

U.S. Department of Labor

Office of Inspector General
Washington, D.C. 20210



DEC 3 1998

The Honorable Dick Arme
Majority Leader
U. S. House of Representatives
Washington, D.C. 21515-6502

Dear Congressman Arme:

This is in response to your letter requesting that we identify the 10 most serious management problems facing the Department of Labor, including agency operations that are most vulnerable to fraud, waste, error, and mismanagement. In our opinion, the following are areas that we have identified as vulnerable and which merit attention:

- 1) Quality of Program Results Data
- 2) Year 2000 Compliance
- 3) Effectiveness of the Welfare-to-Work Initiative
- 4) Accounting for ETA Grant and Contract Funds
- 5) Security of Pension Assets
- 6) Protection of Worker Benefit Funds
- 7) Collection/Disbursement of Back Wages and Related Penalties
- 8) Compliance with New Financial Management Requirements
- 9) Stewardship over DOL Information Technology Resources
- 10) Accounting for Equity in Real Property

Enclosed is a description of our concerns in each of these areas for your use and consideration. I thank you for the opportunity to present our views on issues needing attention in the Department of Labor. If you need additional information or wish to have a more detailed briefing, please contact me at 202-219-7296.

Sincerely,

A handwritten signature in black ink, appearing to read "Charles C. Masten".

Charles C. Masten
Inspector General

Enclosure

cc: The Honorable Dan Burton
Chairman
Committee on Government Reform and Oversight

The Honorable Steve Horn
Chairman
Subcommittee on Government Management, Information, and Technology

Working for America's Workforce

U. S. DEPARTMENT OF LABOR TOP TEN MANAGEMENT ISSUES

1) QUALITY OF PROGRAM RESULTS DATA

Important initiatives are under way to improve the results of Federal programs and operations. With passage of the Government Performance and Results Act (GPRA), Congress intended to create a management process where Federal Agencies develop strategic plans, articulate program goals, allocate federal resources to meet desired performance levels, and measure and report program results. Similarly, the Federal Accounting Standards Advisory Board's Statement of Federal Financial Accounting Standard Number 4 (SFFAS 4), which was fully implemented in Fiscal Year 1998, is aimed at providing reliable and timely accounting for the full cost of Federal programs and activities. It will be vitally important for DOL to ensure that the performance and cost information generated be accurate and auditable in order for DOL's March 2000 performance reporting to be credible. However, there are a number of challenges faced by the Department in achieving the full accountability envisioned through these two measures, which are detailed below.

Linking Financial and Performance Data: Unlike the private sector where success is largely measured in terms of a bottom line, to determine the success of Government programs both financial and performance information is needed. By linking this type of information, the Department and Congress can determine the value and future direction of Federal programs and achieve the accountability demanded by the public. However, most Federal agencies, including DOL, have not yet achieved this linkage. DOL currently does not have an integrated strategic management process in which program objectives in strategic plans, the resources appropriated for carrying out the programs, the costs of activities, and the performance results achieved are closely linked. To this end, the Department needs to ensure the successful expansion of financial accounting to include cost accounting to identify the full cost of specific programs and activities. The Department is currently developing a cost accounting system. Initially, it will be performed at the DOL goal level. Eventually cost information will be accumulated for specific activities and performance results. However, even with the best effort, it will take a few years before DOL will be able to achieve this linkage.

Complications from Allocating Costs and Results Among Participating Agencies: A significant feature of the Workforce Investment Act of 1998 (WIA) is the establishment of one-stop delivery systems within each local workforce investment area. WIA designates certain entities as required one-stop partners and allows for additional partners, at local discretion. WIA requires that each local workforce investment board enter into memoranda of understanding with the partners to define how the one-stop system will operate in the local area and how the costs of the system and the services provided will be funded. However, cost funding and cost sharing present special problems in a one-stop environment. It increases the administrative burden of accounting for costs and benefits in a system where it was increasingly difficult to discern to which program the participants belonged and who should be paying the cost of services. This is further complicated by a key principle of Federal grant accounting -- that costs may be charged to a program only to the extent that benefits are received by that program.

To assist in addressing these issues, ETA published a technical assistance guide that proposed alternative cost allocation methodologies focusing on bottom line measures of benefits based on outcomes achieved, as opposed to more traditional approaches that emphasized processes and inputs. ETA will need to continue its efforts to reduce the administrative burden, while ensuring meaningful accounting for program costs by benefits received. Notably, these same difficulties will be faced by other job training programs as organizations attempt to portray the achievements associated with their respective investments. ETA needs to address these issues through the policy development and rule making process.

Data Limitations: Another challenge is the Department's limitations to access, or control the quality of, program results data that will be used to determine the attainment of its strategic plan goals. This includes difficulties associated with ensuring the quality of the myriad of data provided by states and other sources below the Federal level. It also includes ensuring that adequate internal controls exist over DOL financial and performance data systems.

In addition, two important tenets of GPRA are the requirements that agencies conduct program evaluations to determine program effectiveness and validation of performance data. In the employment and training area, it is particularly important to know whether programs have resulted in individuals becoming self-sufficient by obtaining long-term, unsubsidized employment, at livable wages. Two important tools that may be used to this end are unemployment insurance and social security wage records of individual program participants. However, the Department is limited in its ability to obtain such data for program evaluation and validation purposes. To enhance its ability to conduct program evaluation and validation in this and other equally important areas, the Department needs to have statutory authority to easily obtain and utilize these types records as one tool in determining or validating the results achieved for the substantial public investment.

2. YEAR 2000 COMPLIANCE

In the past year, considerable attention has been given to the impact the Year 2000 (Y2K) problem may have on the delivery of services by the Federal Government . The ultimate impact of the Y2K problem on DOL is still uncertain. As such, DOL must be persistent and timely in ensuring that it adequately converts, implements, and verifies its systems so that they will not be affected by this problem. In April, the OIG and DOL Chief Information Officer (CIO) began to assess and respond to the areas of greatest concern to the Department with respect to the Y2K problem. Since April, the OIG has worked collaboratively with the CIO, the DOL Information Technology Center, and each agency Y2K coordinator. This collaboration with the Department included the OIG conducting an audit to "baseline" the magnitude of the Y2K problem. The audit covered the 61 DOL mission-critical systems and focused on developing baseline information as to their status and progress, as well as the identification of concerns.

Our major immediate concern involves the benefit component of the Unemployment Insurance (UI) System. The UI system processes about \$22 billion in benefit payments annually in 53 jurisdictions nationwide. UI benefits are provided to approximately 7 million people through a Federal-State partnership with each state's State Employment Security Agency (SESA) office.

The OIG is concerned with the effect the Y2K problem may have on the disbursement of UI benefits after January 1, 1999, because when a claim is initiated, a benefit year is established for 1 year forward from the date when the claim is filed. Therefore, if a claim is filed on January 4, 1999, the system will calculate a benefit year ending date of January 4, 2000. Consequently, a system could deny benefits and/or eligibility to a claimant who files after January 1, 1999, if it is not Y2K compliant or if an effective contingency plan is not in place. There are seven states and territories struggling to maintain sufficient Y2K progress. They include: Arkansas, Delaware, the District of Columbia, Montana, New Mexico, Puerto Rico, and the Virgin Islands. In addition to the seven "at-risk" states and territories, other states were placed on a "watch list" due to previous performance problems relating to system development efforts. These states include: Illinois, Louisiana, Maine, and Nevada.

DOL is focusing on the problem and has formed a technical assessment and assistance team. However, solutions must be found and implemented before January 1999 to ensure a smooth transition and continuation of benefits for individuals who must temporarily rely on UI as a source of income.

Our audit also disclosed a number of other management-related issues of concern including: errors within agency status reports to the CIO, delays in the scheduling of independent verification and validation reviews of compliant systems, a lack of evaluation of DOL contingency plans, and delays in contingency planning by some states.

3. EFFECTIVENESS OF THE WELFARE-TO-WORK INITIATIVE

The Department's ability to provide effective training and employment services to help individuals transition from welfare dependency to self-sufficiency will be key to the success of welfare reform. The recently enacted Welfare-to-Work program has been added to the arsenal of DOL services available to help severely disadvantaged individuals change their lives. The success of the program will hinge not only on the effectiveness of the Department's stewardship and the quality of services provided, but also on its ability to capture and report the results of its efforts on behalf of eligible individuals. In addition, with billions of dollars invested in this initiative it will also be critical for the Department to provide effective monitoring of the substantial dollars awarded to grantees for employment and training services. This is an area of major concern, which is discussed in item 4.

4. ACCOUNTING FOR ETA GRANT AND CONTRACT FUNDS

ETA is DOL's largest grant and contract awarding agency. In FY 1998, ETA awarded \$10.3 billion in grants and contracts. These funds pay for employment and training programs and services and for the administration of unemployment insurance programs run by the States. Despite many improvements in this area in the past few years, our FY 1997 Financial Statement Audit revealed that DOL needs to address a number of grant and contract management issues.

The OIG audit disclosed that more attention is needed by management to ensure that ETA cost data is recorded promptly. While adequate systems are in place to facilitate this, there are still pockets of ineffectiveness within DOL with respect to complying with such requirements. For example, in our audit we found that an ETA regional office failed to record cost data for the Job

Corps program in FY 1997. This caused a \$69 million understatement of costs. We also found that grantee cost reports were not being recorded promptly. This is the result of delays by grantees in providing reports to ETA and delays by ETA in recording the information. Another deficiency identified is that of grant close-outs, which are conducted to complete a full accounting for the substantial dollars in each of the thousands of grants awarded by the Department. As of the date of our audit, there was a backlog of some 300 grants that needed to be closed out. Our audit also revealed that weaknesses relating to accounting for debt activity continued. Our major concerns are that the accounting system for ETA debts was not maintained current and that it does not allow for tracing transactions to source documents. We also found that ETA does not charge administrative costs or penalties to its debtors, as provided in the Debt Collection Act of 1982. These weaknesses diminish the Department's ability to collect debts or to do so in a timely manner.

Our concerns are compounded by the fact that ETA is now responsible for awarding and monitoring millions of additional grant dollars for the Welfare-to-Work Program. Grants awarded under this program in FY 1998 totaled \$1.2 billion. Because of the substantial dollars involved, it is even more critical for DOL to quickly and effectively address the weaknesses we have identified. To assist the Department in ensuring accountability over Welfare-to-Work grant funds, we are currently conducting post-award surveys of 34 grantees that were awarded funds in the first round of Welfare-to-Work's competitive grant process. The purpose of these post-award surveys is to examine the grantee's financial and program systems that are being planned and/or currently in operation for administering the grant. Our goals are to provide an early independent assessment of the grantee's capabilities for delivering a successful program, to determine whether internal controls are adequate, and to identify deficiencies in the design of the financial and program systems. The results will assist grantees in correcting any deficiencies and help them to avoid unallowable costs or administrative findings in the future.

5. SECURITY OF PENSION ASSETS

The security of pensions assets is a priority of the Department and of the OIG. This includes ensuring that weaknesses, vulnerabilities, and criminal activity are identified and addressed. The following are two areas that we have identified as particularly problematic.

Pensions Plan Audits: The Pension and Welfare Benefits Administration (PWBA) carries out activities aimed at protecting 6 million private sector benefit plans controlling more than \$3.5 trillion in pension plan assets. For the past several years, the OIG has raised a concern regarding the way pension plans are audited under the Employee Retirement Income Security Act (ERISA). Specifically, ERISA exempts from audit coverage all pension plan assets that have been invested in institutions, such as savings and loans, banks and insurance companies, that are already regulated by Federal or state governments. Because of this scope limitation, independent public accountants (IPAs) conducting audits of pension plans cannot render an opinion on the plan's financial statements in accordance with professional auditing standards. Nearly half of pension plan audits receive a disclaimer of opinion as a result of the limited scope exemption, which we believe should be repealed. The OIG has also recommended that IPAs and plan administrators be required to report serious ERISA violations directly to the Department to enhance oversight of plan assets.

Abuses by Pension Plan Service Providers: Private pension plans serve as an attractive target to organized crime elements, corrupt pension plan officials, and individuals who influence the investment activity of the pension assets. Recently, labor racketeering investigations involving the investment of pension plan monies that are jointly-administered by labor union representatives and management representatives (Taft-Hartley plans), have elevated the OIG's concern over the security of the assets in this segment of the pension plan universe.

OIG investigations have uncovered many criminal enterprises perpetrated by financial and investment service providers to the Nation's pension plans. These investigations have revealed abuses by sophisticated investment advisors and pension plan administrators who have the opportunity and ability to structure complex financial schemes to conceal their criminal activity. The OIG is concerned that abuses by financial investment service providers can result in great dollar losses because they typically provide investment or financial advice to more than one plan.

Based on recent investigative results and the fact that service providers typically control the investment of hundreds of millions of dollars of pension monies, the OIG has identified this area of the pension arena as especially vulnerable to organized crime activity and abuse.

6. PROTECTION OF WORKER BENEFIT FUNDS

The Department administers several programs and statutes designed to provide and protect the benefits of workers. Protection of such benefits is critically important because such programs affect the lives of millions of workers and retirees and involve billions of dollars of taxpayer dollars. The OIG has identified serious vulnerabilities within three of the Department's major worker benefit programs.

Continued Proliferation of UI Fraud Schemes: As with any multi-billion dollar Federal benefit payment program, there are those who benefit from the program illegally. Unfortunately, many states do not have the capability to effectively detect and investigate fraud schemes that stem from individuals, let alone, the growing number of increasingly complex interstate UI fraud schemes. A recent informal survey of the state employment security agencies (SESA) disclosed that the majority of the SESAs have concentrated on investigative work involving single claimant fraud cases, rather than the more complex interstate schemes (see appendix). Because of the large number of single-claimant cases, many states elect to direct their investigative resources into this area. That focus may ultimately increase a state's vulnerability to other fraud schemes, including fictitious/fraudulent employer schemes, internal embezzlements, manipulation of Standard Industrial Codes, as well as other expansive and complex fraud schemes being perpetrated against the UI Program.

In addition, a number of systemic weaknesses pose problems for the UI system. These include: loss of contributions due to the inability of states to search for hidden wages by employers who misclassify workers as independent contractors; increased vulnerability of the telephone initial claims system; loss of contributions due to the inability of states to audit large interstate companies; "shell" leasing companies which circumvent the payment of UI contributions; the selection process states use to audit employers; and the structural integrity in the reporting system of UI data from the states to UIS.

Through oversight of the UI program, we have identified a number of schemes used to defraud the program including fraudulent employer schemes, internal embezzlement schemes, and the fraudulent collection of UI benefits by illegal aliens using counterfeit or unissued social security numbers. These investigations have identified schemes which have resulted in substantial losses to the UI trust fund. Our investigations have disclosed that the ability to file electronic and mail claims presented these individuals with the opportunity to defraud multiple states from a single location. In addition, they were able to create unlimited false identities through the use of fraudulent or unissued social security numbers thereby creating an unlimited potential for filing false claims. The OIG is very concerned about the continued proliferation of these types of schemes against the UI program. We believe there is a need for: increased training of state employees in fraud detection techniques, improved internal program controls, and improved enforcement.

Federal Employees' Compensation Act (FECA): FECA provides compensation and medical care for Federal employees who suffer job-related injuries, diseases or deaths. The OIG has been working with the Department to improve the cost-efficiency of the FECA program. Our September 1997 audit report on FECA Medical Provider Payments concluded the Department can save millions each year by utilizing commercial code manipulation detection packages to screen for improper billings. An OIG recommendation from our audit of the FECA Special Benefits Fund Financial Statements for Fiscal Year 1992 was that the Office of Workers' Compensation Programs request automated wage data from the Social Security Administration on an annual basis to determine continuing eligibility for FECA compensation, instead of the labor-intensive manual procedure currently in use. We are doing additional work in this area to quantify the potential savings to be realized through automated cross-matching with SSA records.

In addition, a 1996 OIG report, done in conjunction with the President's Council on Integrity and Efficiency, took a multi-agency look at the effectiveness of Federal civilian agencies' management of their FECA programs. The audit report, which summarized the results of audits undertaken by the Inspectors General of 13 agencies, disclosed that employing agencies generally needed to improve the management of their workers' compensation programs. The audits found employing agencies paid more in workers' compensation than was necessary and that injured employees sometimes experienced an interruption of their incomes. Recommendations addressed the need to improve returning injured employees to work, verifying FECA chargeback reports and processing FECA claim forms.

Finally, OIG investigations continue to disclose the vulnerability of this program to fraud.

Fraudulent activities include medical providers who: bill the Government for services that were not rendered, charge multiple times for the same procedure, bill for non-existent illnesses or injuries, or overcharge for services; and claimants who defraud the program by reporting false injuries, recover but continue claiming benefits, or do not report or under-report their outside employment income to OWCP.

The OIG has proposed a number of legislative recommendations to address some of the weaknesses of this program including: providing DOL with statutory authority to access social security wage records to identify claimants abusing the program; requiring a 3-day waiting period before continuation of benefits can be received; reducing compensation levels that currently offer no incentive for claimants to go back to work; and establishing a mandatory retirement age, whereby FECA recipients who reach a designated age would revert to benefit levels more consistent with the levels provided through Federal retirement.

Black Lung Trust Fund Deficit: DOL administers a trust fund to provide disability benefits and medical services to eligible workers in the coal mining industry, when a mine operator cannot be determined liable for providing such benefits. The OIG is concerned with the escalating indebtedness of the Black Lung Disability Trust Fund. The Department's consolidated financial statements for Fiscal Year 1996 reflected that the trust fund was in debt \$5.1 billion to the U.S. Treasury. For Fiscal Year 1998 the debt has risen to \$5.9 billion.

The debt results from advances provided to the program. These advances, which have become an annual necessity for the fund, were originally obtained to fund benefit payments that could not be met by coal excise tax collections (the principal source of revenue to the fund). Currently, the excise taxes are sufficient to pay benefits and administrative costs; however, the fund must continue to borrow from the Treasury to pay the interest due on past advances. Of the \$5 billion of cumulative advances in FY 1996, only \$2 billion were spent for benefit payments, \$3 billion were spent on interest. The fund has been unable to repay any principal on these advances, and it must continue to borrow to pay interest.

Management's annual projections of future receipts and outlays indicate that cumulative borrowings from Treasury could total \$30 billion (unaudited) or more by 2038. At this point, annual benefit payments by the fund arising under the Black Lung Benefits Revenue Act of 1977 are expected to be less than 10 percent of current benefit payments. However, based on legislation enacted in 1987, coal tax rates will be dropping by 50 percent after the year 2013. Therefore, the debt problem is compounded and, according to management's estimates, the excise tax collections by 2038 would cover less than 30 percent of the interest that is accruing and annual advances will exceed \$1.2 billion per year. The Department has acknowledged that if current operating conditions continue, a change in the statutory operating structure of the Trust Fund will be necessary to meet its obligations.

7. COLLECTION/DISBURSEMENT OF BACK WAGES AND RELATED PENALTIES

In some circumstances, the Department assumes responsibility for distributing to workers back wages paid by employers who have been found to have violated labor laws. For a number of years we have raised concerns about the effectiveness of the Department's back wage collection and disbursement activities. We have raised our concerns in this area in our audits of the DOL consolidated financial statements, and two audit reports related to the Wage and Hour Division's Back Wage Collections and made recommendations for improvements. Specifically, these include the need to improve the accounting and collection of back wages and related penalties, improve the methods for locating and restoring back wages to the affected employees, and revert undistributed amounts to the Treasury.

8. COMPLIANCE WITH NEW FINANCIAL MANAGEMENT REQUIREMENTS

The Department has made great strides in financial management and has positioned itself to prepare timely and accurate annual financial statements, as required by the CFO Act and the Government Management Reform Act. This is most notably evidenced by the fact that the Department received its first ever clean opinion on its financial statements for FY 1997. However, despite this progress, DOL still faces several significant deficiencies in its day-to-day accounting operations, primarily related to needed improvements in financial management system design.

The OIG is required by the Federal Financial Management Improvement Act (FFMIA) to assess the Department's financial management systems for compliance with a number of financial management and accounting requirements. We have determined that seven DOL systems do not substantially meet one or more of these requirements. These systems pertain to the accounting for back wages, ETA grant-related receivables, MSHA and OSHA penalties, and Job Corps' investment in real and personal property. FFMIA gives the Department 3 years to correct the noted deficiencies. The Department will need to employ every effort to ensure these system deficiencies are corrected within the required time frame.

9. STEWARDSHIP OVER DOL INFORMATION TECHNOLOGY RESOURCES

Information Technology (IT) is a high-cost, critically important resource that is used to provide essential data and information to the Congress, the public, and the Department itself. DOL program officials use information residing in DOL computers to pay benefits, target enforcement efforts, compile labor statistics and make other decisions that affect the health, safety, and economic security of Americans. Information technology is integrally linked to, and will be key to the success of, the GPRA and other management initiatives discussed in item 1. Moreover, implementation of the Information Technology Management Reform Act and the IT strategic plan will be crucial to managing and linking DOL financial and performance systems. Of major importance is the fact that Congress will utilize information generated by DOL's IT systems to assess the results and impact of DOL programs and make decisions as to their future direction.

Because of the high cost and importance to DOL's mission, investments in information technology related to mission-critical systems pose great risks. Recent developments, including the Year 2000 problem and widely publicized breaches of Government computer

security and personal privacy, have focused further attention on this issue. As the Department becomes more dependent on the use of IT resources to carry out its mission and daily operations, effective stewardship by the Chief Information Officer over such resources must be ensured. This includes identifying and mitigating risks to avoid inflated budgets, cost overruns, delays, and failures. In addition, it is important to audit the life-cycles of system development efforts to ensure they meet their intended objectives at acceptable costs. This area is of such importance that the OIG has developed a 5-year audit plan identifying and prioritizing IT issues for oversight. However, competing priorities and increased statutory mandates in other areas have diffused the OIG's ability to provide adequate coverage of IT issues in the Department. Our view is that closer attention is needed in this area.

10. ACCOUNTING FOR EQUITY IN REAL PROPERTY

The OIG remains concerned with ETA's accountability over real properties, held by State Employment Security Agencies (SESAs), in which DOL has an equity interest. An audit issued in September 1997, found that DOL's equity had increased to \$381 million, or 30 percent, between 1988 and 1996. We found states had made significant changes (capital improvements, acquisitions, disposals, etc.) without ETA's knowledge. The \$381 million figure is based on actual costs and does not represent the fair market value of the property, which may be significantly higher. We concluded ETA's current operating procedures are insufficient to keep the inventory reasonably current, placing ETA at risk of not being fairly compensated when the properties are sold, disposed of or put to other use. We made several recommendations to restore accountability over SESA real property.