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Review of the Transportation Security Administration (TSA) Collection of Aviation Security Service Fees



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Preface

The Department of Homeland Security (DHS) Office of Inspector General (OIG) was established by the Homeland Security Act of 2002 (*Public Law 107-296*) by amendment to the Inspector General Act of 1978. This is one of a series of audit, inspection, and special reports prepared as part of our oversight responsibilities to promote economy, efficiency, and effectiveness within the department.

This report assesses the strengths and weaknesses of the Transportation Security Administration's collection of passenger security and air carrier infrastructure fee payments. It is based on interviews with employees and officials of relevant agencies and institutions, direct observations, and a review of applicable documents.

The recommendations herein have been developed to the best knowledge available to our office, and have been discussed in draft with those responsible for implementation. It is our hope that this report will result in more effective, efficient, and economical operations. We express our appreciation to all of those who contributed to the preparation of this report.

A handwritten signature in cursive script that reads "Richard L. Skinner".

Richard L. Skinner
Inspector General

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Abbreviations

ASIF	Aviation Security Infrastructure Fee
ATA	Air Transport Association
ATSA	Aviation and Transportation Security Act
CBP	U.S. Customs and Border Protection
CFR	Code of Federal Regulations
CPA	Certified Public Accountant
CY	Calendar Year
DMS	Docket Management System
DOT	Department of Transportation
FY	Fiscal Year
GAO	Government Accountability Office
GSC	Ground Security Coordinator
LEO	Law Enforcement Officer
OIG	Office of Inspector General
TSA	Transportation Security Administration

*Department of Homeland Security
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Executive Summary

The Aviation and Transportation Security Act (ATSA), Public Law 107-71, established passenger and air carrier¹ security fees to reimburse Transportation Security Administration (TSA) for its costs of providing air passenger and property security services at the nation's airports. ATSA required TSA to impose a uniform passenger civil aviation security service fee (passenger security fee) on passengers of domestic and foreign air carriers whose flights originated in the United States. ATSA also allowed TSA to impose an Aviation Security Infrastructure Fee (ASIF)² on air carriers. During fiscal year (FY) 2004, TSA collected \$1.6 billion in passenger security fees and \$283 million in ASIF.

We evaluated TSA monitoring controls and oversight of passenger security fees to determine if the air carriers adequately identified, collected, and remitted these fees to TSA. At the request of TSA, we also evaluated CY 2000 passenger and property screening expenses reported by air carriers to determine the accuracy of the costs reported and if the costing methodologies used by these air carriers provided a fair and reasonable basis for computing the air carriers' ASIF costs to TSA. See Appendix A of this report for additional details on the purpose, scope, and methodology of the audit.

For passenger security fees, TSA had not developed adequate controls and had not conducted audits to oversee the accuracy of the air carriers' collection and remittance practices until late 2004. As a result, TSA did not know that the three air carriers reviewed did not identify, collect, and remit \$2.7 million in fees for the period covered during the audit. We recommend that TSA (i) collect the \$2.7 million in unpaid fee amounts identified in this report and validate that all air carriers not covered by this audit have accurately collected and remitted all passenger security fees, (ii) increase the number of annual audits, and (iii) enforce its interim final rule on future tickets.

¹ Although "airline" is the normal term used by the general public, this report uses the term "air carrier" as established in ATSA.

² 49 C.F.R. Parts 1510 "Imposition and Collection of Passenger Civil Aviation Security Service Fees" and 1511 "Aviation Security Infrastructure Fees and Assumption of Civil Security Functions and Responsibilities"

For the CY 2000 passenger and property screening expenses, serious problems existed with data accuracy, integrity, and reliability. For example, expenses reported to TSA in the air carriers' Appendix A "*Calendar Year 2000 Costs Paid for Passenger and Property Screening*"³ excluded footnoted items totaling \$9.2 million⁴. Of this amount, \$4.8 million⁵ represented the expenses of two sampled air carriers for indirect costs related to law enforcement and rent charges. (Five other air carriers outside our sample excluded law enforcement and rent charges totaling \$4.5 million.) TSA became aware of air carrier disagreements regarding the costs to be reported and of overall data integrity and reliability problems in 2002 when it began receiving Appendix A submissions. While TSA required air carriers to submit independent audits of the Appendix A submissions, those audits generally resulted in auditors being unable to validate the reliability of the submissions.

Based on our audit work, we estimate that unremitted ASIF amounts from program inception to March 2005, including the air carrier disputed footnoted \$9.2 million in Appendix A, totaled approximately \$49 million. During our audit, the Government Accountability Office (GAO), as mandated by the 2005 Homeland Security Appropriation Act, initiated a review to evaluate the overall reasonableness of the \$319 million⁶ ASIF funds used by TSA as the maximum reimbursement from the air carriers. Their report⁷ estimated that ASIF collections should be between \$425 million and \$471 million. TSA agreed to consider GAO's analysis and estimates in determining the limitation on aggregate air carrier security infrastructure fees. Our report is consistent with GAO's findings and highlights similar concerns with the integrity and reliability of the CY 2000 expenses reported by the air carriers in FY 2002.

We are recommending that TSA (i) resolve outstanding issues raised by the air carriers or otherwise referenced in this report; (ii) determine a fair and reasonable aggregate ASIF amount based on the resolution of outstanding air carrier issues, the results of this audit, and GAO's analyses and estimates, and collect fees where applicable; (iii) establish guidelines to determine the per air carrier ASIF amount; and (iv) initiate enforcement actions against air carriers that fail to remit the ASIF amounts mandated by ATSA.

See Appendix B for a complete text of management's response to the draft report.

³ Appendix A is a document developed by TSA that required air carriers to identify passenger and property screening cost for CY 2000.

⁴ During our September 15, 2005 exit conference, TSA informed us that one air carrier recently increased its footnoted amount by \$40,000 thus making the total footnoted amount \$9,270,149.

⁵ Reported as footnotes to the Appendix A.

⁶ The \$319 million represented the sum of all Appendix A documents submitted by air carriers in operation in CY 2000. This amount served as the aggregate of ASIF to be reimbursed to TSA by the air carrier industry.

⁷ *Review of the Air Carriers' Year 2000 Passenger and Property Screening Costs*, issued April 18, 2005

Background

On November 19, 2001, Congress enacted ATSA, Public Law 107-71, creating TSA and requiring it to assume responsibility for security screening at commercial airports in the United States. To pay for costs of providing civil aviation security services, ATSA required TSA to impose uniform security service fees on passengers enplaning on flights originating from United States airports and at the discretion of TSA, impose the ASIF on domestic and foreign air carriers who previously paid for security services at United States airports during CY 2000. See Appendix C for a chronology of events relating to both fees.

Passenger Civil Aviation Security Service Fee (Passenger Security Fee)

On December 31, 2001, based on ATSA as codified in Title 49⁸, TSA issued an interim final rule requiring air carriers to impose a \$2.50 per enplanement security service fee on passengers of flights originating from United States airports. The interim final rule required domestic air carriers and foreign air carriers to collect passenger security fees on air transportation sold on or after February 1, 2002. TSA established the maximum fee as \$5.00 or two enplanements per one-way trip and \$10.00 or four enplanements per round trip. The passenger security fee also applied to passengers using frequent flyer awards for air transportation, but not to other non-revenue passengers such as air carrier personnel.

The interim final rule implemented ATSA requirements that all air carriers remit the total fees imposed during each month to TSA by the last calendar day of the following month. The rule made air carriers responsible for paying fees imposed on, but not collected from, passengers with its monthly remittance to TSA. The rule also allowed air carriers to retain any interest accrued on the principal between the collection and remittance but prohibited the air carriers from retaining any portion of the principal to offset the costs of collecting, handling, or remitting the passenger security fees.

TSA's rule required air carriers to establish and maintain accounting systems to account for passenger security fees imposed, collected, refunded, and remitted and to identify the airports where the passengers enplaned. TSA also required that air carriers collecting passenger security fees from more than 50,000 passengers annually provide for annual audits of passenger security fee accounts and activities by an independent certified public accountant (CPA). Further, TSA required that such audits opine on the fairness and reasonableness of the air carriers' procedures for collecting, holding, and

⁸ 49 Code of Federal Regulations (CFR), Part 1510,

remitting the passenger security fees and address whether the quarterly reports fairly present the net transactions in the passenger security fee accounts.

On January 25, 2002, Docket TSA-2001-11120-10 (Docket 10)⁹ provided further guidance on how to assess the passenger security fee for one-way trips and round-trips based on hypothetical travel itineraries submitted by the Air Transport Association (ATA) in Docket 6, dated January 8, 2002. In response to Docket 10, ATA stated in Docket 32, dated March 1, 2002, that ATA and its 26 air carrier members believed that the definitions and limitations in the interim final rule were inconsistent with ATSA. Additionally, they believed ATSA and the interim final rule did not support the conclusions in Docket 10. While ATA requested further discussions with TSA regarding this issue, no such discussions have been held and TSA has not issued a final rule. During our exit conference in September 2005, TSA officials told the OIG they do not intend to issue a final rule until more audits are completed. TSA officials also stated they are waiting for more audits to be completed so that they can address all identified problems in the final rule. For details on passenger security fee assessment differences between the Docket 10 guidance and air carriers' practices, see Appendix F. These differences directly affected the results of this report because we used Docket 10 as the governing criteria.

In FY 2003, 174 air carriers collected and remitted about \$1.2 billion in passenger security fees. This amount excluded fees that would have been applicable from June 1, 2003 through September 30, 2003 during a Congressionally-mandated fee suspension period. In FY 2004, 177 air carriers collected and remitted passenger security fees of over \$1.6 billion.

Aviation Security Infrastructure Fee (ASIF)

To the extent that the passenger security fees were insufficient to pay for civil aviation security services, ATSA authorized TSA to impose an infrastructure fee on domestic and foreign air carriers. Per 49 CFR Part 1511, TSA imposed the ASIF on air carriers engaged in air transportation effective February 18, 2002. ATSA limited the ASIF amount for each fiscal year to the aggregate amount of passengers and property screening costs air carriers paid in calendar year CY 2000. To determine the cost of passengers and property screening in CY 2000, TSA required all air carriers who paid for these screening costs to complete and submit an Appendix A by May 18, 2002. TSA also required the air carriers to submit independent audits of those submissions by July 1, 2002, but later extended the deadline to December 31, 2002.

⁹ A docket is an official public record, which can give guidance about proposed and final regulations. For the passenger fee the prefix is 11120 and for ASIF the prefix is 11334. Hereafter, dockets will only be referred to by their short form name, i.e. Docket 10 or 6 etc.

Since February 2002, each air carrier paid its ASIF cost based on its respective CY 2000 passenger and property screening cost information. However, because the per air carrier fee limit through FY 2004 was based on each air carrier's screening costs in CY 2000, air carriers that did not engage in air transportation in CY 2000 were not subject to the ASIF until 2005. Beginning FY 2005, ATSA allowed TSA to determine the per air carrier fee based on the air carrier's respective market share or any other appropriate measurement for each air carrier, while still limiting the total ASIF to the aggregate amount of passenger and property screening costs in CY 2000. On October 1, 2004, TSA notified air carriers that the ASIF amount previously imposed on each air carrier would continue until further notice. As of March 2005, TSA had not reevaluated the per air carrier fees. TSA officials stated during our September 2005 exit conference that they were waiting for our audit report results before continuing with their analysis of ASIF distribution. They further stated they received 16 different proposals regarding "market share" distribution from the air carriers.

TSA required air carriers to pay the CY 2000 ASIF amounts in monthly increments of 8.333 percent, due the last calendar day of each month for the prior month's collected fees. In FY 2003, 167 air carriers paid an ASIF to TSA in excess of \$253 million. As a result of the temporary fee suspension period, this amount excluded fees that would have been applicable from June 1, 2003 to September 30, 2003. In FY 2004, 148 air carriers paid an ASIF of over \$283 million.

Results of Audit

TSA Monitoring Controls and Oversight of Passenger Security Fees

TSA did not receive all of the passenger security fees due from the air carriers because it had not developed adequate controls and, until late 2004, had not conducted audits to oversee the accuracy of the air carriers' collection and remittance practices. TSA monitored air carrier payments, but its oversight did not include reviews or audits of the payments to ensure they were accurate and in compliance with TSA regulations. While TSA's monitoring and oversight practices consisted primarily of spreadsheet type databases that identified the date and dollar amount of air carrier payments, it had no documentation indicating that it reviewed the payments for accuracy and completeness. As a result, TSA did not know that the large, medium, and small air carriers reviewed during the audit had not identified, collected, and remitted \$2.7 million in passenger security fees for the period we reviewed. Increased audit oversight would result in increased collections and decreased government funding of passenger and property screening costs. During our

September 15, 2005 exit conference, TSA officials stated that 12 audits had been completed between late 2004 and July 2005.

The \$2.7 million underpayment identified above did not represent the full passenger security fee period because the large air carrier only had 6 months of data available instead of the 21 months of data reviewed for the medium and small air carriers. However, the 6 months of data resulted in over \$1.7 million for the large air carrier of the \$2.7 million total underpayment. During discussions with Customs and Border Protection officials¹⁰ and air carrier personnel, we determined that results from audits of other similar fees using 6 months of data are projected over the year and collected from the air carrier. Using the agreed upon method would result in the large air carrier's underpayment rising from \$1.7 million to over \$3.5 million¹¹. Appendix A of this report provides details of our audit methodology. For the medium and small air carriers, error rates and projection calculations covered 21 months worth of data.

Air Carrier Implementation of TSA Guidance

The three air carriers reviewed did not implement Docket 10 guidelines for determining the amount of passenger security fees to be collected, resulting in under collections of \$911 thousand. In addition, while auditing three different air carriers for our ASIF review, we processed Docket 10 travel itineraries in their ticket reservation systems and concluded that they were also in non-compliance. Although we did not review tickets and flight segments for these latter three air carriers, we concluded that lack of implementation of the Docket 10 was an industry-wide problem related to the reservation systems. For example, the SABRE and APOLLO reservation systems, the primary reservation systems used for U.S. domestic travel, were not programmed to identify passenger security fees based on segment stopovers. If the Docket 10 error rate identified for the three air carriers reviewed remained the same for all air carriers, TSA could be losing \$7 million in fee remittances annually.¹²

According to air carriers officials, Docket 10 and TSA guidance were unclear, conflicted with other guidance, or were not mandatory. Therefore the air carriers did not modify their ticket reservation systems to meet the Docket 10 requirements. However, TSA specifically responded to air carrier industry questions on how to determine the amount of passenger security fees to be collected prior to the February 2002 implementation, leaving sufficient time

¹⁰ Customs and Border Protection personnel perform audits of similar fees.

¹¹ Based on the requirement to maintain records for 5 years and TSA's authority to retroactively collect all fees, collections would be increased to cover over a 3-year period. Therefore, we estimate that the large carrier underpayment totals at least \$10.5 million.

¹² The \$7 million is not included as part of the actual underpayment reported herein. It merely shows the potential impact of not implementing Docket 10 assuming the error rate determined during the audit is consistent throughout the air carrier industry.

for the air carriers to modify their reservation systems. TSA did not detect that the air carriers had not implemented Docket 10 because it did not audit the fees imposed, collected, refunded, or remitted by the air carriers to identify instances of non-compliance or the system-wide problem with ticket reservation systems.

The following paragraphs discuss the chronology of TSA guidance on passenger security fees.

TSA published an interim final rule in the Federal Register on December 31, 2001. Additional guidance was published in the Department of Transportation (DOT) ¹³ Docket Management System (DMS) under document number TSA-2001-11120. While the interim final rule capped the fee at \$2.50 per enplanement, up to \$5.00 per one-way trip and \$10.00 per round trip, it did not give specific guidance regarding passengers who had two or more one-way trips or round-trips on one travel itinerary. The rule only stated that a “round trip” was one where the flight terminates at the origin point and a “one way” trip is any trip that is not a round trip.

On January 8, 2002, ATA, representing its 26 member air carriers, asked DOT for guidance on “one-way trip” and “round trip” travel itineraries. ATA’s letter, Docket 6, stated that ATA members and global distribution systems (computer reservation systems) needed help in understanding how to program their systems to collect the fees in time to meet the February 2002 implementation date. The ATA letter also provided nine hypothetical travel itineraries and asked the DOT to identify the applicable security fee for each itinerary. That letter referred to previous ATA correspondence to DOT (December 12, 2001) wherein ATA suggested that the “one way” definition¹⁴ commonly used by the air carrier industry would increase the amount of fees collected and submitted to TSA.¹⁵

On January 25, 2002, under DMS Docket 10, DOT provided clarification to ATA regarding the terms “one-way trip” and “round trip” and posted this information on its web site. DOT stated that the interim final rule (December 2001) defined a round trip as a trip that terminates at the origin point and a one-way trip is defined as any trip that is not a round trip. DOT addressed all nine of ATA’s hypothetical travel itineraries and gave ATA two specific examples where it was possible for a passenger to have multiple one-way trips or round-trips on one travel itinerary. This would result in the passenger

¹³ DOT was the parent organization for TSA until March 1, 2003. TSA became a part of DHS when DHS was formally established on that date.

¹⁴ A “one way trip” is continuous travel from a point to another point during which a stopover does not occur. A “stopover is a break in travel of more than 4 hours between two domestic flights or 12 hours between a domestic flight and an international flight or two international flights.

¹⁵ TSA stated in response to the discussion draft report that this type of change would have to occur in the Final Rule not as an interpretation in the docket. TSA added that they will consider ATA’s position in the Final Rule.

paying more than the standard \$5.00 for a one-way trip and \$10.00 for a round-trip. Appendix F provides examples from Docket 10 where fees would increase based on selected itineraries.

On March 1, 2002, under Docket 32, ATA informed DOT that the definitions and limitations contained in the Docket 10 were inconsistent with ATSA. Further, ATA asserted that ATSA and the December 2001 interim final rule did not support the Docket 10 guidance provided on January 25, 2002. While ATA asked to meet with DOT officials to discuss this issue, TSA officials stated the meetings were never held because they believed Docket 10 adequately covered ATA's concerns. However, we believe that ATA did have a legitimate open issue since the Interim Final Rule did not cover the 4-hour rule (see footnote 13).

A TSA Office of Revenue official stated that guidance supplementing the interim final rule and provided through the DMS is legally enforceable and should have been implemented by the air carriers. Officials for two of the three air carriers informed us that TSA guidance on the subject of "one-way trips" and "round-trips" was never portrayed as mandatory and a small air carrier official was unaware of the guidance. Officials from the large and small air carriers stated that they were not responsible for any uncollected segments due to Docket 10, would not pay it, and did not agree with OIG's underpayment finding in this area. The medium air carrier stated they would wait for further TSA guidance before deciding on responsibility for paying the additional fees.

Although DOT guidance to ATA provided examples of how the air carriers should implement the interim final rule, ATA members never modified their ticket reservations systems to collect the passenger security fee on segment stopovers involving one-way and round-trips. Additionally, one significant issue appears to remain open and requires resolution. Whereas ATA suggested that TSA use "stopovers" as the criteria for determining "one way" trips and charging the \$2.50 for each segment, DOT uses "terminations" within the itinerary to determine enplanements and thus the \$2.50 fee charge for one way trips. The difference here is the 4-hour rule for stopovers and defining what a "termination" means.

Manual Ticket Overrides

Manual ticket override errors at the large and small air carriers resulted in underpayments to TSA of \$869,177. Overrides occurred primarily when ticket agents, brokers, or wholesalers did not use one of the accepted worldwide air reservation systems and hand wrote the ticket on an air carrier's ticket stock for later update to the reservation system. According to an air carrier official, manual ticket errors are most likely to occur in smaller foreign countries

where no automated link to the reservation system will identify all applicable taxes and fees for each country. Officials from the two air carriers agreed they were responsible for the underpayment and that TSA should have been paid.

Involuntary Reroutes

The medium air carrier did not follow TSA's involuntary reroute regulations resulting in a \$199,392 under collection. Although the small air carrier did not follow the guidance, we did not find any involuntary reroutes in our sample. Involuntary reroutes occurred when the air carrier changed a passenger's flight itinerary at the last minute for reasons such as bad weather, security, or mechanical difficulties. The reroute can increase or decrease the number of passenger segments flown. According to 49 CFR Part 1510.9(b), direct and foreign air carriers are solely liable to TSA for additional security service fees imposed because of involuntary enplanement changes to the itinerary.

The small and medium air carriers paid TSA the passenger security fees for involuntary reroutes based on the original purchased ticket and not on the number of segment changes. Officials from the medium air carrier stated that the number of segment increases and decreases generally offset each other and that TSA regulations do not address segment decreases. The large air carrier paid TSA for any segment increases and in the case of segment decreases, allowed TSA to keep the security fee.

Under 49 CFR Part 1510.11, the air carriers only collect the money as trustees for TSA and hold neither legal nor equitable interest in the passenger security fee. Further, the law clearly states that air carriers are liable to TSA for the additional fees resulting from involuntary enplanement changes. Additionally, TSA has issued guidance on passenger segment decreases for voluntary reroutes. DMS Docket 59 guidance states that when an air carrier does not refund the passenger security fee to the ticket purchaser, the fee must be remitted to or remain with TSA. Therefore, the air carriers have no grounds to keep fees of any kind that are owed to the ticket purchaser or TSA.

Island Passes

The small air carrier's incorrect handling of security fees for their "Island Pass" program resulted in an under collection of \$173,413. The air carrier issued an "Island Pass" from which a passenger could take unlimited flights between the Hawaiian Islands for a fixed fee. The longest pass was for 1 month and cost about \$1,400. However, the air carrier only collected \$10.00 covering four flight segments regardless of how many segments were flown during that period. This allowed the island pass ticket holder to exceed the number of segments for which the passenger security fee was collected and paid to TSA. Passengers flew a total of 93,181 island pass segments during

our review period, but the air carrier collected and paid TSA for 23,816 segments resulting in 69,365 unpaid segments. Air carrier officials agreed they had not collected the required passenger security fees and that it was likely that other air carriers were also selling inter-island passes in the same manner. Based on our inquiries, it appeared that only two other air carriers may have issued these type passes. Because this was a unique issue with the small air carrier, we did not include the “Island Pass” underpayment in our error rate for projecting the total underpayment amount for the three air carriers reviewed. The air carrier agreed with our computation and stated they would pay TSA accordingly. During the audit, the air carrier informed us they no longer offer the “Island Pass” program, therefore, the additional collections only cover 2002 to 2004.

Foreign Collection

Some foreign countries did not collect passenger security fees resulting in under collections of \$167,474. For example, Guatemala does not enforce collection of the passenger security fee for tickets sold in Guatemala with segments originating in the United States. Officials from the large air carrier stated foreign travel agents could not be compelled to collect the taxes/fees on behalf of the U.S. government. The official also agreed the air carrier was responsible of the underpayment.

Other Unpaid Fees

The five areas discussed above total \$2,320,682 in unpaid passenger security fees. We identified an additional \$384,738 in unpaid fees (based on flight segments); however, the air carriers could not specifically categorize or identify the type of errors that caused the fees not to be collected and remitted to TSA.

Passenger Security Fee Summary

For the three air carriers reviewed in detail, passenger security fees, when collected, were remitted to TSA. However, those air carriers did not accurately collect all monies due to TSA. In addition, four of the six underpayment categories noted previously appeared to be systemic to the air carrier industry as a whole and likely occur at every air carrier operating domestically in the United States. If the underpayment rates resulting from these collection errors are systemic, annual underpayments to TSA would amount to over \$14.5 million. Therefore, TSA needs to provide closer oversight of the air carriers to ensure proper collection and remittance of passenger security fees.

According to officials from TSA's Office of Revenue, they made a request early in the program for additional funding and personnel so that air carrier audits could be completed. However the Office of Revenue did not receive additional personnel, resources, or funding until almost 2 years later to perform audits, and as a result, TSA could not begin to validate the accuracy of the air carriers' collection and remittance of the fees until late 2004.

Despite these shortcomings, TSA took some steps in FY 2004 to improve its oversight. Specifically, TSA began working with U.S. Customs and Border Protection personnel to develop audit plans and perform audits of these fees. The original plan called for three audits in 2004. As of February 2005, four audits have been performed but results have not been provided to TSA. TSA had nine additional audits scheduled in 2005¹⁶. Although this is a good first effort, TSA's efforts will not solve the collection problem. At the planned rate of 13 air carrier audits per year, over 13 years will be required to audit each air carrier only once.

TSA does not plan to audit each air carrier equally but rather it envisions an audit oversight process based on risk that would include reviewing the passenger security fees of the top 20 air carriers every 2 to 3 years and the remaining air carriers every 5 years. TSA could meet the plan for the top 20 air carriers by doing 10 air carriers each year but the rest of the air carriers would rarely, if ever, be audited. Auditing the top 20 air carriers would cover the largest share of the market and is a logical approach based on TSA's limited resources. However, this does not ensure that another 130 air carriers that provide passenger security fee collections are complying with ATSA and TSA regulations. Due to the ability of TSA to retroactively collect all fees owed, the risk is reduced if the audit is accomplished within the 5-year records retention period.

¹⁶ At the exit conference on September 15, 2005, TSA stated 12 audits were completed by July 2005.

During our September 2005 exit conference, TSA officials indicated that they had expected to use our audit report as the means to collect the unremitted passenger security fees identified herein. We explained that this “performance” audit was not intended to replace the “operational” audits conducted by Customs and Border Protection for TSA. We also pointed out that our audit findings and recommendations are provided to TSA for action, and that we would provide any additional information or documentation needed to effect the collection actions that TSA deems appropriate.

Recommendations

We recommend that the Assistant Secretary for the Transportation Security Administration:

Recommendation #1: Collect the \$2.7 million in unpaid passenger security fee amounts identified in this report and continue efforts to validate that all air carriers not covered by this audit have accurately collected and remitted all passenger security fees.

Recommendation #2: Continue efforts to develop and implement a viable plan to perform an increased number of annual passenger security fee audits incorporating the issues raised by this audit and any others identified in the audits performed by Customs and Border Protection personnel.

Recommendation #3: Enforce the interim final rule on passenger security fees as clarified by Docket 10, and resolve ticket reservation system software issues with the airline industry to assure collection and remittance of all passenger security fees on future air carrier tickets.

Management Comments and OIG Analysis

Management Comments to Recommendation #1: TSA concurred and stated that action on this recommendation is pending receipt of the OIG documentation that would allow it to invoice the carriers for due amounts. Absent the information requested, TSA would be forced to undertake repeat audits incurring additional costs and delays.

In extrapolating to the entire industry the OIG findings relative to the reported finding on three carriers, TSA noted that the collection efforts exceed over 99 percent success. TSA indicated it would continue to seek improvements. In addition, TSA stated that it has established an audit program with U.S. Customs and Border Protection (CBP), as discussed in recommendation 2, below, which will assist in this effort.

OIG Comments and Analysis: Actions planned and taken by TSA should ensure that the air carriers accurately collect and remit all passenger security fees in the future. Regarding the collection of the \$2.7 million in unpaid fees noted in the recommendation, OIG provided specific information and documentation on the audited air carriers during the audit and after our exit conference. Unlike CBP who performs operational audits for TSA, in order to maintain our independence, OIG does not perform the normal operational activities of the audited organization. However, to obviate the need for a separate operational audit at additional costs and delays, OIG will provide whatever additional supporting documentation from our working paper files that TSA requires and requests from us to effect collection of the unpaid passenger security fees. We consider this recommendation resolved but open until TSA provides us documentation that the \$2.7 million in unpaid fees noted in the finding and recommendation has been collected.

Management Comments to Recommendation # 2: TSA concurred and stated that since the OIG audit, it has implemented a Memorandum of Understanding with CBP's Regulatory Audit Division to provide compliance audits. TSA has decided that the best use of its resources is to outsource on-site audit work to CBP. TSA commented that CBP was unable to supply all the desired audits in FY 2004 due to DHS restructuring (Immigration and Naturalization Service/Animal and Plant Health Inspection Service auditors), but it conducted 12 audits in FY 2005 and plans to complete 13 more in FY 2006. TSA also intends to audit the major carriers every 3 years and other carriers less frequently due to the expense of conducting such audits. TSA stated that since audits of air carriers continue to show very high levels of compliance, there is little risk to the Government as audit findings are applied retroactively and the air carriers are invoiced for the outstanding amounts.

Management Comments to Recommendation #3: TSA concurred and stated that it has had further discussions with various air carriers and associations to better understand any issues that have arisen on implementing the passenger security fee requirement. TSA indicated that the air carriers have asked for further clarification and/or future changes on several specific aspects of the regulation and that TSA is still considering the merits of making any such changes. TSA stated that it is also awaiting the results of its passenger security fee audit program to determine whether there are other changes that it may need to consider but noted that past audits have shown that discrepancies only affect about 1% of the fees collected. TSA noted that where appropriate, TSA action has been initiated to collect any outstanding passenger fees.

OIG Comments and Analysis (Recommendations #2 and #3): Actions planned and taken by TSA to enhance and expand its compliance audit function and to clarify outstanding collection issues with the air carriers are

the initial steps to implementing these two recommendations. As stated in Recommendation 2, compliance audits performed for TSA by CBP should consider the issues raised in this report as well as any other issues raised in the compliance audits. Further, while discussions with air carriers have taken place in the past, some issues have remained unresolved with the air carriers for extended periods of time. In addition, while past audits have only identified a 1 percent discrepancy in collections, those audits may not have considered the systemic issues raised in this report. It is noteworthy that TSA is attempting to clarify air carrier issues and decide what regulatory changes, if any, are warranted. However, until such time as these issues are resolved and regulations are changed, TSA cannot ensure the proper collection and remittance of all passenger security fees.

Although TSA has expanded and enhanced its compliance audit program, we consider Recommendation 2 resolved but open until TSA provides us with assurance that it considered the results of this audit in its Memorandum of Understanding with CBP. In addition, TSA needs to provide us the results of its discussions with air carriers and documentation on the specific actions it plans to take or has taken as a result of clarifying the issues raised by those air carriers. While resolved, in order for us to close Recommendation 3, TSA should provide us specific comments on actions taken to enforce or modify the interim final rule and to resolve the reservation system software issue discussed in the finding.

Accuracy of CY 2000 Passenger and Property Screening Costs Reported by the Air Carriers

The various costing methodologies used by three air carriers did not provide a fair and reasonable basis for accurately computing the aggregate ASIF due to TSA. When TSA began receiving Appendix A submissions in 2002, it became aware of serious air carrier disagreements regarding the costs to be reported and of overall problems with the integrity and reliability of the passenger and property screening costs. While TSA required air carriers to submit independent audits of the Appendix A submissions, those audits generally resulted in “no opinion” reports and did little to assist TSA in correcting the problems or identifying other means of computing a fair and reasonable aggregate ASIF. Further, TSA did not enforce all ATSA regulations regarding the identification and remittance of air carrier security infrastructure fees.

By determining a fair and reasonable aggregate ASIF amount and providing better oversight and stronger enforcement actions, TSA would increase ASIF collections and decrease the amount of government funding needed for passenger and property screening.

Appendix A

Appendix A submissions were plagued with a myriad of problems that hindered the air carriers' efforts to accurately report their CY 2000 passenger and property security screening costs. These problems are listed below and kept us from determining fair and reasonable Appendix A costs for the three air carriers reviewed in detail.

1. Due to the large number of air carriers, TSA provided the air carriers broad guidance that allowed them to use their own methodologies to identify CY 2000 passenger screening costs. However, this led air carriers to view the guidance as unclear;
2. Air carriers accounting systems could not identify and track passenger and property screening costs;
3. Air carriers cost methodologies for determining Appendix A expenses varied significantly;
4. Original invoices at two air carriers were not always available and invoices at all three air carriers to support Appendix A costs were often vague and non-descriptive;
5. Passenger-related expenses were shared among air carriers with no clear audit trail separating passenger processing costs from passenger and property screening costs;
6. Airport passenger and property screening cost methodologies were not uniform;
7. Screening contractors' costs for both passenger and property screening and other non-screening costs were commingled;
8. Air carriers could not identify specific costs associated with Appendix A cost categories; and
9. Institutional knowledge shortfalls were prevalent due to job layoffs at the air carriers, departure of the screening contractors after federalizing the screening function, and staff turnover at CPA firms and the port authorities.

The above problems highlight why reported Appendix A costs were unreliable and inaccurate and why CPA firms representing over 59 air carriers¹⁷ stated they could not opine on the reasonableness of the procedures used to

¹⁷ These 59 air carriers accounted for more than 90 percent of the total industry's ASIF dollars.

determine and remit the fees, as required by ATSA. Further, we noted that 26 air carriers did not report on their accounting procedures as required by ATSA, 10 air carriers did not file the Appendix A in a timely manner, and as of February 2005, 6 air carriers had not submitted an Appendix A.¹⁸ Based on these “red flags,” TSA sent letters, e-mails, faxes, and made follow-up phone calls in an attempt to ensure the accurate identification and remittance of CY 2000 passenger and property screening costs. However, stronger enforcement type actions did not begin to occur until 2004.

As discussed in the paragraphs below, our audit encompassed (i) a detailed review of the Appendix A submissions of a large, medium, and small air carrier, (ii) an examination and assessment of costing methodologies and documentation supporting billing to those air carriers by national Airports, (iii) a review of the invoices Passenger and Property Screening Contractors provided to the to the three air carriers, and (iv) an assessment of the documentation that the three Air Carriers used to support Appendix A costs reported to TSA. Our review of Appendix A submissions maintained by TSA identified unresolved footnote disclosures, misapplied TSA guidance, and peculiarities and inconsistencies among air carrier payments.

Unresolved Footnote Disclosures

Two of the air carriers in our sample and five additional air carriers outside our sample did not include certain passenger and property screening costs, totaling \$9,230,149, in their Appendix A totals because they considered these costs unreasonable and duplicative. However, the seven air carriers identified these unremitted costs as footnote disclosures to their Appendix A submissions. TSA never resolved the issue of the unremitted costs related to the footnote disclosures or the fact that most air carriers reported and remitted such costs since program inception while these seven did not. Since program inception through February 2005, the footnoted but unremitted costs for these seven air carriers totaled more than \$25 million.

Of the \$9,230,149, \$4,754,889 related to the large and medium air carrier in our sample. These two air carriers argued that TSA had not assumed certain indirect passenger and property screening costs, e.g. law enforcement, rent expenses, program management, and administrative, and therefore, they should not be required to reimburse TSA for costs they still are incurring. Since TSA took over screening services, air carrier officials said that their indirect costs have not decreased but rather increased. Officials from both air carriers stated that many of the costs were duplicative and that ATSA never intended for the air carriers to pay twice for the same service.

¹⁸ Although these 6 air carriers were no longer in operation, an Appendix A for each former air carrier was required by Docket 19 so that these passenger and property screening costs could be included in the aggregate ASIF total.

Although the medium air carrier did not pay footnoted costs, it established a trust account to reserve the funds pending a TSA decision on this matter. However, the air carrier's subsidiary "Express" air carrier paid its footnoted amount from its trust account based on a TSA letter to the medium air carrier requesting payment.

ATSA required each domestic and foreign air carrier engaged in air transportation in the United States in CY 2000 to remit monthly to TSA 8.333 percent of the total amount the air carrier included in its Appendix A. By not resolving the footnoted costs, the seven air carriers have continued to remit a lesser amount while other air carriers are paying the same type of passenger and baggage screening services each year and have been since inception of the fee. In this regard, more than 140 other air carriers have not footnoted similar indirect passenger and property screening costs but have been remitting these ASIF amounts to TSA. TSA officials stated that over \$27 million has been collected from these 140 air carriers¹⁹ for these categories. Without timely resolution of this issue, TSA will have difficulty collecting the footnoted amounts because of the individual air carriers' and overall industry's financial difficulties.

TSA Guidance Misapplied by Air Carriers

As stated previously, TSA provided broad guidance to the air carriers in CY 2002 on preparing the Appendix A. That guidance purposely lacked specificity so as to allow the air carriers to use their own methodologies on how to identify and compute passenger and property screening costs. TSA issued Docket 19²⁰ on April 29, 2002 that provided additional guidance relating to use of labor cost, assigning equipment cost, dividing grouped cost etc. While the Appendix A identified 35 cost categories to be reported, the three air carriers we reviewed did not identify costs in a number of categories but, instead, lumped costs together. In some cases, air carrier officials who prepared the Appendix A in CY 2002 differed from those who accounted for the costs in CY 2000. Because the guidance lacked specificity, the nature and amount of passenger and property security costs incurred in CY 2000 were subject to varying interpretations by air carrier officials in CY 2002. Docket 19 recognized the possibility of varying interpretations of what constituted Appendix A costs and indicated that TSA would individually contact air carriers if it was apparent that applicable regulations, previous guidance, and the additional guidance in Docket 19 had been misunderstood or misapplied. TSA also indicated it would issue further clarification in the future if needed,

¹⁹ The data was provided by TSA in total as of March 2005. We did not request a breakdown by air carrier.

²⁰ "Guidance for the Aviation Security Infrastructure Fee: Completing and Submitting Appendix A on Cost Related to Passenger and Property Screening for Calendar Year 2000."

but did not provide further information. The following examples seem to indicate that additional guidance was warranted.

The large air carrier identified costs in only 2 of the 35 cost categories, the medium air carrier identified costs in 9 categories, and the small air carrier identified costs in 6 categories. For the large and medium air carriers, Appendix A cost categories with no costs were (i) footnoted as identified but not paid, (ii) noted as having been added with other categories having costs, or (iii) left blank without explanation. The small air carrier provided notes to the Appendix A explaining 4 of the 29 categories that were blank. For example, the notes for categories related to program management and contract oversight over third party vendors stated that the air carrier did not maintain detailed records in CY 2000. The fact that the air carriers grouped or combined ASIF-related costs into just a few categories, simply left those categories blank, or did not provide adequate support for the grouped amounts prevented us from determining the accuracy and reasonableness of reported Appendix A costs.

Since TSA could not provide specific examples for all possible scenarios on how to identify and segregate the costs to be reported on the Appendix A, the air carriers did not clearly understand what and where to report specific amounts related to passenger and property screening. For the most part, the air carriers simply combined amounts into one cost category or ignored the cost. Docket 19 did provide the air carriers additional guidance in areas where costs were shared or allocated between passenger screening and non-passenger screening. However, officials from the large air carrier stated they were not given clear examples of how to identify and segregate expenses. Therefore, they combined many cost categories on the Appendix A. In this case, the broad nature of the TSA guidance contributed to our inability to determine accurate Appendix A costs for this air carrier.

Subsequent to our on-site visit, TSA brought to our attention Docket 19 which addressed the area of the air carriers' commingling of costs. Docket 19 was a response by TSA to ATA's March 18, 2002 request for clarification on reporting various Appendix A cost categories. In its letter, Docket 7, ATA requested clarification by April 18, 2002 or an extension to the May 2002 Appendix A submission requirement. Docket 19 was issued on April 29, 2002, and did not provide for an extension.

The air carriers did not use the guidance provided by Docket 19 because the guidance was late in coming and did not extend Appendix A submissions after May 2002. Therefore, the air carrier issue continued to group reportable Appendix A costs into just a few cost categories. For example, individuals who performed passenger and property screening duties also performed other duties not related to passenger and property screening. Duties performed by

the same individual that were difficult to segregate included exit lane monitors, security program management, contract administration, legal and accounting support, supervisory personnel, law enforcement officers, and ground security coordinators.

Officials from the large air carrier also stated that many of their invoiced passenger and property screening costs from the airports, port authorities, and contractors were commingled with non-passenger and property screening costs. As a result, they did not know the exact amount related to passenger and property screening. However, Docket 19 did provide a possible method of allocation. Rent was cited as an example wherein an airport formulated its rental rate on all airport costs²¹ and then allocated those costs to the air carriers based on their leased space. Since the air carriers received one combined rental bill, it was then left up to the air carriers to declare what portion, if any, would be allocated to the appropriate Appendix A cost category.

In our view, the late issuance of Docket 19 (in terms of the Appendix A submission deadline) contributed to the air carriers grouping many of the cost categories on the Appendix A without necessarily considering whether all costs were related to passenger and property screening. Subsequent TSA analysis of Appendix A submissions as stated in Docket 19 could have identified many of the problems associated with the accurate segregation and reporting of passenger and property screening costs.

Peculiarities and Inconsistencies in Air Carrier Reporting

As highlighted below, TSA identified and we confirmed peculiarities and inconsistent treatment of Appendix A costs reported by various air carriers.

- TSA required that the air carriers' Appendix A identify all direct costs for real estate utilized in the screening of persons and property. The three air carriers did not report any real estate costs to TSA. Our review of the Appendix A submissions of the five air carriers withholding footnoted costs showed that two additional large air carriers did not report any direct real estate costs.
- ATSA required a Ground Security Coordinator (GSC) for each domestic and international flight departure. The GSC's duties are to review all security related flight functions. GSC costs to be included in Appendix A included salaries, benefits, retirement, and training. The air carriers did not consistently report these costs. For example, the large and small air carriers did not include any costs for this position, while the medium air carrier identified and paid TSA \$7,705 for the

²¹ In this example, rental rates could include costs associated with airfield, terminals, maintenance and operation, debt service costs, established reserve account and capital items.

parent company and \$16,891 for the smaller subsidiary. Further, a limited review of the TSA universe identified that one large air carrier paid \$19,950 for GSCs, while another large air carrier paid TSA nothing. The TSA database also showed one medium air carrier paid \$303,438.

- TSA required the air carriers to identify and remit the cost of law enforcement officers (LEO) whose duties related to the screening of persons and property. The small air carrier identified and paid \$34,164 while the large and medium air carriers paid nothing. The review of the five air carriers that footnoted costs identified two large air carriers who also paid nothing.

The examples above again highlight our concerns regarding the reliability of the passenger and property screening costs reported in the Appendix A. Additionally, if immediate corrective actions to address the data peculiarities had been taken less passenger and property screening costs would have gone unpaid by the air carriers. Further, the air carriers reported some costs to TSA on an ad-hoc basis with no clear methodology or support on how the costs were determined or why costs were omitted from the Appendix A. At our exit conference in September 2005, TSA stated that peculiarities in the data received early in the process was the reason why independent audits of all Appendix A submissions were required. However, TSA did not take further action even after audits came back with “no opinion” on the reliability of the data submitted by the air carriers.

Review of Air Carriers Records

We audited the records of three air carriers to: (1) determine if they had accurately reported passenger and property screening costs and properly remitted the ASIF to TSA and (2) identify costs not correctly reported in the Appendix A submissions or remitted to TSA as required. The air carriers misidentified passenger and property screening invoices as non-screening invoices, did not include all applicable account codes having screening costs, or simply omitted appropriate costs which in turn kept these costs from being reported in the Appendix A. We did not include the portion of these amounts relating to LEOs and rental cost in the calculated amount of errors because we could not be certain that those costs did not duplicate amounts reported as footnote disclosures.

As with other areas already discussed in this report, the air carriers faced many difficulties in documenting Appendix A costs. Those difficulties are discussed below.

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- As previously stated, (1) TSA guidance on preparing the Appendix A was purposely general in nature and was considered unclear by the air carriers, (2) air carrier accounting systems did not segregate Appendix A costs from non-passenger and property screening costs, and (3) air carriers lacked corporate knowledge due to staff departures.
 - The large and medium air carriers lacked detailed accounting records that would allow us to identify all screening costs by station and by contractor.
 - The large and medium air carriers only provided copies of original invoices to audit. We noted specific time frames where no invoices, or any other support could be identified for the medium air carrier.

These types of problems prevented us from corroborating air carrier records with other independent data from the national airports and the private contractors who performed the screening services.

Small Air Carrier

The small air carrier underreported Appendix A costs because invoices relating to these expenses were not correctly identified in any of the air carrier's spreadsheets used to support reported Appendix A costs.

The air carrier's airport stations did not consistently report screening costs. For example, only 10 of the 23 airports where the small air carrier operated reported equipment expenses, only 4 airports reported management expenses, and only 3 airports reported LEO expenses. Additionally, no airports reported rent expenses, yet the air carrier's chart of accounts identified almost \$8 million in station rent. The lack of consistency indicated the degree of subjectivity exercised when air carrier personnel at the airports identified and reported Appendix A costs and is an indicator that the air carrier did not report all required costs.

Medium Air Carrier

The medium air carrier underreported its costs because invoices relating to Appendix A expenses were not included in the air carrier's spreadsheets supporting Appendix A costs.

We reviewed documentation supporting \$14,495,106 (70.2 %) of the \$20,641,503 reported on Appendix A, line 1 that identified the passenger and property screening costs of the private contractors. The review included the air carrier's hub airports, the top 26 revenue producing airports, and a majority of the subsidiary's airports. We also reviewed supporting documentation from

their external auditor regarding Appendix A expenses and traced microfiche invoices to weekly billing statements and summary spreadsheets.

Inconsistencies existed in the screening costs reported by the air carrier's airport stations. For example, the air carrier had five passenger and property screening contracts in place with other air carriers to share screening expenses, yet no costs were shown on the Appendix A for these contracts. Also, only 35 of the 88 airports where the parent air carrier operated reported equipment expenses and 57 of the 106 airports where the Express subsidiary had operations showed equipment expenses.

Large Air Carrier

The large air carrier underreported its costs because invoices relating to Appendix A expenses were not correctly identified in the air carrier's spreadsheets supporting Appendix A costs. Further, other chart of account categories were related to passenger and property screening but were not included.

We reviewed documentation supporting \$10,421,800 (29.2%) of the \$35,717,301 reported on line 1 of the Appendix A. We randomly sampled invoices from 13 airports and 2 large hub airports to determine the reliability of the reported amount. In addition, we randomly sampled transactions totaling \$1,001,386 from 10 airports whose chart of accounts, numbers 85 and 86, were not included on line 1 of Appendix A. We selected these accounts because account number 85 and 86 were included at two other airports (San Francisco and JFK) as passenger and property screening costs on line 1. We were not able to review the external auditor's documentation regarding the air carrier's Appendix A submission because the audit firm no longer maintained the supporting documentation.

The large air carrier was the dominant signatory air carrier at various airports and as such, screening contractors billed them for the services of the whole terminal or airport. The signatory air carrier in turn billed back a portion of the screening services to the secondary air carriers. Our review of the large air carrier's invoices identified problems with this billing system. For example, at one airport, the contractor billed the large air carrier for services identified only as screening. The large air carrier then reduced its total costs by the amounts allocated to the secondary air carriers using the same terminal or checkpoint. However, the large air carrier's invoice to a secondary air carrier (the small air carrier in our review) included both screening and facility costs.²² The small air carrier only reported the screening portion of the charge on their Appendix A. Thus, while the large air carrier reduced its Appendix A passenger and property screening costs by the total amount allocated to the secondary air carrier, it did

²² The secondary air carrier indicated that the facility charges covered gate, ticket counter, and hangar use.

so incorrectly because secondary air carrier charges included facility use costs. If this large air carrier applied this bill back practice to secondary air carriers at other airports across the nation, overall screening cost would be understated by the amounts transferred to these other air carriers that relate to facility charges.

Independent Validation of Reported Passenger and Property Screening Costs

As a final step, we attempted to validate the amounts reported by the carriers by reviewing costs paid for services during CY 2000. To perform this work, we obtained information from entities that provided services to the air carriers. These entities included the national airports where the air carriers operated, as well as the passenger and property screening contractors who previously provided security services.

National Airports

We determined that the three air carriers have collectively understated their passenger and property screening costs in their Appendix A by about \$6.5 million. The understated costs were related to law enforcement and rent expenses. This condition occurred because the air carriers (i) were unable to identify a clear methodology on how to identify these costs, (ii) misidentified costs in their accounts, and (iii) lacked corporate knowledge from CY 2000 to accurately identify Appendix A amounts in CY 2002. TSA did not detect the underreported amounts because it did not have the audit resources to provide sufficient oversight for the Appendix A submissions. However, TSA realized the Appendix A submissions were understated in total from the beginning; however, they did not know by which air carriers and how much.

We audited billing records at the national airports to determine whether all applicable airport costs were reported in the air carriers' Appendix A. Many of these airports billed the air carriers for passenger and property screening services in different ways using unique criteria. The differing methodologies and unique criteria contributed to the air carriers' problems in accurately identifying and reporting Appendix A costs. See Appendix H for additional information on individual airport results and on the complexities involved in determining LEO and rent costs.

LEO Costs

We concluded that the large air carrier may have underreported LEO costs by \$3,119,026, the medium air carrier may have underreported these costs by \$2,042,135, and the small air carrier may have over-reported LEO costs by \$3,401. Airports used four primary methodologies to bill the air carriers for LEO expenses. They:

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1. Took total LEO expenses and billed the air carriers based on their percentage of passenger enplanements at the airport;
 2. Built the LEO costs into the air carriers' rental rates;
 3. Allocated the costs into the air carriers' landing fee rates; or
 4. Absorbed the costs and did not directly or indirectly bill the air carriers for LEO expenses.

Eight of the 13 airports did bill the air carriers directly or indirectly for applicable law enforcement costs. The other five airports absorbed these costs internally.

Regardless of the methodology or allocation process used by the airports, the air carriers still had to subjectively decide what percentage of the billed LEO costs was applicable to passenger and property screening. Further, air carriers needed to estimate applicable LEO costs on an airport-by-airport basis, as we did, because of differing methodologies and unique criteria used by the airports. This time consuming and difficult task may have contributed to the under reported amounts for the medium and large air carriers. The small air carrier paid a total LEO cost of \$34,164 but only operated at 7 of the 13 airports.

TSA guidance regarding the reporting of LEO costs on Appendix A only indicated that the LEO services be performed in connection with the screening of persons and property. Since the guidance did not specify physical locations where LEOs perform these services, the air carrier's application of TSA guidance was entirely subjective with no definitive criteria with which to identify LEO costs. Because of the subjectivity, LEO costs could include the costs for LEO passenger and property screening performed anywhere in the terminal, the costs for the rapid response team, or the costs for an LEO physically assigned to the security checkpoint.

Rent Costs

Our work at the 13 airports showed that the large, medium, and small air carriers may have underreported rental expenses by \$1,377,185; \$27,191; and \$17,999; respectively. While the Appendix A required air carriers to identify all direct real estate costs utilized for the screening of persons and property, e.g. security checkpoints, none of the airports broke down rent costs in this manner. In identifying the underreported amounts noted above, rent computation methodologies differed from airport to airport and 2 of the 13

airports we visited did not directly or indirectly charge the air carriers for rent for Appendix A purposes.

TSA guidance on identifying Appendix A rent expenses stated that the air carriers should identify and remit direct real estate costs associated with the screening of persons and property. Subsequent guidance in Docket 19 recognized the many intricacies and methodologies of how airports bill the air carriers for Appendix A rent expenses and suggested square footage as one possible method. We used an allocation methodology similar to what was described in Docket 19 to determine both real estate and LEO expenses. Using this methodology resulted in the underreported amounts identified above. We further determined that the small and large air carriers did not remit any rent charges to TSA and the medium air carrier identified \$142,510 but footnoted the entire amount as unreasonable and duplicative.

Passenger and Property Screening Contractors

We visited the headquarters of five former passenger and property screening contractors to compare and reconcile their billing invoices with the invoices and other data provided by the three air carriers to support Appendix A amounts. Two contractors did not provide us any invoices to support air carrier billings; therefore, we performed detailed reviews only at the 3 remaining contractors. We calculated that Appendix A passenger and property screening costs for the large air carrier may have been understated by \$480,217. This occurred because the air carrier did not correctly associate some contractor billing records with passenger and property screening costs. While we did not identify underreported amounts for the medium and small air carriers, the three contractors lacked the supporting documents we needed to ensure that all Appendix A costs were actually reported to TSA. See Appendix H for a complete discussion of the methodology we used and the limitations that precluded a more exact determination of the amounts paid to passenger and property screening contractors.

ASIF Summary

The air carriers reviewed have understated their CY 2000 passenger and property screening costs by at least \$9,230,149 in unresolved footnote disclosures. As reported above, Appendix A submissions were plagued with a myriad of problems hindering the air carriers from accurately reporting passenger and property screening costs and our efforts to determine the reliability and accuracy of the aggregate ASIF amount to be remitted annually by the air carrier industry to TSA.

Also, TSA identified, and OIG confirmed, many instances of program non-compliance by the air carriers, including the following:

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- 10 air carriers did not timely file an Appendix A,²³
 - 6 air carriers still had not filed an Appendix A as of February 2005 and other Appendix A submissions were inaccurate,
 - 19 air carriers had not obtained CPA opinions on the fairness and reasonableness of the procedures used for accounting and remitting the fees as of February 2005, and
 - 7 air carriers refused to remit certain Appendix A costs.

In April of 2004, TSA's Office of Revenue received authority to assign civil monetary penalties to non-compliant air carriers, including penalties for air carriers that have not filed the Appendix A or received the required CPA opinions on their Appendix A submissions. TSA officials indicated a reluctance to use its enforcement authority because of the air carriers' weak economic conditions, the possibility of prolonged legal proceedings, and their belief that using all other means to ensure compliance is a good government practice. TSA officials indicated that some of the unpaid ASIF costs, e.g., footnoted LEO and rent expenses, have been considered an "acceptable risk" because these unpaid costs can be collected at a later date.

Recommendations

We recommend that the Assistant Secretary for the Transportation Security Administration:

Recommendation #4: Determine a fair and reasonable aggregate ASIF amount and collect the fees envisioned by ATSA, where applicable, based on the results of this audit and GAO's analysis and estimates.

Recommendation #5: Resolve outstanding issues raised by the air carriers, e.g., duplicative costs, or otherwise referenced in this report, e.g., rent methodology, LEO methodology, and inconsistent reporting, if TSA continues to utilize the Appendix A as the basis for aggregate ASIF collections from the air carriers.

Recommendation #6: Continue with the determination of the per air carrier ASIF amount based on implementation of Recommendation 4 and comments received from air carriers.

²³ TSA informed us at the exit briefing that they obtained these Appendix A submissions and their respective delinquent funds, as well as the Appendix A submissions for the 6 air carriers who did not file.

Recommendation #7: Initiate enforcement actions against the seven air carriers that fail to remit ASIF amounts mandated by ATSA and other air carriers who fail to comply with ATSA and TSA regulations.

Management Comments and OIG Analysis

Management Comments to Recommendation #4: TSA concurred and stated that TSA has recently determined a fair and reasonable aggregate ASIF amount and a means of allocating those additional costs among air carriers. In taking its decision on the aggregate industry amount subject to collection, TSA carefully considered the work reported in the April 16, 2005 GAO report. Extended comments are included in Appendix B.

Management Comments to Recommendation #5: TSA concurred and stated that as acknowledged by the OIG in their audit report on page 16, TSA purposely provided broad guidance to the air carriers on preparing their response to the cost questionnaire (Appendix A). This broad guidance was sufficient for approximately one half of the air carriers subject to this fee to provide TSA with clean opinions from their independent auditors on the completeness of the data they submitted in their cost questionnaire using the guidance provided by TSA. The agency continues to rely on the air carrier cost questionnaire submissions as the basis for the air carrier fee allocation. However, TSA is unable to rely on the completeness of those air carriers' questionnaires that were unable to substantiate their cost submissions by receiving an unqualified audit opinion. Therefore, TSA has relied on the approach initiated by GAO to identify the level of industry-wide understated costs and the agency has allocated those costs on the basis of the formula described in Recommendation 4 above.

Management Comments to Recommendation #6: TSA concurred without specific comments.

Management Comments to Recommendation #7: TSA concurred and stated that on December 2, 2005, it sent Demand Letters to the seven air carriers that had failed to remit ASIF amounts mandated by the regulations establishing the Air Carrier Fee. Those air carriers not subject to a bankruptcy proceeding have paid or completed a payment agreement that cover all of the amounts due to TSA from inception of the fee. Where permissible, TSA is working with the Department of Justice to claim amounts due through the appropriate bankruptcy court.

OIG Comments And Analysis (Recommendations #4 through #7):
The actions planned and taken by TSA meet the intent of the recommendations. TSA's implementation of GAO's approach to determining a fair and reasonable ASIF amount resolves and closes Recommendation 4

and eliminates the requirement to resolve the specific outstanding issues discussed in Recommendation 5. Although TSA did not specifically comment on Recommendation 6, its comments to Recommendation 4 are sufficient to resolve and close this recommendation. Based on the actions taken on Recommendation 7, we also consider this recommendation resolved and closed.

OIG initiated this audit to determine:

1. The accuracy of passenger security fees collection and remittance and ASIF amounts paid by air carriers to TSA.
2. The adequacy of TSA program controls and controls used by air carriers to ensure proper payment.
3. Compliance with legislative reporting requirements.
4. Whether the security fees were remitted to TSA timely.

In addition we answered the following questions:

1. Are TSA's controls adequate to ensure that air carriers are accurately identifying, collecting, and remitting passenger security fees to TSA?
2. Are the air carriers' reports of CY 2000 passenger and property screening costs accurate and do they provide a fair and reasonable basis for computing the air carriers' ASIF reimbursements to TSA?

To gain background and knowledge regarding the collection and remittance of security fees, we reviewed Public Law 107-71, *Aviation and Transportation Security Act*; applicable Federal Regulations, Register and notices; TSA press releases on security fees; prior federal audits relating to the fees, and various congressional reports and newspaper articles that were applicable.

We conducted the audit from February 2004 through February 2005. We initiated the audit at TSA headquarters to identify program policies, procedures, and controls used in monitoring fee payments. We reviewed records from a different large, medium, and small air carrier for each type of fee. For the passenger security fee, we reviewed tickets, accounting records, and other supporting data. For the ASIF review, we reviewed accounting records, CPA audits, air carrier databases, invoices, and other supporting documents. The ASIF review also included a review of invoices, databases, real estate documents, and other supporting documents at 13 airports and 3 private security contractor facilities²⁴ to identify and corroborate air carrier expenses incurred during CY 2000. See Appendix D for a complete description of the work performed and results of passenger security fee remittance procedures. Appendix E provides information on how tickets were sold.

²⁴ Five private security contractors were in our sample and interviewed; however, only 3 provided the listed documents.

As discussed below, audit fieldwork consisted of three distinct review components: TSA Headquarters, passenger security fees, and the aviation security infrastructure fees.

TSA Headquarters. Audit work at TSA Headquarters in Arlington, VA included researching the history of, and obtaining background information on both security fees. We interviewed Office of Revenue personnel to identify TSA guidelines and program policies and procedures used in the collection of the security fees. We reviewed TSA's database of air carriers responsible for remitting security fees, evaluated TSA's monitoring practices and controls over the collection and remittance of the fees, and reviewed applicable management and monitoring reports. We also interviewed regulatory audit division personnel at U.S. Customs and Border Protection to gain an understanding of their methodology for auditing air carriers' collection of international passenger user fees. This methodology was used for the passenger security fee component of this audit and was an agreed upon method with the air carriers reviewed. Lastly, we spoke to U.S. Department of Transportation, Office of Inspector General personnel to identify methodologies used in a previous audit of the Aviation Security Infrastructure Fee.

Passenger Security Fees. Audit work was completed at a large, medium, and small air carrier using the following methodology to categorize the air carriers. We judgmentally selected FY 2003 as the base year for our review and determined that 174 air carriers paid nearly \$1.1 billion in passenger security fees. We sorted air carrier payments in descending order and selected the top 50 air carriers. Subsequently, we eliminated foreign air carriers and air carriers that paid less than \$5 million and stratified the passenger security fee payments of the remaining 16 air carriers using the following criteria: a large air carrier made over \$50 million in passenger security fee payments, a medium air carrier made between \$10 million and \$50 million in payments, and a small air carrier made under \$10 million in payments. We then selected one air carrier from each group to review.

For the small and medium air carriers, we randomly selected about eight flights per air carrier over a 25-month period.²⁵ However, for the large air carrier, the flights were selected over a 6-month period due to limited records retention. We based our selections on flight origins and destinations to obtain larger volume flights and we excluded the fee suspension period from our review. Generally, we performed a 100 percent review of one flight per CY quarter to determine whether passengers paid the \$2.50 passenger security

²⁵ The review period was from the initial collection of security fees (February 2002) to the beginning of on site audit fieldwork (February 2004).

fee based on applicable flight segments. To increase air carrier acceptance of our methodology, each air carrier selected the day in each quarter for the review.²⁶ We identified each flight manifest and disallowed any tickets not sold using the air carriers' ticket stock.²⁷ We also reviewed tickets for proper payment based on TSA guidance for one-way and round-trips focusing on the number of collected and remitted segments. In total, we examined, 2,610 tickets with 6,730 flight segments.

Air carriers identified the passenger security fee on each ticket under the code AY. We reviewed ticket itineraries and identified the number and dollar value of AY segments that should have been paid and then added these unpaid segments to the AY fees actually paid. To determine air carrier collection error rates, we first divided the unpaid AY fees by the total AY fees and subtracted this percentage from 100, thus computing the percentage of fees air carriers actually collected. We then divided the total AY fees collected for all flights by this percentage to identify what the air carrier should have collected. This amount resulted in the underpayment. Based on the precedence set by U.S. Customs and Border Protection for its audits of international passenger fees and the acceptance of that audit methodology by the air carrier industry, we projected the error rate against each air carrier's total AY fee collections for the period reviewed to determine the total underpayment.

Aviation Infrastructure Security Fees. Audit work was completed at a different large, medium, and small air carrier using the following methodology to categorize the air carriers. We judgmentally selected FY 2003 as the base year for our review and determined that 167 air carriers paid \$203.2 million infrastructure security fees. We sorted the air carrier payments in descending order and selected the top 50 air carriers. Subsequently, we eliminated foreign air carriers and judgmentally grouped the remaining 32 air carriers into three categories as follows: a large air carrier had over \$15 million in ASIF payments, a medium air carrier paid between \$2 million to \$15 million, and a small air carrier paid under \$2 million. We then selected one air carrier from each group ensuring that the air carriers differed from those chosen for our passenger security fees review. We performed audit work at the 3 air carriers corporate headquarters, at 5 passenger and property screening contractors that provided security services to the air carriers, and at 13 national airports where the air carriers operated.

Air Carrier Review. We accomplished this portion of the review to identify and assess the supporting documentation behind the ASIF amounts reported

²⁶ This methodology was similar to the U.S. Customs and Border Protection's audit methodology for international passenger fees that previously had been accepted by the air carriers.

²⁷ An example of this disallowance would be where a secondary air carrier sold and collected a portion of the ticket on a flight operated by a different air carrier.

on the Appendix A. The small air carrier provided original invoices and we reviewed almost 100 percent of the invoices supporting Appendix A costs. The medium and large air carriers could not provide original invoices but rather provided photocopies or microfiche copies of invoices. For both air carriers, we took a representative sample of invoices focusing primarily on air carrier costs at large airports and air carrier hubs. For the medium air carrier, we reviewed supporting documentation for about \$14.5 million in reported Appendix A costs and for the large air carrier, we reviewed over \$10.4 million in documentation.

Passenger and Property Screening Contractor Review. To verify that the three air carriers reported all appropriate Appendix A costs, we visited and asked five passenger and property screening contractors to (1) provide supporting documentation for total screening service costs billed during CY 2000 to those air carriers, and (2) identify specific screening costs at 13 airports included within the scope of this audit. The contractors visited included Cognisa Security (formerly Argenbright) in Atlanta, GA; Globe Aviation in Irving, TX; ICTS Technologies (formerly Huntleigh) in New York, NY and St. Louis, MO; Olympic Security in Tukwila, WA; and Wackenhut Corporation in Palm Beach Gardens, FL.

National Airport Review. We performed audit work at 13 national airports to assess how the airports billed the air carriers for passenger and baggage related screening services including costs related to rent, utilities, and law enforcement. The national airports visited were: Ronald Reagan Washington National Airport in Arlington, VA; Dulles National Airport in Dulles, VA; Baltimore Washington International in Linthicum, MD; Logan International Airport in East Boston, MA; Newark International Airport in Newark, NJ; JFK International Airport in Jamaica, NY; Los Angeles International Airport in Los Angeles, CA; LaGuardia International Airport in Flushing, NY; Oakland International Airport in Oakland, CA; Ontario International Airport in Ontario, CA; San Diego International Airport in San Diego, CA; San Francisco International Airport in San Francisco, CA; and San Jose International Airport in San Jose, CA.

This audit was conducted under the authority of the Inspector General Act of 1978, as amended, and according to *Government Auditing Standards* issued by the Comptroller General of the United States.

Office of the Assistant Secretary

U.S. Department of Homeland Security
601 South 12th Street
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FEB 12 2 2006



Transportation
Security
Administration

INFORMATION

MEMORANDUM FOR: Richard L. Skinner, Inspector General
Department of Homeland Security

FROM: Kip Hawley *KH*
Assistant Secretary

SUBJECT: Formal response to the Department of Homeland Security (DHS) Office of Inspector General Report "Review of the Transportation Security Administration (TSA) Collection of Aviation Security Service Fees," OIG-06-XX, March 2006

Purpose

This memorandum constitutes the Transportation Security Administration's (TSA) formal agency response to the Department of Homeland Security (DHS) Office of Inspector General Report "Review of the Transportation Security Administration (TSA) Collection of Aviation Security Service Fees," OIG-06-XX, March 2006. TSA thanks the DHS Office of Inspector General (OIG) for their work in planning, conducting, and issuing this study. The review is the culmination of a 2-year effort that will greatly assist TSA in furthering the administration of two very important aviation security fees. The recommendations identified in this review will help facilitate the continued collection of funding streams necessary to ensure aviation security throughout the nation.

Background

As recommended in the review, TSA will continue to develop and implement a robust compliance program to ensure the legal and equitable collection of the September 11th Security Fee. The program will identify, and ensure payment of, all fees provided for in the September 11th Security Fee Federal Regulation. Initial findings from the compliance program demonstrate a 99 percent collection rate. Concurrently, TSA will continue to work with air carriers to ensure full collection of this fee.

Discussion

TSA has made significant progress in the implementation of the Aviation Security Infrastructure Fee (ASIF). As recommended in the review, TSA has determined a fair and reasonable industry-wide ASIF. Through this recent determination, TSA has addressed a long-standing concern with this security fee. Additionally, TSA has addressed the unilateral decision by some air carriers to withhold portions of the ASIF.

Recent correspondence to the air carrier community should eliminate the need for further enforcement action regarding outstanding ASIF liabilities. TSA will continue to pursue a "current market share" approach for implementation of the ASIF, shifting the basis of the ASIF from calendar year 2000 costs to a method that fairly measures an air carrier's current market share. In moving to this new ASIF allocation, TSA will consider the numerous and diverse methodologies proposed by the air carrier community.

Passenger Fees

OIG has determined that there are some specific situations in which air carriers have not been fully collecting and remitting passenger fees in accordance with title 49 of the Code of Federal Regulations (49 CFR), part 1510, TSA's regulation establishing its air carrier passenger fee. TSA's own audit program has yielded similar results. The agency continues to both strengthen its audit program and address any issues that have prevented full collection of the airline passenger fee.

Air Carrier Fee

For their review, OIG attempted to validate for three air carriers the cost information each one submitted on their 2000 costs of passenger and property screening. These costs form the basis of TSA's air carrier fee. The regulation establishing this fee, 49 CFR, part 1511, required air carriers to submit information on these costs directly to TSA. The OIG review concludes that while their auditors were able to ascertain that the individual air carrier cost submissions were incomplete, the OIG staff was unable to determine how much additional cost each air carrier should have added to their submission. The reasons for OIG's inability to make this final determination are summarized on page 14 of their report.

TSA continues to be disappointed that many air carriers were unable to produce the full cost information necessary to provide the agency with the information it needed to determine how much each air carrier should pay in air carrier fees, despite the agency's efforts to facilitate this process. As a result, TSA has been unable to rely on the cost information provided by many air carriers to make its final determination. Instead, TSA agrees with the OIG that the agency should base its final determination of the industry 2000 passenger and property screening costs on the analysis provided by the Government Accountability Office in their April 20, 2005 report: "Review of Air Carriers' Year 2000 Passenger and Property Screening Costs."

TSA appreciates the time and resources that the DHS OIG has devoted to this important review. The recommendations and findings of this report will help to develop a more effective, efficient, and economical administration of TSA's aviation security fees.

Attachment

TSA Response to OIG Recommendations:
"Review of the Transportation Security Administration (TSA)
Collection of Aviation Service Fees"

Recommendation 1: Collect the \$2.7 million in unpaid passenger security fee amounts identified in this report and continue efforts to validate that all air carriers not covered by this audit have accurately collected and remitted all passenger security fees. (Passenger Fee)

TSA concurs. TSA action on this recommendation is pending receipt of the OIG documentation that would allow TSA to invoice the carriers for due amounts. Absent the information requested, TSA would be forced to undertake repeat audits incurring additional costs and delays.

In extrapolating to the entire industry the OIG findings relative to the reported finding on three carriers, TSA notes that the collection efforts exceed over 99 percent success. TSA will continue to seek improvements. In that regard, TSA has established an audit program with U.S. Customs and Border Protection (CBP), as discussed in recommendation 2, below, which will assist in this effort.

Recommendation 2: Continue efforts to develop and implement a viable plan to perform an increased number of annual passenger security fee audits incorporating the issues raised by this audit and any others identified in the audits performed by Customs and Border Protection personnel. (Passenger Fee)

TSA concurs. Since the OIG audit began in January 2004, TSA has implemented a Memorandum of Understanding with CBP's Regulatory Audit Division to provide compliance audits. TSA has decided the best use of resources is to outsource on-site audit work to CBP. While CBP was unable to supply all the desired audits in FY 2004 due to DHS restructuring (INS/APHIS auditors), they have conducted 12 audits in FY 2005 and plan to complete 13 more in FY 2006. TSA intends to audit the major carriers every three years and other carriers less frequently due to the expense of conducting such audits. There is little risk to the Government as audit findings are applied retroactively and the air carriers are invoiced for the outstanding amounts. Audits of air carriers continue to show very high levels of compliance.

Recommendation 3: Enforce the interim final rule on passenger security fees as clarified by Docket 10, and resolve ticket reservation system software issues with the airline industry to assure collection and remittance of all passenger security fees on future air carrier tickets. (Passenger Fee)

TSA concurs. Since the OIG audit began, TSA has had further discussions with various air carriers and associations to better understand any issues that have arisen on implementing the passenger fee. Air carriers have asked for further clarification and/or future changes on several specific aspects of the regulation. TSA is still considering the merits of making any such changes. TSA is also awaiting the results of its passenger fee audit program to determine whether there are other changes that it may need to consider. However, it is important to recognize that TSA's audits have shown that these discrepancies only affect about 1 percent of the fees collected. Where appropriate, TSA has already initiated action to collect any outstanding passenger fees.

Recommendation 4: Determine a fair and reasonable aggregate ASIF amount and collect the fees envisioned by ATSA, where applicable, based on the results of this audit and GAO's analysis and estimates. (Air Carrier Fee)

TSA concurs. TSA has recently determined a fair and reasonable aggregate ASIF amount and a means of allocating those additional costs among air carriers. In taking its decision on the aggregate industry amount subject to collection, TSA carefully considered the work reported in the April 16, 2005 GAO report.

The Aviation and Transportation Security Act (ATSA) established two aviation fees to fund TSA's aviation security requirements (49 USC § 44940). One of these fees, the ASIF (49 CFR part 1511), is paid by air carriers and the overall amount is capped by the aggregate of costs paid by all air carriers in CY 2000 for screening passengers and property. The per-carrier limit is capped at the amount expended by that individual air carrier in CY 2000. This cap will remain in effect until TSA revises the per-carrier limit by market share or any other appropriate method (49 USC §§ 44940(a)(2)(B)(ii), (iii)).

According to the ATSA requirement that the ASIF be based on each air carrier's CY 2000 aviation security costs, TSA required each air carrier to complete and submit a cost questionnaire to the agency in May 2002, along with an independent audit of this questionnaire. In the FY 2005 DHS Appropriations Act, Congress required GAO to conduct a review of these

costs. In the resulting report, GAO concluded that the industry-wide aviation security costs were between \$425 and \$471 million with a midpoint mark of \$448 million, compared with the air carriers' reported costs totaling \$319 million, leaving an annual gap of \$129 in underreported, uncollected ASIF²⁸.

To ensure fairness and consistency in the allocation of the underpayments, TSA first made adjustments for three categories of air carriers: 1) carriers that existed in 2000, but did not report any ASIF costs; 2) carriers that noted ASIF costs, but did not include those costs in their ASIF calculations; and 3) carriers that reported ASIF costs, but no longer operate. TSA made these adjustments to avoid overcharging the air carriers that are currently operating. These three adjustments, subsequent to the GAO report, raise the overall originally reported ASIF to \$344 million. Compared to the \$448 million reported by GAO, this leaves a \$104 million underpayment that must be allocated equitably and in accordance with the law among qualifying air carriers.

Using the GAO Report as guidance, TSA has validated an additional \$104 million in underreported screening costs and has determined an underpayment for each qualifying air carrier beginning January 1, 2005.

The FY 2005 DHS Appropriations Act states: "*beginning with amounts due in calendar year 2005, if the result of this review is that an air carrier or foreign air carrier has not paid the appropriate fee to the Transportation Security Administration pursuant to section 44940(a)(2) of title 49 United States Code, the Secretary of Homeland Security shall undertake all necessary actions to ensure that such amounts are collected.*" On January 3, 2006 TSA sent out a cover letter and invoice to each carrier subject to the underpayment for the period of January 1 through December 31, 2005.

The letter also included the additional ASIF liability due for future periods. Beginning with the ASIF due for the month of January 2006, and for every month thereafter, each assessed carrier must remit both the ASIF based on reported costs (required by 49 CFR §§ 1511.5 and 1511.7; and 69 Fed. Reg. 58943) and the additional monthly ASIF.

Recommendation 5: Resolve outstanding issues raised by the air carriers, e.g. duplicative costs, or otherwise referenced in this report, e.g., rent methodology, LEO methodology, and inconsistent reporting, if TSA continues to utilize the Appendix A as the basis for aggregate ASIF collections from the air carriers. (Air Carrier Fee)

²⁸ The GAO report "Aviation Fees: Review of Air Carriers' Year 2000 Passenger and Property Screening Costs" is available on the TSA website (<http://www.tsa.gov/public/display?theme=31>).

TSA concurs. As acknowledged by the OIG in their audit report on page 16, TSA purposely provided broad guidance to the air carriers on preparing their response to the cost questionnaire (Appendix A). This broad guidance was sufficient for approximately one-half of the air carriers subject to this fee to provide TSA with opinions from their independent auditors on the completeness of the data they submitted in their cost questionnaire using the guidance provided by TSA. The agency continues to rely on the air carrier cost questionnaire submissions as the basis for the air carrier fee allocation. However, TSA is unable to rely on the completeness of questionnaires for those air carriers that were unable to substantiate their cost submissions by receiving an unqualified audit opinion. Therefore, TSA has relied on the approach initiated by GAO to identify the level of industry-wide understated costs and the agency has allocated those costs on the basis of the formula described in Audit Finding 4 above.

Recommendation 6: Continue with the determination of the per air carrier ASIF amount based on implementation of Recommendations 4 and comments received from air carriers. (Air Carrier Fee)

TSA concurs.

Recommendation 7: Initiate enforcement actions against the seven air carriers that fail to remit ASIF amounts mandated by ATSA and other air carriers who fail to comply with ATSA and TSA regulations. (Air Carrier Fee)

TSA concurs. On December 2, 2005, TSA sent Demand Letters to the seven air carriers that had failed to remit ASIF amounts mandated by the regulations establishing the Air Carrier Fee. Those air carriers not subject to a bankruptcy proceeding have paid or completed payment agreements that cover all of the amounts due to TSA from inception of the fee. Where permissible, TSA is working with the Department of Justice to claim amounts due through the appropriate bankruptcy court.

Nov. 19, 2001	Public Law 107-71, <i>Aviation and Transportation Security Act</i> , created TSA and established passenger security fee and ASIF requirements.
Dec. 31, 2001	TSA issued an interim final rule on Passenger Civil Aviation Security Service Fees requiring air carriers to establish and maintain an accounting system to account for the security fees imposed, collected, refunded, and remitted.
Jan. 8, 2002	ATA requested clarification from DOT regarding passenger security fee assessments for hypothetical travel itineraries (Docket 6).
Jan. 25, 2002	DOT provided clarification to ATA’s passenger security fee assessment request (Docket 10).
Feb. 1, 2002	TSA required air carriers to start collecting passenger security fees from this date forward and to remit the fees to TSA monthly by last calendar day of the following month.
Feb. 20, 2002	TSA published interim final rule on Aviation Security Infrastructure Fee, effective February 18, 2002 and required that air carriers remit 1/12 of the fees to TSA by last calendar day of each month.
Mar. 1, 2002	ATA requested further discussion regarding DOT’s January 25, 2002 clarification of passenger security fee assessments.
May 18, 2002	TSA established this date as the deadline for the Appendix A submissions.
Jul. 1, 2002	TSA initially established this date as the deadline for independent audits of Appendix A submissions.
Dec. 31, 2002	TSA extended the final deadline for independent audits of Appendix A submissions to this date.
Jun. 1, 2003 to Sept. 30, 2003	Congress suspended both passenger security fee and ASIF collections during this 4-month period.
Apr. 20, 2004	TSA received authority to impose civil monetary penalties on air carriers for non-compliance with regulations.

Oct. 1, 2004 Effective on this date, ATSA gave TSA authority to determine a per-air carrier ASIF amount based on each air carrier’s market share of the industry or any other reasonable measurement. (Note: As of the end of our fieldwork, TSA continued assessing ASIF amounts based on previously imposed fee amounts.)

We tested the air carriers' accounting systems to evaluate the reliability of passenger security fee remittance processes and to assess whether the air carriers properly accounted for and remitted to TSA the fees generated from ticket sales. We accomplished these tests by tracing tickets from daily sales reports to general ledger postings. Appendix E provides additional information on how tickets were sold through different sales channels. We determined that the small and large air carriers had adequate accounting systems to track the passenger security fee remittance. However, we could not express an opinion on the medium air carrier's system because of the manner in which the air carrier accounted for passenger security fees collections.

Small Air Carrier. We tested 10 tickets purchased through 8 different sales channels to evaluate the reliability of the air carrier's general ledger. We traced ticket sales and actual passenger security fee amounts to postings of the fees to the daily and monthly sales reports. We then traced monthly sales report amounts to the journal entries leading to the general ledger. We also evaluated whether the general ledger journal entries and account codes supported the passenger security fee amounts remitted to TSA. We determined that the air carrier remitted all passenger security fees it collected to TSA.

Medium Air Carrier. The medium air carrier did not maintain a system that identified each individual ticket sold along with the corresponding passenger security fee. Rather, the air carrier tracked the total number and dollar amount of tickets sold daily and commingled the amounts collected into one large lump sum for that day for each type of sales channel. The individual passenger security fee segments could not be traced back to a particular ticket unless a manual review was conducted for each ticket sold on a particular day.

We tracked the passenger security fee from one ticket purchased on a credit card and followed the amount through to the general ledger. However, if there had been refunds in this sales channel, the validity of the test could be questioned as a refund could have affected the ticket in question. As a result, OIG does not express an opinion on the accuracy or reliability of the air carrier's remittance process. An air carrier official told us that its internal auditor is developing a mapping matrix of the collection process and will test the reliability in the future.

Large Air Carrier. At the large air carrier, three tickets were tested through two different sales channels. No problems were identified for the air carrier's revenue collection system.

We evaluated the month end passenger security fee payments from the three air carriers to TSA. Outgoing monthly wire transfers were reviewed at the air

carriers and compared to incoming wire transfers at TSA for proper payment and timeliness with no problems identified. We did not identify any legislative reporting requirements or timeliness issues that need to be corrected by TSA.

We identified that the air carriers in our review used many different types of sales channels to sell tickets. The accurate collection of passenger security fees can be difficult because different air carrier controls for each sales channel. We identified the following primary sales channels during our review.

ATAC – “Automated Ticket Agent Checkout”. This sales channel includes tickets sold at airports and city ticket offices, and on the internet.

ARC – “Airline Reporting Corporation”. This is the sales channel for all domestic U.S. travel agencies. This channel represents the largest percentage of all tickets sold.

BSP – “Bank Settlement Plan”. Many foreign countries use this sales channel.

GSA – General Sales Agent and international ticket brokers use this channel.

MSTA – “Manual Station”. This channel is generally used by small countries and the ticket can be handwritten for travel into and out of the U.S.

MTTA – “Manual Travel Agency”. Small ticket agencies generally use this sales channel.

WHOL – This sales channel relates to wholesalers who sell tickets using the air carriers’ ticket stock.

BILB – “Billbacks”. This sales channel occurs when an air carrier bills a travel agency or wholesaler after they take the ticket from the passenger upon entering the plane. (Note: The air carrier did not sell the ticket and is not reimbursed until the passenger flies.)

In Docket 6, ATA requested guidance on how to assess passenger security fees for one-way trips and roundtrips, based on hypothetical travel itineraries. In Docket 10, DOT assessed the applicable passenger security fees for each travel itinerary. Using travel itineraries proposed in Docket 6, the examples below show how the passenger security fee assessments differed between the Docket 10 criteria and current air carrier industry practices.

Itinerary A

<u>Depart</u>	<u>Arrive</u>
Los Angeles	Honolulu
Honolulu	Kona (stopover)
Kona	Honolulu
Honolulu	San Francisco

Docket 10

This itinerary begins with a passenger enplaning in Los Angeles and again in Honolulu before terminating travel in Kona. Next, the passenger enplanes in Kona and Honolulu, and then terminates travel in San Francisco. Docket 10 defines this itinerary as two one-way trips. Because the passenger enplaned twice during each of these one-way trips, a \$5.00 fee would be charged for each trip for a total of \$10.00. In addition, since the focus of the passenger fee is on “enplanements,” a “stopover” in Kona would not be relevant when calculating the fee amount.

Air Carrier Industry Practice

This itinerary does not terminate at the origin point of Los Angeles. Thus, this is a one-way trip regardless of stopovers, with four one-way enplanements. Because the passenger fee for a one-way trip is limited to two enplanements, at \$2.50 per enplanement, the total fee charged would be \$5.00.

Itinerary B

<u>Depart</u>	<u>Arrive</u>
JFK	Los Angeles (stopover)
Los Angeles	Kahului (stopover)
Kahului	Kona (stopover)
Kona	Honolulu (stopover)
Honolulu	San Francisco (stopover)
San Francisco	Washington Reagan

Docket 10

This itinerary describes a passenger enplaning an aircraft six times with travel terminating each time at airports in the United States that are not co-terminals.

Docket 10 defines this itinerary as six one-way trips. Thus, the air carrier would charge a fee of \$2.50 for each enplanement for a total of \$15.00.

Air Carrier Industry Practice

This itinerary does not terminate at the origin point of John F. Kennedy. Therefore, it is a one-way trip regardless of stopovers, with six one-way enplanements. Since the passenger fee for a one-way trip is limited to two enplanements, at \$2.50 per enplanement, the total fee charged would be \$5.00.

Itinerary C

<u>Depart</u>	<u>Arrive</u>
Orlando	Pittsburgh (stopover)
Pittsburgh	Orlando (stopover)
Orlando	Pittsburgh (stopover)
Pittsburgh	Orlando (stopover)
Orlando	Pittsburgh (stopover)
Pittsburgh	Orlando

Docket 10

This itinerary shows a passenger with travel terminating three times at the origin point, which would be considered three round trips. The passenger enplaned twice during each round trip. Therefore, the air carrier would collect a fee of \$5.00 for each round trip for a total of \$15.00.

Air Carrier Industry Practice

This itinerary terminates at the origin point of Orlando. Thus, it would be considered a round trip regardless of stopovers, with six enplanements. Because the passenger fee for a round trip is limited to four enplanements, at \$2.50 per enplanement, the total fee charged would be \$10.00.

Small Air Carrier Appendix A Costs and Port Authority Audited Amounts

<u>Airports</u>	<u>App. A - Rent</u>	<u>Per Audit</u>	<u>App. A - LEO</u>	<u>Per Audit</u>
Boston – BOS	\$0	\$0	\$6,994	\$6,797
Baltimore – BWI	\$0	\$287	\$21,170	\$5,146
Reagan – DCA	N/A	N/A	N/A	N/A
Newark – EWR	N/A	N/A	N/A	N/A
Dulles – IAD	N/A	N/A	N/A	N/A
New York –JFK	N/A	N/A	N/A	N/A
Los Angeles - LAX	\$0	\$0	\$0	\$0
LaGuardia – LGA	\$0	\$3,700	\$0	\$0
Oakland – OAK	N/A	N/A	N/A	N/A
Ontario – ONT	N/A	N/A	N/A	N/A
San Diego – SAN	\$0	\$199	\$0	\$0
San Francisco – SFO	\$0	\$13,813	\$0	\$18,820
San Jose – SJC	N/A	N/A	N/A	N/A
Total	\$0	\$17,999	\$34,164	\$30,763

N/A – Air Carrier did not use airport.

Small Air Carrier Results – Rent Underpaid \$17,999 LEO Overpaid \$3,401

Total Underpayment \$14,598

Medium Air Carrier Appendix A Costs and Port Authority Audited Amounts

<u>Airports</u>	<u>App. A - Rent</u>	<u>Per Audit</u>	<u>App. A - LEO</u>	<u>Per Audit</u>
Boston – BOS	\$83,425	\$0	\$0	\$122,452
Baltimore – BWI	\$2,447	\$2,137	\$0	\$38,378
Reagan – DCA	\$0	\$32,517	\$0	\$155,496
Newark – EWR	\$325,944	\$325,944**	\$0	\$1,523,280
Dulles – IAD	\$0	\$5,655	\$0	\$9,321
New York –JFK	\$0	\$0**	\$0	\$0
Los Angeles - LAX	\$14,594	\$0	\$0	\$0
LaGuardia – LGA	\$16,016	\$36,000	\$0	\$83,264
Oakland – OAK	\$450	\$1,147	\$0	\$0
Ontario – ONT	\$1,165	\$5,396	\$0	\$0
San Diego – SAN	\$3,475	\$2,840	\$0	\$0
San Francisco – SFO	\$0	\$80,043	\$0	\$109,944
San Jose – SJC	\$20,398	\$3,968	\$0	\$0
Total	\$467,914*	\$495,647	\$0	\$2,042,135

* Appendix A Rent was footnoted and not actually paid.

** Unable to verify.

The rent analysis shows that had they paid the amount, they still would have been short.

Medium Air Carrier Results – Rent Underpaid \$27,191 LEO Underpaid \$2,042,135

Total Underpayment \$2,069,326

Large Air Carrier Appendix A Costs and Port Authority Audited Amounts

<u>Airports</u>	<u>App. A - Rent</u>	<u>Per Audit</u>	<u>App. A - LEO</u>	<u>Per Audit</u>
Boston – BOS	\$0	\$0	\$0	\$88,828
Baltimore – BWI	\$0	\$3,297	\$0	\$59,091
Reagan – DCA	\$0	\$25,608	\$0	\$122,033
Newark – EWR	\$0	\$0**	\$0	\$317,030
Dulles – IAD	\$0	\$143,786	\$0	\$349,614
New York –JFK	\$0	\$0**	\$0	\$611,959
Los Angeles - LAX	\$0	\$0	\$0	\$0
LaGuardia – LGA	\$0	\$75,000	\$0	\$216,685
Oakland – OAK	\$0	\$11,736	\$0	\$0
Ontario – ONT	\$0	\$79,328	\$0	\$0
San Diego – SAN	\$0	\$10,338	\$0	\$0
San Francisco – SFO	\$0	\$1,011,920	\$0	\$1,353,786
San Jose – SJC	\$0	\$16,172	\$0	N/A
Total	\$0*	\$1,377,185	\$0	\$3,119,026

* Appendix A Rent was footnoted and not actually paid. Amount not available by airport.

**Unable to verify.

Large Air Carrier Results – Rent Underpaid \$1,377,185 LEO Underpaid \$3,119,026

Total Underpayment \$4,496,211

LEO costing methodologies. To illustrate the complexities in determining air carrier LEO costs, a large airport in California allocated all LEO costs to maintenance and operations expenses--an off terminal site cost center. The airport then added these costs with other cost centers such as airfield and apron, and built these costs into landing fee rates. However, no direct nexus existed between passenger and property screening costs and the landing fee rate. While the air carriers at this airport did not report LEO costs to TSA, it is reasonable to believe LEOs were frequently needed and used at passenger and property screening areas. Another California airport used a double residual methodology, where some LEO costs were factored into the air carriers' terminal rates and another portion into their airfield rates.

To determine applicable Appendix A costs for the LEO expenses at national airports, we spoke to airport officials and gathered documents relating to rates and charges. Based on these meetings, airport records, and individual airport methodologies, we reconstructed LEO costs for the three air carriers in our sample. In all cases, we made subjective decisions for distributing rates and charges based upon each airport's billing practices and methodology. For example, one airport in the Washington, D.C. area billed the air carriers for LEO expenses based upon passenger enplanements. This airport established a cost center totally dedicated to terminal security requirements that represented 35 percent of total airport security costs. Airport officials stated that the air carriers should report 100 percent of this cost center on their Appendix A submission. We applied the same methodology at this airport. We used LEO costs identified by airport officials for the whole terminal and then factored this amount against each air carriers' passenger enplanement percentage. While the air carriers could argue that LEOs perform many different duties in the terminal, we concluded that this method of determining Appendix A LEO costs resulted in an amount that should be considered in connection with the screening of passengers and property. In addition, these airport officials did not make any distinctions regarding LEO duties performed within a terminal.

Rent costing methodologies. Two examples of these differing methodologies are presented below:

- An airport in the Washington, D.C. area determined an air carrier's rent predicated on rentable terminal space consisting of areas available for lease and common use premises. For all signatory air carrier space, this airport factored in the use of the terminal space (exclusive use, preferential use, joint use and common use space where the passenger security checkpoints were located). Further, rental rates differed by type of terminal space and an air carrier's rent bill could include a combination of costs in the above categories. The air carrier would then need to decide what portion of their rent charges were directly related to passenger and property screening.
- A different airport in the Washington, D.C. area used an 80/20 methodology to charge rent. The airport directly billed all signatory air carriers' evenly for 20 percent of the terminal costs based on square footage. The airport then charged the remaining 80 percent to all air carriers based on enplaned passenger counts. At this airport, two of three air carriers were signatory air carriers. Because 100 percent of

the space in the terminal did not relate exclusively to passenger and property screening, for Appendix A purposes, air carriers needed to: (1) determine the percentage of security checkpoint square feet to the total terminal square feet, (2) apply this percentage to the airport's rent charges, and (3) determine the percentage of this amount applicable to the Appendix A when numerous air carriers shared the security checkpoint.

We could not independently determine a completely accurate Appendix A amount for passenger and property screening contractors because of the following limitations and issues.

- The contractors' accounting systems did not segregate passenger and property screening costs from other non-passenger and property screening costs provided to the air carriers during CY 2000 (e.g., skycap and wheelchair services).
- The contractors could not provide us any data on the total dollar cost the air carriers paid for passenger and property screening at the airports across the nation. Because of this, we took a bottom-up approach by necessity and piecemealed passenger and property screening costs together as best we could under the circumstances. For example, we started with contractor invoices or databases listing invoices for the airports where we previously had received billing information from the air carriers. We then reconciled the contractor and air carrier data to determine the accuracy of what the air carriers claimed supported their Appendix A submissions. In some cases, that meant either adding or subtracting costs such as freight, taxes, non-passenger and property screening services, etc. from contractor invoices. We also used any other form of supporting documents that showed billings from contractors or payments by air carriers.
- The contractors no longer perform passenger and property screening services, records were boxed up in different warehouses, and when available, the 4-year old records were not categorized and filed in a manner to easily identify costs for Appendix A purposes.
- Two of the three air carriers in our review could not provide us detailed cost summaries of passenger and property screening services provided by contractors at each airport. We did receive some contractor billing information at the air carriers and these costs were compared against the contractor's records when available.

We asked the first contractor to provide passenger and property screening cost data for seven airports where the large air carrier operated. The contractor lacked sufficient data at two airports for comparing contractor cost with air carrier cost. For three other airports, either the contractor or the air carrier lacked the documentation or sufficient information on the documents needed to reconcile the amounts. For the two remaining airports, we reconciled 50 percent of the invoices for one airport and 65 percent for the other. Our

Appendix H

Review of Costs Paid to Passenger and Property Screening Contractors During CY 2000

reconciliation showed that \$346,080 in applicable contractor costs were not included in the air carrier's records. Therefore, the large air carrier did not include this amount in the Appendix A. Furthermore, the amount not included in the Appendix A would likely have been greater if we could have reconciled the remaining invoices and if we had access to cost documentation for the five airports not reviewed.

Similar to the first contractor, \$28,154 in the second contractor's passenger and property screening invoices could not be reconciled to the costs reported in the Appendix A of the large air carrier. We reconciled invoices between the small air carrier and the contractor and observed no discrepancies. However, we could not compare the contractor's invoices at the medium air carrier due to insufficient detail.

The third contractor also had \$105,983 in invoiced passenger and property screening costs not identified in the Appendix A of the large air carrier. We performed limited review work for the other two air carriers in our sample and identified no underreported amounts.

To monitor the collection of the passenger security fee and air carrier security infrastructure fee payments, TSA program analysts use the following kinds of tracking sheets.

1. Universe data tracking sheet. This identifies information such as all applicable air carriers' monthly and year to date payments.
2. Passenger fee non-payments listing. This identifies all air carriers who have not paid passenger security fees and ASIF.
3. Appendix A tracking sheet. This identifies all air carriers who did not file an Appendix A and identifies which air carriers filed the appendix late.
4. Issue tracking sheet. This details conversations held with various air carriers regarding any program concerns.
5. Payment sheet. This identifies whether air carrier payments are current and identifies each air carrier balance to TSA.
6. Air carrier payment schedule. This summarizes payment time frames, dollars received and dollars due.
7. Audit summary. This identifies the date that 125 air carriers received an audit opinion on whether their Appendix A costs were fair and reasonable.

Appendix J
Major Contributors to This Report

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Chief Financial Officer
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Chief Security Officer
DHS GAO/OIG Audit Liaison

Transportation Security Administration

Assistant Secretary
TSA Audit Liaison

Office of Management and Budget

Chief, Homeland Security Bureau
DHS OIG Budget Examiner

Congress

Committee on Homeland Security and Governmental Affairs
United States Senate

Committee on Homeland Security
United States House of Representatives

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