U.S. Department of Agriculture
Office of Inspector General
Great Plains Region
Audit Report

Monitoring of RMA's Implementation of Manual 14 Reviews/Quality Control Review System

Report No.
05099-14-KC
March 2002

UNITED STATES DEPARTMENT OF AGRICULTURE

OFFICE OF INSPECTOR GENERAL
Washington, D.C. 20250

DATE: March 15, 2002

REPLY TO
ATTN OF: 05099-14-KC

SUBJECT: Monitoring of Risk Management Agency's Implementation of Manual 14 Reviews/Quality Control Review System

TO: Ross L. Davidson, Jr.
Administrator
Risk Management Agency

ATTN: Garland Westmoreland
Deputy Administrator
Risk Compliance

This report presents the results of our review of the Monitoring of Risk Management Agency's (RMA) "Implementation of Manual 14 Reviews/Quality Control Review System". Your October 24, 2001, response to the draft report is included as exhibit A with excerpts and the Office of Inspector General's position incorporated into the relevant sections of the report.

The response showed general concurrence with Recommendations Nos. 1, 2, and 3. Before we can consider the management decisions for these three recommendations, we need to be provided details specifying the objectives, tasks, and milestones for accomplishing the program delivery process study including clarification on those tasks addressing the RMA quality assurance system. We also need to be provided the overall timetable and contemplated actions for implementing the study's results relative to a new approach for a RMA quality assurance system, codifying this system in regulations and specifying those alternative actions to be taken for the interim period. For Recommendation No. 4, RMA does not believe that the report has provided sufficient evidence or justification showing the operation of this activity, is such, that it meets the criteria for reporting material weaknesses defined under the Federal Manager's Financial Integrity Act. We disagree because RMA's quality assurance system in place does not meet standards for internal control in the Federal Government. Also, the ineffective quality assurance system in place does not provide any reliable measure of the extent of erroneous payments within the Federal Crop Insurance Program.

In accordance with Departmental Regulation 1720-1, please furnish a reply within 60 days clearly describing the corrective action taken or planned and the timeframes for implementing each audit recommendation. Please note that the regulation requires a management decision to be reached on all findings and recommendations within a maximum of 6 months from report issuance.

We are available to meet with you to discuss the specifics needed to reach management decision. We appreciate the courtesies and cooperation extended to us by members of your staff during the review.

/s/

RICHARD D. LONG
Assistant Inspector General
for Audit

EXECUTIVE SUMMARY

RISK MANAGEMENT AGENCY
MONITORING OF RMA'S IMPLEMENTATION OF MANUAL 14 REVIEWS/QUALITY CONTROL REVIEW SYSTEM

AUDIT REPORT NO. 05099-14-KC

RESULTS IN BRIEF

This report provides our assessment of the status of the Risk Management Agency's (RMA) system of ensuring quality performance by the providers of Federal crop insurance. Federal crop insurance is available solely through private insurance companies that market crop insurance policies and provide full service, including claims processing. The companies are reinsured by the Federal Government and are compensated for their services through underwriting gains and reimbursements for administrative costs. To evaluate overall program integrity and compliance, RMA uses a quality control (QC) system that consists largely of company internal reviews and periodic agency verifications.

This year, RMA continues an 8-year struggle to develop and implement a reliable QC review system capable of evaluating private sector delivery of Federal crop insurance. RMA's stated commitment to quality control has not answered basic policy questions, including what constitutes an error, the amount of improper payments made, and at what level program delivery should be assessed - whether at the national level or at the individual company level. The RMA Administrator needs to determine what he/she expects the agency's QC system to accomplish and what actions the agency needs to take to achieve this end. Until the objectives of the system are established and a long-term plan of action is implemented, RMA may continue to expect the Federal Crop Insurance Program to suffer from errors and abuses that largely go unreported by the insurance companies and to incur dollar losses that frequently go undetected.

Our current assessment raised the following concerns:

<u>Over the years, RMA has been unsuccessful at responding to recommendations</u> made by the Office of Inspector General and the General Accounting Office to establish a meaningful QC system.

Corrective actions have either not been implemented or have not had their intended effect on problems with the system. Error rates found during reviews by the Office of Inspector General have generally been higher than those found by RMA, and dollar losses disclosed by audits have been overlooked during insurance company internal reviews. A 1998 audit, for example, noted that one company's internal review verified the propriety of a $280,000 indemnity paid on a portion of a crop that the audit found to have been unreported and therefore uninsured.

RMA abandoned its standard error rate review. RMA needs to establish an acceptable error rate by insurance companies and hold companies that exceed that rate accountable. However, the review RMA initiated was not designed to measure errors at the company level and produced an error rate that was valid only for the year it was established. Moreover, RMA recognized that its error rate did not encompass a large number of RMA programs and was dependent on insurance company internal reviews, which were not always accurate. To date, RMA has not determined an accurate error rate and has no method of arriving at one. To this end, RMA cannot report on the amount of improper payments made by insurance companies.

Insurance company internal reviews implemented through the Manual 14 process were not reliable. In performing the reviews, the companies did not always adhere to the manual, and the manual itself is confusing and redundant. RMA's Compliance Division made recommendations to correct the problems, but the agency has yet to take corrective action.

The QC process does not have regulatory authority. The QC process is largely contained in Manual 14, and the contents of Manual 14 are negotiated with the insurance companies as part of negotiations over the Standard Reinsurance Agreement. Over the last year, RMA has attempted to revise the Manual 14 process; however, this revision effort has stalled due to a lack of consensus by all parties and inadequate direction and commitment from RMA. A QC process that was mandated by legislation and codified in Federal regulations would remove areas of dispute and give RMA greater control over the quality of program delivery.

RMA's error rate does not count all errors. Because the QC process has been subject to negotiation and not regulatory authority, insurance companies have skewed the definition of "error" to their advantage. Company internal reviews have measured an overall program error rate of less than 7 percent, whereas RMA has measured an error rate in the Actual Production History calculation (upon which future indemnities are based) of over 45 percent. Companies generally only count errors that result in dollar losses beyond established tolerances. Only one company informed us that it counts errors with no dollar losses.

An effective QC review system must be in place to ensure implementation of the Agricultural Risk Protection Act of 2000, whose purpose, among other things, is to improve compliance with the Federal Crop Insurance Program and strengthen its integrity. Under this act, RMA is required to notify insurance companies in writing of any error, omission, or failure on their part that may result in a debt owed to the Federal Government. Moreover, an accurate measurement of the effectiveness of the Federal Crop Insurance Program is critical under the requirements of the Government Performance and Results Act (GPRA). GPRA mandates that each agency define its goals and measure how effectively it attains them. As noted above, we have concluded that RMA's current performance measurements do not reflect the crop insurance program's actual effectiveness or a reliable estimate of improper payments made by insurance companies. RMA recognized this same condition in its reports to Congress under the GPRA. Although RMA had originally identified an accurate QC system as a performance goal, its current GPRA report acknowledges that the system's performance measurements are flawed: the standard error rate omits a large number of RMA programs and is dependent on insurance company internal reviews, which are not always accurate.

Because the crop insurance delivery system relies on the private insurance companies, these companies must be the first line of detection and prevention of program abuses and improper payments. Companies that deliver Federal crop insurance and also carry private property and casualty policies, generally practice some form of quality control. But we were not able to identify an industry wide standard, and we found no one model that would suit the crop insurance program. We therefore concluded that a QC system modeled on the one used by the Food and Nutrition Service (FNS) could provide satisfactory results. The FNS relies on States to measure the accuracy of their own performance and uses Federal sample testing to verify the State measurements. Most importantly, the system holds States accountable for their performance in the form of percentage shares of administrative costs; a State can increase its administrative funding by reducing its error rate below the FNS-established tolerance. A State that fails to improve a bad performance can have funding reduced through sanctions. All requirements of this QC system, including its incentives and liabilities, are contained in one comprehensive document in the Code of Federal Regulations.

We further noted that RMA did not identify the absence of a reliable QC review system as a material internal control weakness in its Federal Managers' Financial Integrity Act (FMFIA) report.

KEY RECOMMENDATIONS

The RMA Administrator should develop and propose a legislative proposal to mandate a QC review system to evaluate private sector delivery of the Federal Crop Insurance Program. Whether or not a legislative mandate is forthcoming, the Administrator needs to establish an overall goal, with supporting policy decisions and a plan of operation, for development and implementation of a QC review system. The developed system should set forth detailed procedures for the conduct of QC reviews and the reporting of program performance results, not subject to negotiation with the insurance companies. These procedures and all other requirements of the reviews, including incentives and liabilities, need to be given regulatory authority through publication in the Code of Federal Regulations.

Pending development and implementation of a reliable QC review system, RMA should annually report a material internal control weakness in its QC system, in accordance with the Federal Managers' Financial Integrity Act.

RMA RESPONSE

In its response, RMA agreed that improvements are needed in the current QC system, but that enacting legislation to mandate a review system would not solve the current problem and would in fact make the system more difficult to manage and change. RMA is in the process of awarding a contract to study its program delivery process which includes the QC system. The new QC system will include clear goals and objectives to evaluate performance and measure results. The estimated completion date for this effort is March 2003. In the mean time, RMA will consider alternative actions that can be taken to address the weaknesses cited in this report.

RMA does not believe that the report has provided sufficient evidence or justification showing the operation of this activity, is such, that it meets the criteria for reporting material weaknesses and system nonconformance defined under the FMFIA.

OIG POSITION

RMA must take aggressive action to define and describe its QC system. At a minimum, this quality assurance system must be codified in a regulatory process. Although RMA has attempted and abandoned various approaches intended to evaluate the integrity of the crop insurance program, it has not demonstrated a sense of urgency in integrating an effective QC system into its insurance program. Based on past problems and the critical importance of new management philosophy, policy direction, and operating style, RMA needs to create a QC system capable of accurately evaluating private sector delivery of the Federal Crop Insurance Program, providing effective stewardship of public resources and should, at a minimum, be codified in regulations and/or legislation to establish its authoritative basis.

RMA stated that it proposes to contract for a study to recommend a new QC system, which will include goals and objectives to evaluate performance and measure results, and is estimated for completion in March 2003. It is unclear as to whether the study or a reliable QC system will be completed by March 2003. In any event, RMA needs to take aggressive action and put in place interim actions necessary to strengthen its present QC system. In order for us to consider RMA's management decisions for Recommendations Nos. 1, 2, and 3, it will need to provide additional details, clarifications, and milestones on its contemplated actions to implement a new effective QC environment, including those actions it intends to put in place in the interim.

RMA reported on October 1, 2001, to the Acting Chief Financial Officer that it had no new material weaknesses or system non-conformances for the period ended September 30, 2001. We disagree because RMA's QC program does not provide any reliable measures of the extent of erroneous payments within the Federal Crop Insurance Program. We believe the present QC system meets the criteria for reporting as a material weakness because it does not provide reasonable assurance over the propriety of Federal Crop Insurance Program payments and expenditures. Despite many years of effort, RMA has failed to implement such a system. Therefore, RMA needs to report in its future FMFIA reports that the absence of a reliable QC review system is a material weakness until an effective QC is established and successfully implemented.

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INTRODUCTION

BACKGROUND

The Federal Agriculture Improvement and Reform Act of 1996 created the Risk Management Agency (RMA). Under the act, RMA was established as an independent agency to provide supervision to the Federal Crop Insurance Corporation (FCIC) and oversight of all crop insurance programs. FCIC is a wholly owned Government corporation that issues insurance regulations and manages crop insurance funds. The crop insurance program is a joint effort by the private sector (insurance companies) and RMA to provide crop insurance to qualified producers.

RMA delivers crop insurance programs under Standard Reinsurance Agreements (SRA) with insurance companies. Insurance companies are private insurance companies that provide marketing, underwriting, loss adjustment, and other servicing of crop insurance policies. The SRA establishes the terms and conditions under which RMA will provide premium subsidy, expense reimbursement and reinsurance to the insurance company.

While RMA works closely with the insurance companies to implement the crop insurance program, RMA itself is responsible for reviewing and evaluating the program. Federal policy[1] states that agencies shall provide reasonable assurance that "both existing and new program and administrative activities are effectively and efficiently managed to achieve the goals of the agency." To implement this policy, RMA has enlisted the help of the insurance companies. Following procedures set forth by RMA's Insurance Services, the insurance companies review the quality of their performance in delivering the Crop Insurance Program. They evaluate their own compliance with program requirements and correct activities that are not in compliance. The types of reviews include proficiency evaluations of sales agents and loss adjustors, compliance crop insurance contract reviews, underwriting reviews, and claim reviews. These reviews and their procedures are incorporated into Manual 14 and are referred to as quality control (QC) reviews.

After the insurance companies perform their QC reviews, RMA's Compliance Staff has the responsibility to review and validate them. As

[1] Office of Management and Budget Circular A-123 (revised), "Management Accountability and Control," dated June 21, 1995.

part of this validation process, RMA makes recommendations to correct noted deficiencies. The Compliance Staff performed its first review in 1999 for the 1998 crop year company internal reviews.

An adjunct to the insurance company internal reviews is the development of a standard error rate against which improvements in performance can be measured. RMA began collecting data for such an error rate in 1998. This initiative, known as the Baseline Error Rate Review, or BERR, was scheduled to continue through 3 years and arrive at an error rate that would become an integral part of the QC system.

Subtitle B of “The Agriculture Risk Protection Act of 2000” directs the Secretary of Agriculture to improve the compliance and integrity of the crop insurance program. The Secretary is required to develop and implement a coordinated plan for FCIC and the Farm Service Agency (FSA) to reconcile, at least annually, all relevant information received by FCIC or FSA from a producer who obtains crop insurance coverage, beginning with the 2001 crop year. Further, in an effort to identify and eliminate fraud, waste and abuse the Secretary is directed to develop and implement a plan for FSA to assist FCIC and insurance providers in auditing a statistically appropriate number of claims made under any policy or plan of insurance.

The Agricultural Risk Protection Act does not mandate the elements of RMA’s QC system, but it does expand the efforts that RMA and the insurance companies currently make under that system. Manual 14 reviews, which include randomly selected samples, are key to the information RMA now receives in its efforts to ensure the integrity of the crop insurance program. With the assistance of FSA, farm program data will also play an important part in eliminating fraud, waste, and abuse. Nonetheless, the activities of FSA will not affect the responsibilities of insurance companies to conduct any audits of claims or other program reviews required by RMA. The act’s mandate for identification of noncompliance by producers or insurance companies and of fraud, waste, and abuse will call upon RMA and the insurance companies to commit greater resources than currently used to fulfill the oversight function. Consequently, the risk protection act addresses only a part of the function that RMA’s QC system fulfills.

OBJECTIVE

The objectives of the audit were to determine whether RMA’s implementation of a QC review system was adequate and to evaluate RMA’s management controls designed to ensure that insurance companies accurately perform and report the results of their internal QC reviews.

SCOPE AND METHODOLOGY

To accomplish the audit objectives, we interviewed RMA Headquarters officials regarding their QC review philosophy and reviewed reports and memoranda from 1989 to present issued by RMA, the Office of Inspector General (OIG), and the General Accounting Office (GAO) concerning RMA's efforts to implement a QC review system (refer to References). We also monitored the meetings and teleconferences conducted by the Manual 14 working group from March 27, 2000 to present, and reviewed 16 Compliance Crop Insurance Contract Reviews completed by two insurance companies and reviewed by staff in one RMA Compliance Office. The audit was performed in accordance with Government Auditing Standards.

FINDINGS AND RECOMMENDATIONS

CHAPTER 1	USDA LACKS A SYSTEM TO EFFECTIVELY EVALUATE THE INTEGRITY AND DELIVERY OF THE FEDERAL CROP INSURANCE PROGRAM

FINDING NO. 1

RMA ADMINISTRATOR NEEDS TO MAKE BASIC DETERMINATIONS

RMA has failed to achieve measurable progress in developing a QC review system capable of evaluating private sector delivery of the Federal Crop Insurance Program. We concluded that the failure is largely a result of RMA's level of commitment: RMA has not determined what it expects the agency's QC system to accomplish and what actions the agency needs to take to achieve this end. As a result, the Federal Crop Insurance Program continues to suffer from errors and abuses that are largely unreported by the insurance companies, and it continues to incur dollar losses from improper payments that frequently go undetected. RMA's QC system, with its reliance on insurance company internal reviews, must serve as RMA's first line of defense against erosion of integrity in the crop insurance program.

Agency efforts to develop a QC review system have been rendered ineffective by the absence of policy establishing what the system should measure and what standards of accountability should apply. RMA has not determined whether it should measure each insurance company's performance, has not established an acceptable standard error rate to hold companies accountable for excessive errors, and has not defined an error so as to make error rate or improper payment measurements meaningful. RMA's definition of what constitutes an error, largely formulated by the insurance companies, generally excludes mistakes that have little or no monetary effect and therefore results in lower error rates than actually occur. RMA has recognized defects in its error rate and has discontinued its use but has not found a replacement method for measuring the rates or improper payments. As a result, the Department is no closer to having a fully developed and reliable QC review system in place to evaluate delivery of the Federal Crop Insurance Program than it was 8 years ago.

An effective QC review system must be in place to ensure implementation in 2001 of the Agricultural Risk Protection Act of 2000. This legislation requires RMA to maintain the integrity of the Federal Crop Insurance Program by, among other things, notifying insurance companies of program errors; identifying and eliminating fraud, waste, and abuse; detecting disparate performances among sales agents and loss adjusters; and imposing sanctions on producers, sales agents, or loss adjusters who willfully fail to comply with program requirements.

An accurate measurement of the efficiency of the Federal Crop Insurance Program is also critical under the requirements of the Government Performance and Results Act (GPRA). GPRA mandates that each agency define its goals and measure how effectively it attains them. We concluded that RMA's current measurements do not reflect the crop insurance program's actual efficiency. RMA recognized this same condition in its reports to Congress under the GPRA. Although RMA had originally identified an accurate QC system as a performance goal, its current GPRA report acknowledges that the system's measurements are flawed. Specifically, the report announces that RMA is abandoning the standard error rate it had established, noting that the rate omits a large number of RMA programs and is dependent on insurance company internal reviews, which are not always accurate.

In April 2000, OIG issued a memorandum to the Honorable Senator Richard D. Lugar, Chairman, Committee on Agriculture, Nutrition and Forestry, in response to congressional concerns about media reports of abuse of the Federal Crop Insurance Program. In our letter, we stressed that with RMA's limited resources, the agency must rely on the insurance companies to effectively monitor the crop insurance program through a system of internal reviews. Because of this reliance, insurance companies are the first line of detection and prevention of program errors and abuse. We also advised the Senator that many of the program problems cited by OIG and highlighted in the press could have been corrected by an effective QC review system. Although OIG and GAO have recommended improvements in RMA's QC system over the last 8 years, corrective actions were not effectively implemented.

The Monitoring Standard for Internal Controls provides that monitoring of internal control should include policies and procedures for ensuring that findings of audits and other reviews are promptly resolved. Managers are to (1) promptly evaluate findings from audits and other reviews including those showing deficiencies and recommendations reported by auditors and others who evaluate agencies' operations, (2) determine proper actions in response to findings and recommendations from audits and reviews, and (3) complete, within established time frames, all actions that correct or otherwise resolve the matters brought to management's attention. The resolution process begins when audit or other review results are reported to management and is completed only after action has been taken that (1) corrects identified deficiencies, (2) produces improvements or, (3) demonstrates the findings and recommendations do not warrant management action.[2]

In addition, The President's Management Agenda, Fiscal Year 2002, includes a government wide initiative for improved financial performance. Under this initiative, the administration will establish a baseline of the extent of erroneous payments and require agencies to include, in their fiscal year 2003 budget submissions, information on erroneous payment rates, including actual and target rates, where available for benefit and assistance programs over $2 billion. Using this information, the Office of Management and Budget (OMB) will work with agencies to establish goals to reduce erroneous payments for each program. According to OMB, public reporting of progress in meeting goals for minimizing erroneous payments enhances accountability and it expects agencies to do so in their agency performance reports under the GPRA, annual financial reports, or other program reports. Stewardship responsibility over public funds requires that RMA have appropriate policies and procedures to ensure the integrity of Federal program payments and implement its existing responsibilities to minimize erroneous payments.

Corrective Actions Were Not Effectively Implemented

Over the last decade, error rates in the crop insurance program have, by OIG measurements, remained relatively high, in some cases as high as 50 percent of our samples. RMA's efforts to control the quality of program delivery have been unfocused and ineffective, and its own error rate measurements have been inaccurate. As a result, RMA managers have themselves discarded some of these measurements because of their limited use as management tools.

OIG's most recent concerns with RMA's QC system began in 1993, when OIG completed an audit[3] of 1991 claims. The audit discussed issues that were to become central during that decade to the development of a meaningful QC system. The audit recommended that RMA[4] (1) develop a

[2] General Accounting Office Standards for Internal Controls in the Federal Government, GAO/AIMD-00-21.3.1, dated November 1999.
[3] Audit Report No. 05600-4-Te, Crop Year 1991 Claims, issued September 30, 1993.
[4] Prior to 1996, OIG audits of the Federal Crop Insurance Program were directed to RMA's predecessor, the Federal Crop Insurance Corporation.

standardized definition for what constitutes an “error,” (2) annually perform reviews of statistically selected sample claims to determine the error rate by insurance company, (3) define what constitutes an unacceptable error rate and track each company’s performance against this standard, and (4) determine what actions to take to hold a company accountable for a poor performance.

In its response to the audit, RMA agreed to the recommended actions, but its efforts to institute them were unsuccessful. The agency announced it would establish a standard error rate beginning with crop year 1994, but it did not begin to collect data for such an error rate until 1998; it chose to further study the definition of “error” rather than to define it; it did not establish a performance standard and, consequently, was unable to measure each company’s performance against such a standard; and the list of sanctions it planned to publish in its QC manual did not materialize.

Since the mid 1990’s, OIG has revisited RMA’s QC system to determine what progress had been made in reforming the system. We have issued a number of reports that have pointed out potentially serious flaws in RMA’s overall QC methodology. The content of those reports portrays a history of the ineffectiveness of RMA’s QC system.

- An OIG audit[5] completed in early 1998 concluded that RMA’s control over the quality of the crop insurance program had made little progress since 1993. Insurance company internal reviews of large claims ($100,000 or over) were not effective in identifying and correcting program violations. During the audit, RMA issued new guidelines that (1) required companies to conduct field reviews for all large claims, and (2) required all such claims be subject to independent verification by an adjuster who was not involved in evaluating the original claim.

- We returned to RMA in the summer of 1998 and reported on the effectiveness of its QC activities. Our audit[6] showed that company internal reviews remained ineffective. Internal reviews at two large insurance companies did not produce meaningful results for improving program delivery and maintaining program integrity. Although the internal reviews generally complied with RMA guidelines, these guidelines were so vague that the effect of the reviews was minimal. RMA also did not effectively monitor the progress of QC activities and conclusions to ensure the companies produced meaningful results.

[5] Audit Report No. 05601-3-Te, Federal Crop Insurance Claims, issued February 18, 1998.
[6] Audit Report No. 05099-2-KC, Quality Control for Crop Insurance Determinations, issued July 14, 1998.

RMA officials generally concurred with our findings, and agreed to (1) require insurance companies' internal reviews to meet minimum guidelines, and (2) require companies to develop statistically valid error rates which would be used to establish QC error rates for each insurance company and all insurance companies as a whole. RMA anticipated establishment of these error rates by November 1999.

- By the beginning of 1999, we completed another audit[7] of RMA's monitoring of insurance companies' performance. We found that although RMA's Risk Compliance Division had made a "considerable effort" to monitor insurance companies' operations, RMA was still struggling to determine what it could use as a valid error rate and what minimum guidelines it could hold companies to. We concluded that RMA needed to make more effective use of the results of the agency's own compliance reviews. RMA also needed to proactively identify potential compliance problems before they resulted in overpayments or appeals.

  OIG recommended that the Risk Compliance Division institute a system to analyze the results of its reviews in order to determine trends and vulnerable areas and establish written policies for performing periodic reviews of "key" RMA activities (i.e., field offices and regional service centers). RMA agreed to address these OIG recommendations.

- A concurrent audit in the spring of 1999 resulted in a special report to the Secretary on Federal crop insurance reform.[8] In this report, we noted that insurance company internal reviews were superficial and did not provide independent verification of proper claims activities. We emphasized that numerous previous audits had found improperly paid or incorrect indemnities, while the insurance companies' internal reviews found few problems. The company internal reviews consisted largely of a series of questions requiring only a "yes" or "no" answer. Although the reviewer was supposed to rework the loss as if it were being done for the first time, OIG found no evidence the reworking had been performed.

  The April 1999 report also noted a recurring problem within the QC system: company internal reviews were inadequate to detect and prevent conflicts of interest among sales agents and loss adjustors.

[7] Audit Report No. 05005-1-Ch, Controls Over Monitoring of Private Insurance Companies," issued January 22, 1999.
[8] Audit Report No. 05801-2-At, Report to the Secretary on Federal Crop Insurance Reform, issued on April 19, 1999.

> OIG recommended that RMA develop and implement a system of ongoing reviews of insurance companies' QC activities to assess their effectiveness in identifying and correcting program weaknesses. We also recommended that RMA consider developing a system for rating companies' delivery and administration of the crop insurance program. As part of the system, RMA could provide monetary rewards to companies or sanction them, based on their performance compared to an accepted standard of satisfactory performance.

To date, RMA has no system for rating companies or for rewarding or sanctioning them based on the results of the QC reviews. Although it increased its number of ongoing reviews of the companies, our current work has shown that these reviews have not been adequate to assess the effectiveness of company efforts to identify and correct program errors.

In September 1999, GAO issued a report, "Crop Insurance: USDA Needs a Better Estimate of Improper Payments to Strengthen Controls Over Claims", which reiterated many of the concerns we had raised in our previous audits. GAO found that there were no precise estimates of the extent to which crop insurance claims were paid in error. While RMA estimated that about 5 percent of claims were paid in error in 1997, the agency's methodology for estimating errors relied on an inadequate sample size and did not include the results of timely, onsite reviews to detect errors resulting from fraud. Although information on payment errors for other types of property and casualty insurance is limited, insurance industry studies report higher rates of fraud-related payment errors than RMA does.

In its report, GAO recommended that RMA evaluate the costs of alternative methods for developing more accurate estimates of error rates and implement an alternative that would improve the estimate at a reasonable cost to the Federal Government. Alternatives that could be considered include (1) having RMA sample and analyze a sufficient number of claims to make an estimate, and (2) using the claims sampling done by the insurance companies during their internal reviews to make the estimate.

GAO noted that the Agriculture Department generally agreed with the conclusions and recommendations in the report. However, to date, RMA has not developed a more accurate estimate of error rates and remains uncertain, pending the issuance of agency policy, whether one error rate should be established for the program on the whole or whether separate error rates should be established for each insurance company.

Weaknesses in the QC System Have Resulted in Losses and Overpayments

Errors by insurance companies have, over the years, resulted in large dollar losses to the program. Our audits determined that a reliable QC system could have identified these errors and prevented some of the losses. The quality of insurance company internal reviews, and by extension oversight of those reviews by RMA, was at the core of the problem.

- Our audit[9] of 1988 claims found that over 67,000 claims were in error and that claimants had been overpaid $90 million. Errors occurred in production to count, units, yields, shares, acreages, and premium adjustment factors. For one type of error alone—actual production history (APH) yields—the error rate exceeded 50 percent. We recommended that RMA provide increased coverage to the categories where we found the largest number of overpaid claims.

- In reviewing RMA's compliance review program for 1988 and 1989,[10] we found RMA compliance reviews of insurance companies for these 2 years had determined net overpayments of only $284,000 (about one-hundredth of a percent of total indemnity payments), even though our random reviews of loss adjustments found that over 10 percent of indemnities were overpaid. Contributing to RMA's small dollar error detection was a lack of documentation from compliance reviewers.

- During our review of the 1996 crop insurance program,[11] we found errors in 30 of the 75 policies reviewed. We questioned indemnity payments of over $133,000 as a result of these policies. In three cases, indemnities were paid for prevented planting although the insured land had been used for crawfish production. In another case, indemnities were paid on doubled-cropped land that had no prior history of double cropping. For two of the claims, loss adjustors worked claims for claimants with whom they had a personal or business relationship. None of the company internal reviews detected or took exception to these conflicts of interest.

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[9] Audit Report No. 05600-1-Te, Crop Year 1988 Insurance Contracts With Claims, issued September 29, 1989.

[10] Audit Report No. 05099-51-Te, Compliance Review Program 1988-1989 Review Schedule, issued March 29, 1991.

[11] Audit Report No. 05601-5-Te, Prevented Plantings of 1996 Insured Crops, issued March 15, 1999.

- Our review of claims on fresh market tomato losses in 1996[12] found significant problems in all seven policies reviewed. Indemnities totaled about $4 million. There was no evidence that any of the claims had been reworked by the company during its internal reviews, and we recommended that RMA become more directly involved in claim reviews when claims result in large indemnities. RMA agreed to review claims in excess of $250,000 prior to payment of the indemnity, but such a proposed change has yet to appear in the Federal Register or in an RMA manager's directive.

- During the same year, we found that insurance company internal reviews were also ineffective at detecting errors in APH yields. RMA projected that in 1995 producers overpaid premiums by $15 million and the Government overpaid insurance company administrative expenses by $4.6 million. Our audit[13] noted that RMA had not tried to analyze company internal reviews for trends and abuses until 1995, at which time it discovered it could not perform the analysis because the companies did not always report the results of their internal reviews.

- During crop years 1995 and 1996, RMA relied on insurance company internal reviews to ensure the propriety of policies and claims for nursery crops, but we found those reviews were deficient. Our audit,[14] disclosed that one company paid almost $287,000 in indemnities on crop inventory that was not insured. We recommended once again that RMA itself perform verification reviews when producers file claims that result in large indemnity payments.

- Large dollar claims again showed significant errors when we completed an audit[15] of 17 such claims in 1998. We questioned a net overpayment of $1.2 million and recommended that RMA ensure greater indepth coverage of claims during company internal reviews. As a result of this audit, RMA issued new guidelines requiring field visits during company reviews of all claims over $100,000.

Current OIG reviews of RMA's QC system have not shown any significant improvement in that system. Although RMA has updated its QC review manual and initiated studies for a standard error rate, RMA's current

[12] Audit Report No. 05099-1-At, Crop Insurance on Fresh Market Tomatoes, Crop Year 1996, issued September 30, 1997.
[13] Audit Report No. 05099-1-Te, Reinsured Companies' Actual Production History Internal reviews, issued September 30, 1997.
[14] Audit Report No. 05099-2-At, Nursery Crop Insurance Program, Crop Years 1995 Through 1996, issued December 16, 1998.
[15] Audit Report No. 05601-3-Te, Federal Crop Insurance Claims, issued February 18, 1998.

methodology for establishing meaningful performance measures remains flawed and application of that methodology will not result in the accurate measurement of insurance company performance. Deficiencies in insurance company internal reviews continue, and no clear system of incentives and sanctions has emerged to aid RMA's management of the quality of program delivery.

RMA's Current Methodology and Application Are Flawed

RMA's Revised Fiscal Year 2000 and 2001 Annual Performance Plan,[16] required under the Government Performance and Results Act, states that RMA is committed to reduce program vulnerabilities through a multitude of internal and external review processes including a "baseline" error rate review (BERR), insurance company internal reviews, and RMA QC followup reviews. Procedures for the insurance company internal reviews are set forth in RMA's Manual 14 and are referred to as Manual 14 reviews. We concluded that neither RMA's BERR nor the Manual 14 reviews performed by insurance companies have produced a rate of occurring error that could be used to evaluate program delivery, free from qualification.

a. Establishment of a Baseline Error Rate

BERR was developed as a 3-year initiative to be completed in 2000. BERR results were derived from tests conducted by RMA on a statistically selected sample of policies to determine actual error rates given a specified population, sample size, and confidence level. As such, the baseline error rate was based on historical percentages of occurring errors.

The initial testing of BERR sample policies and analysis of review results was completed in 1998, supporting an average error rate of 4.83 percent (+/- 4.06 percent). However, this did not provide RMA with a standard of measure for determining acceptable or unacceptable levels of performance relative to private sector delivery of the Federal Crop Insurance Program. As designed, the BERR establishes an error rate that can only be applied to the overall program, not to any individual insurance company performance, and is valid only for the year during which the tests are made. The BERR

[16] RMA issued its Revised Fiscal Year 2001 and 2002 Annual Performance Plan during our current review. According to this new plan, RMA will no longer use the Baseline Error Rate Review (BERR) figures because those figures did not encompass a large number of programs that were developed and delivered and because the BERR measurements are dependent on the Manual-14 quality control reporting requirement.

was also designed for “attribute” sampling, assigning each error the same value, regardless of the dollar effect the error may have. A low error rate composed of errors that cost the program millions of dollars gives a false impression.

Our analysis of the BERR also found that RMA’s methodology was flawed: RMA did not question the insurance companies’ reporting of Actual Production History (APH) data used in the BERR testing, even though RMA’s own review of the APH yields in 1996 found an error rate of 48 percent. Such a high error rate in the APH yields casts serious doubt on the 1998 BERR of only 4.83 percent. In addition, while BERR was developed as a 3-year initiative, testing and analysis has only been completed for the first year, 1998. Tests completed for 1999 were never analyzed, and according to RMA, the BERR testing figures will no longer be used.

We concluded, an initiative such as the BERR cannot establish a standard error rate because it was only intended to measure an actual historical error rate. A standard error rate should represent the percentage of error the agency considers the standard of measure for evaluating acceptable program performance and could well be based on the best performing insurance company; it should not be based on or influenced by historical percentages of occurring errors, which are not necessarily desirable. A standard error rate can be subjectively determined based on sound reasoning and logic. Once established, it should remain relatively constant, unlike historical percentages, which will change annually in direct relation to overall performance.

In general, the insurance industry has been reluctant to support establishing an error rate. Company representatives we spoke to saw an error rate as too arbitrary and were afraid such a calculation would allow cases of producer fraud to count against the company. In general, insurance companies avoided the term “errors” and spoke only of “adjustments” or “misclassifications.” However, we also found that some companies did compare their individual performances against available loss ratios or loss experiences. In these cases, the companies sought to identify unprofitable sectors of their business with the aim of discontinuing any particular segment or agency within that business. Consequently, even without a formal “error rate,” insurance companies had a mechanism for monitoring underwriting practices that were not improved by “adjustments,” and for maintaining accountability from sales agents and loss adjustors.

b. Manual 14 Reviews

OIG recommended that RMA develop and implement a system for ongoing reviews of insurance companies' QC activities to assess their effectiveness in identifying and correcting program weaknesses. RMA responded by developing Manual 14. Included in Manual 14 are the compliance crop insurance contract reviews, which like the BERR, involve multiple-year reviews of statistically selected samples of policies to assess occurring rates of errors in delivery of the Federal Crop Insurance Program. We concluded that RMA had no plan of action for implementing the Manual 14 reviews, including the compliance crop insurance contract reviews; the procedures for these reviews do not produce a consistent approach toward accurately measuring the quality of program performance, either at the company level or at the national level. In our opinion, detailed criteria and instruction are needed to ensure consistency in the conduct of the review process, as well as the analysis and reporting of review results. RMA efforts to monitor and evaluate insurance company reviews in accordance with Manual 14 support the same conclusion.

In 1999, as part of their Manual 14 reviews, 16 insurance companies performed compliance crop insurance contract reviews of approximately 1,700 statistically selected policies with indemnities for the 1998 crop year. Of these 1,700 policies, 179 were selected for followup reviews by the six RMA regional compliance offices. (The RMA regional compliance offices reviewed a total of 545 quality control reviews performed by the insurance companies as required by Manual 14.) RMA performed independent verification of entity and producer shares, but generally did not validate other program data affecting premium and indemnity. Based on the results of the Manual 14 reviews completed by the 16 insurance companies, RMA reported an estimated error rate of 6.58 percent (+/-2.74 percent) for delivery of the crop insurance program. However, RMA determined that this projected error rate was unreliable for several reasons: review conclusions reached by the insurance companies were not always supported by documentation, field reviews were not always documented, there was no evidence that some reviews were completed, and some reviews did not meet Manual 14 criteria. RMA reviews of 28 sample policies disclosed discrepancies in policy, share, actual production history, and monetary amount not disclosed by private insurance company reviews.

Our review of 16 compliance crop insurance contract reviews, performed by two insurance companies, confirmed that review documentation was insufficient to support the performance and content of the required reviews.

We concluded that the Manual 14 reviews, as practiced by the insurance companies, are ineffective in part because Manual 14 is unfocused and inconsistent. It calls for a large number of reviews, many of which are redundant, and it does not establish clear procedures for the reviews or distinguish the purpose of each. For example, there is little distinction between a compliance contract review ("to determine whether all FCIC procedures were followed by the sales agents and loss adjustors") and either a large claims review or an agent review. Again, in describing both underwriting reviews and claims reviews, RMA notes that the "requirements for [these] reviews…may be satisfied through other reviews required under this section." However, the "other reviews" are not identified. Also, references to tolerances and determination guidelines are vague and depend on the type of review and program, requiring the reviewer to consult the crop insurance handbook and the loss adjustment manual. In the absence of specific review steps, insurance companies have relied on checklists, which do not encourage explanatory or consistent conclusions.

In its correspondence, RMA has manifested an awareness of problems with the insurance company checklists. It also acknowledges that Manual 14 contains duplication and needs to be revised. Our monitoring of joint RMA-industry working groups disclosed that insurance company representatives were themselves concerned with the time and resources they needed to perform the various reviews required by the manual. We concluded that by eliminating redundancies in Manual 14, RMA would both increase the efficiency of the review process and improve private sector attitude towards quality control of the crop insurance program by reducing the burden of its requirements.

Contributing to the unreliability of the 6.58 percent error rate calculated by RMA are the inconsistencies practiced by the insurance companies in their measuring and reporting of errors. For the BERR, RMA had defined "error" as an exception that may or may not have a monetary effect on the claim, and it categorized errors as unintentional, intentional, or a result of program vulnerabilities. Manual 14, however, does not define or address how errors are to be identified, classified, or reported.

On March 27, 2000, RMA assembled a Manual 14 working group, composed primarily of representatives from the private insurance companies, to propose revisions to the Manual 14 guidelines. Members of a subgroup assigned responsibility for developing definitions for terms struggled to reach final concurrence on an accepted definition for identifying, classifying, and reporting errors. Representatives of the private sector generally supported the definition of "error" as a discrepancy resulting in a net monetary impact (premium offset from indemnity) exceeding an established tolerance. For example, if a producer underpays a premium and is overpaid an indemnity but the difference between underpayment and overpayment is less than $250, there is no measurable or reportable error because the payment mistakes did not exceed the $250 tolerance.

To obtain an accurate picture of program efficiency and integrity, RMA should consider any discrepancy that has a potential monetary impact as an error for QC purposes. This includes any discrepancy in coverage level, price election, share, yield, acreage, or production-to-count that can be linked to a verifiable cause. Such a discrepancy may have a significant dollar impact in future years, especially in the establishment of an APH, upon which all indemnities are based. For example, a 1999 prune indemnity on a 40-acre orchard with the minimum insurance coverage could have been overpaid by over $2,500 if the orchard's 1998 APH was inflated by only one-tenth of a ton per acre. If the producer did not claim a loss in 1998, insurance reviewers looking for monetary impact that year would have no reason to verify the orchard's revised APH. Procedures for netting monetary impacts on premiums and indemnities and the application of a monetary tolerance should be limited to the debt collection process, and should have no bearing on the identification, classification, and reporting of errors under a QC review system.

According to RMA, over $100,000 was expended toward establishing a baseline error rate, an effort that was unproductive and that was ultimately abandoned. As of the date of this report, RMA's reported costs of the Manual 14 compliance reviews, whose data has been generally too unreliable to hold insurance companies accountable, stands at almost $300,000. This does not include the additional cost to insurance companies to perform QC reviews. We concluded that expenditures in these areas produced little of value towards ensuring the integrity of the crop insurance program.

RMA Management Needs to Establish Intended Goals

Although BERR and the Manual 14 reviews resulted from RMA's explicit commitment to evaluate the integrity of the crop insurance program, that commitment has not taken the form of a clear policy statement or a long-term plan of action. RMA's management at the highest level needs to establish a policy regarding how private sector delivery of the Federal Crop Insurance Program will be evaluated, whether on the basis of the overall program or on the basis of each individual insurance company. Once RMA has established its QC goals, it needs to develop a long-term plan of action upon which to base its Manual 14 reviews.

When RMA originally selected its samples of policies and indemnities for compliance crop insurance contract reviews, it based sample selection on an overall program basis. Consequently, the reviews have been geared toward analyzing and projecting an overall rate of error for the program but not for individual companies. RMA has not subsequently broadened its analyses beyond the original program level or determined specifically what its goal for the QC program should be.

Some RMA officials have expressed a desire to evaluate performance on an individual insurance company basis. Such an evaluation would likely be necessary in order to implement the Agricultural Risk Protection Act of 2000. That act requires RMA to identify any sales agent or loss adjuster whose activities result in sales or claims greater than 150 percent of the mean sales or claims in the same area. To identify these individuals, RMA needs to measure performance in much smaller units than program-wide. However, such a decision needs to be made by agency management at the highest level. The basis on which program delivery will be evaluated directly impacts the number of required reviews and resources associated with the conduct of these reviews, as integral design elements of a QC review system.

Policy decisions related to the level at which program delivery will be evaluated are needed to ensure that system design and implementation are consistent with the Congress and Department goals and expectations. A corresponding long-term plan of action would eliminate much of the confusion and redundancy of Manual 14 reviews. Lack of a clearly defined plan of action has resulted in expenditures of departmental and private sector resources with virtually no corresponding progress towards timely development and implementation of a QC review system. The absence of basic policy decisions related to system design and implementation brings into question RMA's stated commitment to develop and implement a reliable QC review system.

RMA needs to establish a policy that sets forth what it hopes to accomplish through the development and implementation of a QC review system. The agency then needs to work with qualified technical and program specialists to develop a detailed plan of action, with a corresponding timeline, that will enable the Department to realize the established goal.

RMA Needs To Redefine its QC Partnership Role With the Insurance Industry

In terms of Government operations, RMA currently exercises little effective control over its own quality control system. None of the QC activities practiced by the insurance companies and RMA have a statutory or regulatory basis that establishes and validates RMA's actions. We concluded that most RMA quality control decisions and procedures reflect an imbalance of influence from the insurance companies, whose performance RMA should be trying to objectively evaluate.

RMA's QC system, as carried out through the BERR and the Manual 14 reviews, is an accretion of methods and procedures that existed under FCIC and became gradually formalized through RMA handbooks and directives. At no time was the system incorporated into a law or codified in regulations; consequently, it does not have the authoritative basis on which Government programs normally rest. A high-ranking RMA official has stated that a regulatory formulation of the QC system would provide greater agency control over program evaluation and reduce the level of influence that the private sector has felt invited to exert over the review process.

RMA's efforts to update QC review requirements included in Manual 14 have focused heavily on input from the private insurance companies. While private sector participation in the process may be viewed as integral to successful implementation of a QC review system, the result will be a system that reflects private sector interests rather than those of the Congress and Department. Documentation from Manual 14 reviews suggests that some companies view Manual 14 as simply a checklist of things to review rather than a system of checks and balances designed to ensure irregularities are identified and corrected.

Discussions with RMA personnel disclosed that the current version of Manual 14, approved in 1997, was negotiated with the private insurance companies in conjunction with negotiation of the SRA. In our opinion, the general nature of the guidance included in Manual 14, with its vague definitions and references, is directly related to the problems encountered with the insurance companies' conduct of Manual 14 reviews.

Current efforts to update Manual 14 have been assigned to a Manual 14 working group, with a majority of the group members again representing the private sector. The Manual 14 working group, while generally successful in identifying areas for needed revisions, has struggled to reach concurrence on recommended solutions to noted problems. The struggles have resulted in piecemeal changes and no coherent system. Manual 14 has come to represent this patchwork approach to solving program problems, while the problem-solving process is itself slowed by RMA's emphasis on insurance company contributions.

During an interview, one RMA official stated that administrative functions like Manual 14 reviews should be placed in regulations implemented through the normal process. This would allow for a commenting period but would not involve negotiations. The SRA itself would only include financial agreements - i.e., risk sharing, etc. - between RMA and the companies

We concluded that RMA needs to reevaluate its QC partnership with the insurance companies. Clearly some level of industry involvement in the QC system is necessary; given the limited resources RMA is faced with. RMA must rely on the insurance companies to monitor the program and themselves. In our contacts with some of these companies, we determined that while they generally support RMA's QC process, they believe they devote a substantial amount of their resources to completing the requirements of Manual 14 - more than they devote to their non-Federal business. When performing QC reviews of their property and casualty policies, some companies compare data from their books of business with that of outside vendors, share their findings with the sales agent or loss adjuster whose work showed deficiencies, and plan corrective actions. In short, the QC reviews of non-Federal business were more structured and focused than the Manual 14 reviews; however, no industry wide standard for QC reviews emerged, and no one company model appeared suitable to the crop insurance program. Consequently, we concluded that RMA should take the initiative to reform its partnership with the insurance industry. It should create a QC system that relies on industry to monitor the program but that uses RMA resources to independently verify industry's efforts, as called for by the Agricultural Risk Protection Act. Under such a system, insurance companies would perform the QC reviews according to the Federal standard, and RMA would validate these reviews on a selective basis.

Such a system is currently used by the Food and Nutrition Service and is set forth in detail in the Code of Federal Regulations (CFR) (Part 275). The regulations establish the requirements for sample selection, the methods and materials of review, case completion standards, and an error rate against which performance can be measured. States are required to measure themselves, but Federal sample testing is used to verify the State measurements. Most importantly, the system holds States accountable for their performance in the form of percentage shares of administrative costs. States that exceed the tolerance may receive only 50 percent of their costs; States that outperform the tolerance can receive additional funds; and States that do not attempt to improve a bad performance may have funds withheld. All requirements of this QC system, including its incentives and liabilities, are contained in one comprehensive document in the CFR.

RMA should work with Congress and within the Department to develop a legislative proposal to mandate a QC review system that reflects the goals and interests of both Congress and the Department in assessing private sector delivery, as well as reporting erroneous payment information, for the Federal Crop Insurance Program. Whether or not such a mandate is forthcoming, RMA should define and describe its QC system in regulations, where the system would gain an authoritative basis that was not subject to influence from private industry. Requirements for the QC review system would be presented to the insurance companies for their consideration in determining whether they desired to participate in the Federal Crop Insurance Program, but these requirements would not be subject to negotiation.

RECOMMENDATION NO. 1

The RMA Administrator should develop and propose a legislative initiative that would mandate a QC review system that reflects the goals and interests of the Department in assessing private sector delivery of the Federal Crop Insurance Program. Whether or not such a mandate is forthcoming, RMA should define and describe its QC system in regulations, where the system would gain an authoritative basis.

RMA Response

"RMA agrees that improvements are needed in the current QC system. However, enacting legislation to mandate a review system would not solve the current problem and would in fact make the system more difficult to manage and change. Also, the legislative approval process is lengthy and time consuming. The current system needs to be revised to include the changes made by the Agricultural Risk Protection Act of 2000. We are in the process of awarding a contract to study our program delivery process and the underlying agreement. We expect the results to be available later in the year. In the meantime, we will consider alternative actions that can be taken to address the weaknesses cited in the report."

OIG Position

We are concerned that the focus of RMA's proposed study is the program delivery system as a whole and this study may not devote sufficient emphasis to establishing an economical and effective quality assurance system. Also, RMA's approach appears to be an extension of its long standing management philosophy to continually study its systemic quality assurance weaknesses rather than implementing effective corrective actions to address them.

OIG continues to believe that RMA's quality assurance system should, at a minimum, be defined and codified in the regulations. Our reviews have continually shown that the current system's ineffectiveness is that it has been based on piecemeal changes and over reliance on insurance industry contributions. The current condition of the procedures for the QC process (Manual 14) attests to this. Until the contemplated actions and milestones for this new approach for a RMA quality assurance system are spelled out with regard to needed legislation and/or codification of the QC process in the regulations, we are unable to concur with the management decision for this recommendation.

RECOMMENDATION NO. 2

The RMA Administrator should issue basic program policy decisions, such as those reflecting the intended objectives of the QC system, including meaningful performance measures, and to commit itself to implementing these objectives.

RECOMMENDATION NO. 3

The RMA Administrator should develop a plan of action, a document specifically describing how the agency expects to implement an effective QC system over the long term. Such a plan of action should provide a timetable for implementing procedures, defining errors, establishing meaningful performance measures, applying consistent review procedures, and measuring improper payment amounts.

RMA Response

"RMA CONCURS [with Recommendation Nos. 2 and 3]. RMA is in the process of planning for a study and analysis of our contractual agreement for program delivery, which includes the QC system. The new QC system will include goals and objectives to evaluate performance and measure results. The estimated completion date for this effort is March 2003."

OIG Position

While this planned study and analysis may result in important progress in formulating a reliable approach in evaluating the integrity of the crop insurance program, RMA's proposal has not allayed our concerns about the priority the agency now places on successfully implementing an effective QC system. RMA must take aggressive action to define, describe, and implement a reliable and effective QC system.

RMA has stated that it proposes to contract for a study to recommend a new QC system, which will include goals and objectives to evaluate performance and measure results, and which is estimated for completion in March 2003. RMA's reply is vague and does not articulate clarification on those specific tasks addressing the RMA quality assurance program such as, establishing estimates of error rates, revising the insurance company contract review process, etc. Also, it's unclear as to whether the study will be completed by this date or if an effective QC system will be implemented by this date. Based on its past history regarding its approach and philosophy on quality assurance, we remain concerned that RMA's planned endeavor may not result in comprehensive and effective corrective actions being implemented timely. We cannot consider the management decisions for these recommendations until RMA provides its objectives, tasks, and specific milestones for describing the contents of the study, developing and implementing a new QC environment from the study results, and codifying this process in the regulations. The current state of this QC process requires RMA to begin now addressing identified weaknesses and not wait until March 2003 to strengthen or replace its QC system. RMA needs to identify and put in place those alternative actions in the interim to address known deficiencies in its quality assurance system before its management decisions can be considered.

FINDING NO. 2

INTERNAL CONTROL WEAKNESS NOT DISCLOSED UNDER FMFIA

RMA did not identify the absence of a reliable QC review system to evaluate private sector delivery of the Federal Crop Insurance Program as a material internal control weakness under the FMFIA report for the period ended September 30, 1999. Review of the departmental FMFIA report for fiscal year 1999 showed no internal control weaknesses included for RMA. RMA headquarters staff confirmed that no material internal control weaknesses were identified or reported by the agency for fiscal year 1999. The absence of a reliable QC review system to evaluate program delivery constitutes a significant internal control weakness that should be acknowledged by the agency. Agency failure to identify and report a material internal control weakness diminishes the Department's reputation for assessment of programs and operations.

RECOMMENDATION NO. 4

Recognize and report the absence of a reliable QC review system to evaluate private sector delivery of the Federal Crop Insurance Program as a material internal control weakness under the FMFIA. Annually disclose the noted weakness until such time as a reliable QC review system has been developed and fully implemented.

RMA Response

"RMA NON-CONCURS. RMA agrees that improvements can be made to enhance the effectiveness and efficiency of the current QC system. However, we do not believe OIG has provided sufficient evidence or justification showing the operation of this activity, is such, that it meets the criteria for reporting material weaknesses and system nonconformance defined under the Federal Managers Financial Integrity Act (FMFIA)."

OIG Position

RMA reported on October 1, 2001, to the Acting Chief Financial Officer that they had no new material weaknesses or system non-conformances for the period ended September 30, 2001. We disagree because RMA's QC system does not comply with GAO standards for internal control since its system cannot assess the quality of performance over time and identify the additional actions needed to further improve program efficiency and effectiveness. The current QC system suffers from the absence of policy establishing what the system should measure, what standards of accountability should apply, and the lack of prescribed procedures on conducting the individual reviews. The ineffectiveness of insurance company reviews and oversight of these reviews by RMA does not provide reasonable assurance that assets are safeguarded against waste, loss, unauthorized use or misappropriation, and constitute a material weakness. RMA still has not implemented an effective system. Therefore, in order for us to consider the management decision for this recommendation, RMA needs to report in its future FMFIA reports the absence of a reliable QC review system as a material weakness until this condition is successfully corrected.

EXHIBIT A – RMA RESPONSE TO DRAFT REPORT

USDA

United States Department of Agriculture

Farm and Foreign Agricultural Services
Risk Management Agency

OCT 24 2001

TO: Richard D. Long
Assistant Inspector General for Audit
Office of Inspector General

FROM: Phyllis W. Honor
Acting Administrator

SUBJECT: OIG Audit Discussion Draft 05099-14-KC – Monitoring of RMA's Implementation of Manual 14 Reviews/Quality Control Review System

Outlined below is our response to recommendations presented in the subject discussion draft report.

Recommendation 1

The RMA Administrator should propose a legislative initiative that would mandate a QC review system that reflects the goals and interests of the Department in assessing private sector delivery of the Federal Crop Insurance Program. Whether or not such a mandate is forthcoming, RMA should define and describe its QC system in regulations, where the system would gain an authoritative basis that was not subject to the influence from private industry.

RMA Response. RMA agrees that improvements are needed in the current QC system. However, enacting legislation to mandate a review system would not solve the current problem and would in fact make the system more difficult to manage and change. Also the legislative approval process is lengthy and time consuming. The current system needs to be revised to include the changes made by the Agricultural Risk Protection Act of 2000. We are in the process of awarding a contract to study our program delivery process and the underlying agreement. We expect the results to be available later in the year. In the meantime, we will consider alternative actions that can be taken to address the weaknesses cited in the report.

RMA

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Recommendation 2

The RMA Administrator needs to issue basic program policy decisions, such as those reflecting the intended goal of the QC system, and to commit itself to implementing.

RMA Response. RMA CONCURS. RMA is in the process of planning for a study and analysis of our contractual agreement for program delivery which includes the QC system. RMA will clearly define program policy, goals and objectives in any new system. The estimated completion date for this effort is March 2003.

Recommendation 3

RMA needs to develop a plan of action, a document specifically describing how the agency expects to implement an effective QC system over the long term. Such a plan should provide a timetable for implementing such procedures, the definition of an "error," and consistent review procedures.

RMA Response. RMA CONCURS. RMA is in the process of planning for a study and analysis of the QC system as a part of an overall review of our current delivery system. The new QC system will include clear goals and objectives to evaluate performance and measure results. The estimated completion date for this effort is March 2003.

Recommendation 4

Recognize and report the absence of a reliable QC review system to evaluate private sector delivery of the Federal Crop Insurance Program as a material internal control weakness under the FMFIA. Annually disclose the noted weakness until such time as a reliable QC review system has been developed and fully implemented.

RMA Response. RMA NON-CONCURS. RMA agrees that improvements can be made to enhance the effectiveness and efficiency of the current QC review. However, we do not believe OIG has provided sufficient evidence or justification showing the operation of this activity, is such, that it meets the criteria for reporting material weaknesses and system nonconformance defined under the Federal Managers Financial Integrity Act (FMFIA).

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2. OIG Audit Report No. 05099-51-Te, Compliance Review Program, 1988-1989 Review Schedule, issued March 29, 1991.
3. OIG Audit Report No. 05600-4-Te, Crop Year 1991 Claims, issued September 30, 1993.
4. OIG Audit Report No. 05099-1-At, Crop Insurance on Fresh Market Tomatoes, Crop Year 1996, issued September 30, 1997.
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12. GAO Audit Report No. RECD-99-266, Crop Insurance: USDA Needs a Better Estimate of Improper Payments to Strengthen Controls Over Claims, issued September 22, 1999.
13. OIG Audit Report No. 05099-2-At, Nursery Crop Insurance Program, Crop Years 1995 through 1996, issued December 16, 1998.
14. OIG Memorandum to the Honorable, Richard D. Lugar, Chairman, Committee on Agriculture, Nutrition and Forestry, issued April 17, 2000.

ABBREVIATIONS

APH	Actual Production History
BERR	Baseline Error Rate Review
CFR	Code of Federal Regulations
FCIC	Federal Crop Insurance Corporation
FMFIA	Federal Managers’ Financial Integrity Act
FNS	Food and Nutrition Service
FSA	Farm Service Agency
GAO	General Accounting Office
GPRA	Government Performance and Results Act
OIG	Office of Inspector General
QC	Quality Control
RMA	Risk Management Agency
SRA	Standard Reinsurance Agreement
USDA	US Department of Agriculture