 1 dismissed	\$205,317,815 1,500,000	\$ - -
WHITEWASH	1 pending	375,000	-
SPEAKEASY	2 pending	20,166,158	-
FRONTLOAD	6 settled 5 pending 3 dismissed	18,362,183 101,980,508 42,100,000	<u>a/</u> 1,130,138 - -
TURNKEY	1 dismissed	6,000,000	-
CLEVELAND	1 dismissed	23,000,000	-
RE-COUPÉ	2 pending	5,526,944	-
WFO GAMBLING	<u>1 dismissed</u>	<u>1,574</u>	-
Total	<u>29 lawsuits</u>	<u>\$424,330,182</u>	<u>\$1,130,138</u>

a/Includes \$200,905 for the cooperating corporation's legal costs on all the Frontload lawsuits.

The majority of the pending lawsuits involve (1) individuals charging the Government with violating their constitutional rights or (2) businesses seeking reimbursement for losses and legal costs resulting from their involvement in the FBI's undercover operations. For example, some of the lawsuits regarding the ABSCAM operation claim that the FBI entrapped high-level public officials and thus violated their constitutional rights. In a number of other lawsuits, private businesses allege that losses were incurred because FBI-operated front-companies defrauded them in business dealings. Other lawsuits pending involve charges of unprofessional conduct by FBI agents and monetary losses incurred by individuals while cooperating with the FBI.

AGREEMENTS DESCRIBING LIABILITY IN
UNDERCOVER OPERATIONS SHOULD LIMIT
THE GOVERNMENT'S LIABILITY

For a few undercover operations, the FBI entered into agreements with third parties which specified the conditions under which each would be liable for actions taken during the operation. Usually these agreements stated that the Federal Government was liable only for any negligent acts by the FBI. However, three of the eight agreements we reviewed clearly extended the scope of the Government's liability beyond FBI negligence. One of these, from an undercover operation which began in 1978, did not establish a limit on the amount of the Government's potential liability. The Supreme Court and the Comptroller General have ruled that, without express statutory authority to the contrary, agencies entering into such agreements must limit the amount of the Government's potential liability in order not to violate the provisions of the Anti-deficiency Act (31 U.S.C. 1341). FBI officials provided us with no reason as to why this one agreement contained no liability limit, but they told us that no payments have been made as a result of the agreement.

Agreements describing liability
are used infrequently

FBI officials told us that agreements describing the scope of each party's liability were entered into for only seven Group I undercover operations for fiscal years 1979 through 1981. They provided us copies of all seven and an additional agreement from a 1978 operation which was one of the FBI's first Group I operations. They also told us that these agreements were used only when they were absolutely necessary to achieve an undercover operation objective. The formats of the agreements varied because they were tailored to each specific operation.

The agreements usually established guidelines which indicated what the FBI expected from the third party, the scope of the party's and the FBI's liabilities, the need for confidentiality, and the duration of the agreement. Examples of provisions from several agreements follow:

- "The FBI agrees to take reasonable precautions to protect the physical safety of the [companies'] personnel and management, [the owner], and their families from danger arising from the FBI's investigations."

--"The [third party] shall manage, administer, and direct the operations of the companies * * * and * * * cooperate fully in investigative activities * * * as requested by the [FBI]."

--"The liability for any negligent acts of FBI employees will be borne by the FBI. Liability for any negligent or willful acts of [the third party], which acts were undertaken without prior express approval of the FBI, are the sole responsibility of [the third party]. However, [the third party] does not waive any rights or claims to which it is entitled under the Federal Tort Claims Act [(28 U.S.C. 2671 et seq.)]."

Three agreements expand the scope of the Government's liability

Five of the eight agreements we reviewed stated that the Government would be liable for third-party losses resulting from FBI negligence. This is nothing more than the Government would normally be liable for under the Tort Claims Act. Two of the other three agreements were negotiated during the undercover operation and contain statements indemnifying the third party's losses whether or not these losses are due to FBI negligence. One of these two limits the Government's liability as required by Supreme Court and Comptroller General decisions, the other does not. The third agreement involved operation Frontload and, as described previously, was entered into only after the undercover operation was finished and several lawsuits had been filed. It advised the third party corporation to implead the Government as a defendant, after which the Government would assume responsibility for the costs of litigation and settlement, absent improper or illegal conduct by the corporation's employees.

Pertinent sections of the two agreements which were negotiated during undercover operations are as follows:

- (1) "In consideration thereof, the FBI agrees to indemnify and hold harmless [the third party] from and against any and all liability, suit, losses, damages, and expenses * * * in the amount of \$500,000 for any damage or loss resulting to [the third party] as a result of [its] cooperation in this matter."

- (2) "The FBI agrees to indemnify [the third party] from any judgment, fine, assessment, or other expense, including attorneys' fees, of any litigation or proceeding in which damages or other relief are claimed by reason of acts by personnel of the FBI, the investigative nature of the venture, or the involvement or participation of the FBI therein."

The first agreement establishes a maximum liability limit of \$500,000 that the FBI will pay the third party for losses, damages, and other expenses. The second agreement appears to indemnify the third party for an indefinite amount of judgments and other expenses resulting from the investigation. This creates an unlimited contingent or potential liability that may become an actual liability in the event that losses occur.

A former Attorney General entered into the agreement for operation Frontload because he appreciated the third-party corporation's cooperation and he wanted to ensure such assistance in the future. This is the only agreement under which the Government has made any payments. The agreement applied only to the lawsuits pending at the time of the agreement, which were about \$162.4 million. As of December 31, 1982, the Government had paid about \$1.1 million under this agreement, and pending lawsuits totalled about \$102.0 million.

All agreements expanding the scope of the Government's liability must limit the amount of liability

FBI officials were uncertain why one agreement contained no language limiting the amount of the Government's liability, especially since FBI and Government policies require such limits. That particular agreement concerned one of the early FBI undercover operations, and all subsequent agreements have included limits.

FBI policies and procedures require that all requests for agreements be reviewed by FBI headquarters and meet the following criteria:

- The agreement must have a finite liability.
- The agreement must be determined to be in the interest of the Government.

--Reimbursement made under the agreement must be properly chargeable to the specific appropriation from which the funds are taken.

--Funds to cover the total potential liability must be available in the current year's appropriations.

If approved, the agreements are executed by the FBI's Contract Review Unit with assistance from legal counsel. Unit officials told us they notify the Budget and Accounting Section of the amount of any contingent liabilities.

The United States Supreme Court and the Comptroller General have issued decisions which state that, absent express statutory authority to the contrary, the Government may not enter into an agreement to indemnify where the amount of the Government's liability is indefinite or potentially unlimited. Such an agreement violates the Antideficiency Act because the funds appropriated would be insufficient to cover the contingent liability. For an agreement to be in compliance with the act, the Comptroller General has stated that the contingent liability must be limited to available appropriations. The limitation can be established in either of two ways:

--the agreement could simply state that the Government's liability to the third party is limited to a mutually agreed upon dollar amount which does not exceed available appropriations, or

--the agreement could state that indemnity payments will not exceed appropriations available at the time of the third-party's losses. Further, nothing in the agreement will imply that the Congress would appropriate additional funds to meet any deficiencies.

We believe that the FBI should ensure that all future agreements which expand the scope of the Government's liability should also limit the amount to comply with the provisions of the Antideficiency Act.

FBI GUIDELINES TO CONTROL
UNDERCOVER OPERATION FUNDING
APPEAR ADEQUATE

FBI guidelines for controlling funding of undercover operations conform to the FBI's accounting system design, which GAO approved in April 1977. However, we were unable to determine to what extent these guidelines are actually followed because of our limited access to detailed cost records. In any case, because of the nature of undercover operations, the accuracy and propriety of expenditures reported is usually dependent on the integrity of the undercover agent.

Procedures for controlling the funding of undercover operations are set forth in the FBI's "Funding Guide for Undercover Operations," issued in October 1979. The procedures range from requiring headquarters approval for certain undercover operation expenditures to requiring quarterly financial audits of designated ongoing operations. The funding guide provides far more detail than that provided in the FBI's approved accounting system design package. Nothing in the guide conflicts with the approved design.

We attempted to trace the detailed transactions for five undercover operations to assess the FBI's implementation of its funding guidelines. However, FBI officials would provide us only summary level information, such as funding approval dates and accounting record excerpts showing aggregate advances and disbursements. As agreed with your office, we did not pursue access to the detailed records. Consequently, we were unable to independently evaluate the extent to which the funding guidelines were followed.

For example, FBI officials provided us funding data for an undercover operation called "Goldcon." This operation was aimed at identifying high-level con men involved in creating multimillion dollar fraud schemes. The FBI summary documents indicated that:

- The Miami field office requested funding for the undercover operation in October 1978.
- FBI headquarters initially approved about \$47,000 in December 1978 and advanced this amount to the field office over the next 4 months.

- Headquarters approved and advanced additional funds in 1979 and 1980 totalling about \$122,000.
- The Miami field office spent about \$154,000 during the operation for payments to "various establishments" which FBI officials told us included informants and businesses.
- The operation was ended in March 1980, and the field office returned the \$15,000 it had not used (total advances of \$169,000, less total expenses of \$154,000).

To independently verify these transactions, we needed access to copies of (1) correspondence between FBI field and headquarters offices, such as funding request and approval forms and (2) the undercover agents' detailed expense vouchers.

In this operation, as well as in others, the ultimate funding control rests with the undercover agent. Typical accounting controls, such as separation of duties and documented receipts are frequently impractical because of the sensitive and confidential nature of undercover operations. The accuracy and propriety of expenditures reported is usually dependent on the integrity of one person, the undercover agent.

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As arranged with your office, we plan no further distribution of this report until 30 days from its issue date, unless you publicly announce its contents earlier. At that time we will send copies to the Attorney General and other interested parties. Copies will be made available to others upon request.

Sincerely yours,

W. J. Anderson

William J. Anderson
Director

COSTS OF SELECTED GROUP I
UNDERCOVER OPERATIONS
(note a)

<u>Field offices</u>	<u>Case name</u>	<u>Expenditures</u>
Baltimore	Cleanstreets	\$ 43,674.06
Baltimore	Bucknite	80,808.68
Detroit	Bandaid	9,761.62
Jackson	Go-Kart	3,549.07
Los Angeles	Medussa	53,874.54
Louisville	Narcar	11,652.93
Miami	Goldcon	153,815.38
Minneapolis	Minop	4,656.16
Minneapolis	Pesto	310.61
Brooklyn-Queens	Brigantine	23,604.76
New York	Applecure	12,227.00
New York	(b)	48,101.47
Omaha	Eggroll	88,791.00
Philadelphia	Goldwing	38,066.75
Phoenix	Petard	64,512.68
Pittsburgh	Three Rivers	16,416.54
Sacramento	Overdue	95,714.95
San Francisco	Calsound	29,766.43
Savannah	Seagull	22,772.06
Washington	Weduc	37,732.90
Total	<u>20 Operations</u>	<u>\$839,809.59</u>

a/This listing was provided by the FBI and we could not independently verify its accuracy. It includes only cases opened during fiscal years 1979 through 1981 and closed by the end of fiscal year 1982. Closed undercover operations are those which had been completed and did not have outstanding litigation. The FBI provided us only total cost information on open operations with no detailed cost breakdowns by individual operation.

b/This operation was named for an individual. We agreed with FBI officials not to release the name.

PERCENTAGE BREAKDOWN OF EXPENDITURES AND
REVENUES FOR EIGHT UNDERCOVER OPERATIONS
(note a)

<u>Expenditures</u>	<u>Percentage</u>
Operational purchases associated with undercover businesses (such as cost of goods sold and bad debts)	43
Payments to informants, payoffs, kickbacks, etc.	28
Travel, food, lodging, and entertainment	11
Apartment/office rental	6
Automobile expense	5
Office supplies/equipment rental	2
Fixed asset purchases	1
Telephone and utility expenses	1
Miscellaneous	<u>3</u>
Total	<u>100</u>
<u>Revenues</u>	
FBI appropriations	58
Income from operations	41
Interest income	11
Other	1
Less: Interest income returned to the U.S. Treasury	<u>(11)</u>
Total	<u>100</u>

a/These figures are based on data provided by the FBI from the following undercover operations: Applecore, Brigantine, Budmash, Goldwing, Lil Rex, Petard, Weduc, and Whitewash.

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