

**Management's
Discussion and
Analysis**

The Management's Discussion and Analysis (MD&A) is considered Required Supplementary Information for the audit of the financial statements and is designed to provide a high level overview of the Agency. It provides a description of who we are, what we do and how well we meet the goals we have set.

The Mission, Programs and Agency Organization section highlights SSA's mission as set forth in the Agency's Strategic Plan. This section also discusses the major programs we administer: the Old-Age and Survivors Insurance (OASI) and the Disability Insurance (DI) programs (commonly known as Social Security) as well as the Supplemental Security Income (SSI) program.

Following the Mission, Programs and Agency Organization section is a discussion of the Major Issues that SSA will be facing in the future. We used the Performance and Accountability Report to provide a snapshot of the performance we achieved in FY 2001. However, the status of SSA would not be complete without providing a sense of the challenges tomorrow brings. These challenges include long-term solvency of the Social Security program and fulfilling our commitment to world-class service as well as topics that have a more immediate impact on our operations such as SSI and DI management improvement and fraud prevention and detection. While these issues are challenging, we believe we have the policies and plans in place to help ensure they will be adequately addressed.

Next, the MD&A discusses SSA's ability to achieve the five strategic goals contained in our current strategic plan. In March 2000, we provided Congress with our FY 2001 Annual Performance Plan (APP) outlining the performance indicators we used to assess our ability to meet these five strategic goals. In April 2001, we provided Congress with our FY 2002 APP and Revised Final FY 2001 APP, which revised several FY 2001 Government Performance and Results Act (GPRA) performance indicators. The Performance Goals and Results section provides a discussion of SSA's GPRA strategy and includes a summary of FY 2001 performance. It also includes selected indicators from the APP, targeted performance for FY 2001 and actual performance achieved.

In addition to discussing program performance, the MD&A also addresses our financial performance. The major sources and uses of SSA's funds as well as the use of these resources in terms of both program and function are explained. Finally, the Systems and Controls section of the MD&A provides the Commissioner's Federal Managers' Financial Integrity Act (FMFIA) assurance statement, the actions SSA has taken to address our management control responsibilities and a discussion of the Agency's FMFIA material weakness and plan to correct this weakness.

Mission, Programs and Agency Organization

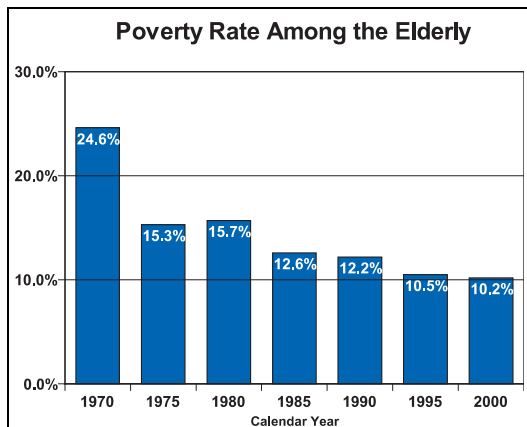
Mission

To promote the economic security of the nation's people through compassionate and vigilant leadership in shaping and managing America's Social Security programs.

The Social Security Programs

The Social Security Act established a program to help protect aged Americans against the loss of income due to retirement. Protection for survivors of deceased retirees was added by the 1939 amendments, thus creating the OASI program. Social Security protection for workers was expanded again in 1956 to include the DI program. SSA's responsibilities were further expanded in 1972 to include the SSI program and again in 1999 to include Special Benefits for Certain World War II Veterans (title VIII).

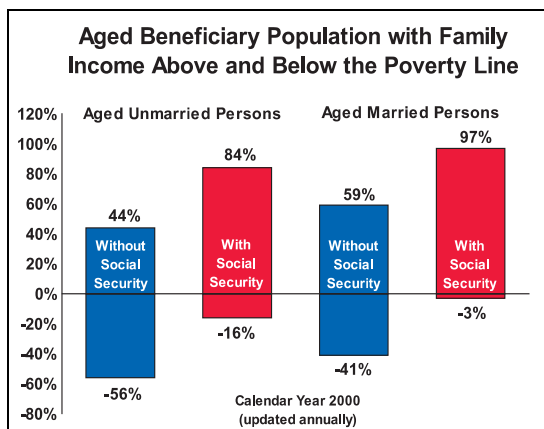
The combined Old-Age, Survivors and Disability Insurance (OASDI) programs, commonly referred to as Social Security, provide a comprehensive package of protection against the loss of earnings due to retirement, disability and death. Monthly cash benefits are financed through payroll taxes paid by workers and their employers and by self-employed people. Social Security is intended to replace a portion of these lost earnings, but people are encouraged to supplement Social Security with savings, pensions, investments and other insurance.



Social Security benefits have significantly improved the economic well being of the nation. Poverty among the elderly has been reduced by 59 percent over the past 30 years. In 1936, when Social Security numbers were first assigned to workers, most of the nation's elderly were living in poverty. Today, monthly benefits are an important part of the quality of life of elderly Americans and millions more who are protected in case of death or disability.

The monthly benefit amount to which an individual (or spouse and children) may become entitled under the OASDI program is based on the individual's taxable earnings during his or her lifetime. The maximum amount of earnings on which contributions were payable in 2000 was \$76,200 and increased to \$80,400 in 2001.

OASI Program: In 2000, the family income of 16 percent of aged, unmarried beneficiaries fell below the poverty line. Without Social Security benefits, 56 percent of those beneficiaries would have income below the poverty line – a difference of 40 percent due to receipt of Social Security.



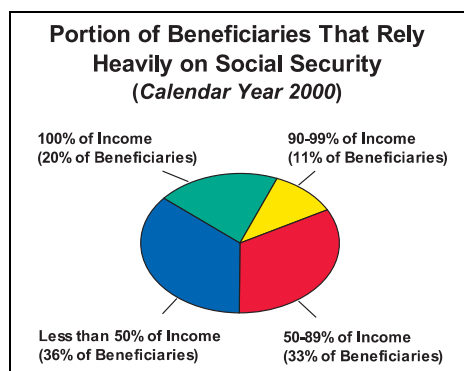
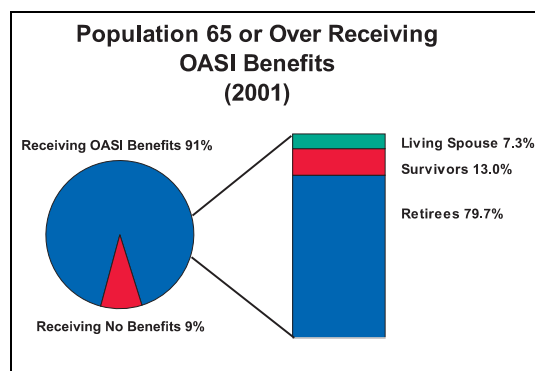
Social Security also lifted many aged married beneficiaries out of poverty. In 2000, 3 percent of aged beneficiaries who were members of a married couple had income below the poverty line. Without Social Security benefits, 41 percent of these beneficiaries would have income below the poverty line – a difference of 38 percent.

To qualify for OASI benefits, a worker must have paid Social Security taxes (Federal Income Contributions Act and/or Self-Employment Contributions Act) for at least 10 years (or 40 credits) over the course of his/her lifetime. Individuals born before 1929 need fewer credits to qualify. Nine out of 10 working Americans can count on benefits when they retire, with reduced benefits payable as early as age 62. Benefits are also paid to certain members of retired workers' families and to survivors.

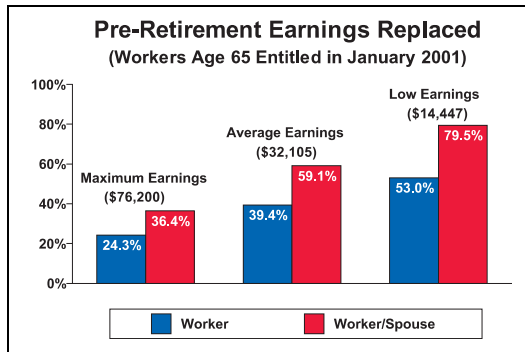
As shown in the chart below on the left, 91 percent of people age 65 or over in calendar year 2001 were receiving benefits. The largest category of beneficiaries over age 65 is retired workers. About 98 percent of children under 18 and their mothers or fathers with children in their care under 16 can count on monthly cash benefits if a working parent dies.

Social Security benefits comprised 38 percent of the aggregate share of all income to the aged population 65 and over of which 90 percent were Social Security beneficiaries. Other sources of income include assets (18 percent), earnings (23 percent), and pensions (18 percent) both Government and private.

While many of the nation's aged population have income from other sources, a portion of the beneficiary population relies heavily on Social Security. For 20 percent of beneficiaries, it is the only income; for 11 percent of the population, it contributes almost all of the income; and for another 33 percent of the beneficiaries, it is the major income source (see chart below on right).

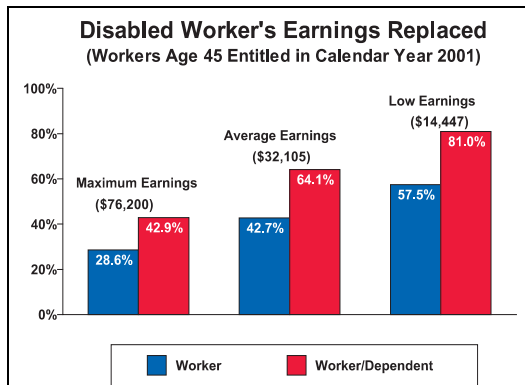


The level of preretirement earnings replaced by Social Security benefits for a worker retiring at age 65 varies because the benefit formula is weighted in favor of workers with low levels of earnings. The chart to the right shows the replacement rate in 2001 for individuals and couples (i.e., worker with a spouse who is not insured) at various earnings levels (2000 earnings levels are shown since that is the assumed last year of earnings).



DI Program: To qualify for DI benefits, an individual must meet a test of substantial recent covered work before becoming disabled. Disability benefits provide a continuing income base for eligible workers who have qualifying disabilities and for eligible members of their families. Three of four working Americans age 21 through 64 can count on receiving benefits if they become disabled. Workers are considered disabled if they have a medically determinable physical or mental impairment that prevents them from engaging in substantial gainful activity. The disability must be expected to last for a continuous period of at least 12 months or to result in death.

Once benefits begin, they continue for as long as the worker is disabled and does not perform substantial gainful work. There are provisions that provide incentives for work. Disability cases are reviewed periodically to determine if the worker continues to be disabled.



The chart to the right shows the replacement rate in 2001 for disabled workers and their dependents at various earnings level (2000 earnings levels are shown since that is the assumed last full year of earnings).

The table below presents a historical perspective on average earnings replacement for both the OASI and DI programs.

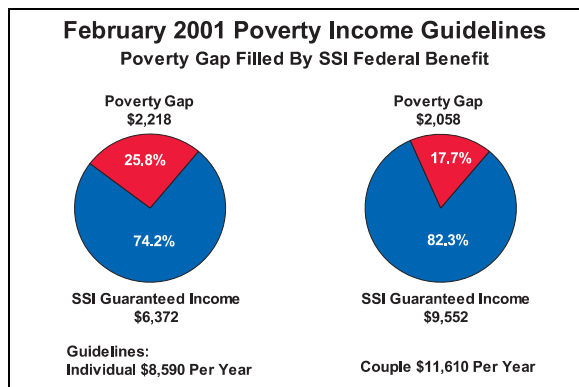
| Average Earnings Replaced Historical Perspective | | | | | | |
|---|-------|-------|-------|-------|-------|-------|
| | 1951 | 1961 | 1971 | 1981 | 1991 | 2001 |
| Disabled Worker ¹ | NA | 32.3% | 36.6% | 43.9% | 43.0% | 42.7% |
| Retired Worker | 27.3% | 32.3% | 36.6% | 54.4% | 43.0% | 39.4% |

1. Data not available for disability benefit payments which began in 1957. Based on 45-year old disabled worker.

SSI Program: SSI is a means-tested program designed to provide or supplement the income of aged, blind or disabled individuals with limited income and resources. SSI payments and related administrative expenses are financed from general tax revenues, not the Social Security trust funds. Qualified recipients receive monthly cash payments from SSA sufficient to raise their income to the level guaranteed by the Federal SSI program. Children, as well as adults, can receive payments because of disability or blindness.



The definitions of disability for adults used in the SSI program, as well as continuing disability review procedures, are the same as those used in the DI program. There is a separate definition of disability for children seeking SSI benefits. There are general provisions to encourage working and special incentives to those beneficiaries who have disabilities or are blind. The Federal benefit rate and eligibility requirements are uniform nationwide. However, those with other income receive less since benefits may be reduced by the income they receive from other sources.

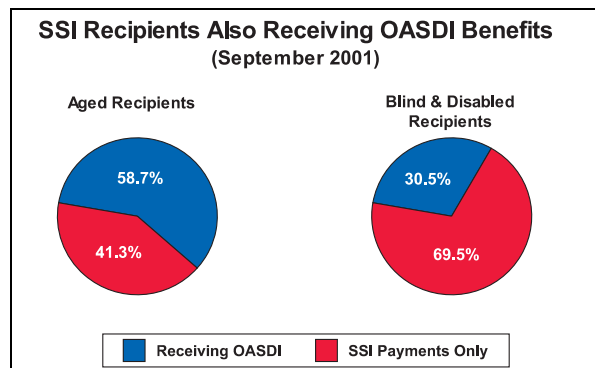


As shown in the chart to the left, SSI recipients with no other income receive the full SSI Federal benefit which is 74.2 percent of the poverty level for an individual and 82.3 percent for a couple.

The portion of the poverty gap not filled by Federal SSI may be filled by State SSI supplementation payments. Also, SSI recipients may be eligible for food stamps, Medicaid and social services.

In September 2001, 35.9 percent of all SSI recipients also received Social Security benefits. Most did not have any other income. For 4.4 percent of the recipients, earnings were a source of additional income, and 11.7 percent had unearned income from other sources, such as Veterans' pensions.

OASDI beneficiaries may qualify for SSI benefits if they meet SSI income and resource eligibility requirements. Although 35.9 percent of all SSI recipients receive OASDI benefits, SSI aged recipients are more likely (58.7 percent) to be receiving Social Security benefits than SSI blind and disabled recipients (30.5 percent).



Special Benefits for Certain World War II Veterans: Title VIII of the Social Security Act, enacted

December 14, 1999 as part of the Foster Care Independence Act of 1999, provides a monthly cash payment to certain World War II veterans who are eligible for SSI in both December 1999 and the month in which he or she files an application for the special benefits and who reside outside of the 50 States, the District of Columbia and the Northern Mariana Islands. Payments began in May 2000.

Support to Other Programs

In addition to its basic programs, SSA also provides a significant measure of service delivery support to other programs, particularly Black Lung, Medicare, Medicaid, Food Stamps and Railroad Retirement.

Black Lung Program: The Black Lung (BL) program pays monthly cash benefits to coal mine workers and their dependents and survivors. SSA is responsible for administering Part B of the BL program under title IV of the Federal Coal Mine Health and Safety Act. Part B covers claims filed by miners before July 1973 and survivor claims filed before January 1974 or within 6 months of the death of a miner or widow on the SSA rolls, whichever is later. Any claims filed after these dates generally are the responsibility of the Department of Labor (DOL) covered under Part C of the program.

SSA is also responsible for taking claims for, and performing certain other services related to, Part C benefits. In FY 2001, SSA field offices took 555 claims for Part C benefits and transferred them to DOL for payment, as required by law. SSA received full reimbursement from DOL for these services. Beginning in FY 1998, DOL provided administrative services for the Part B program under an interagency agreement with SSA and certified for payment all Part B benefits from funds appropriated to SSA. However, SSA retains responsibility for these payments.

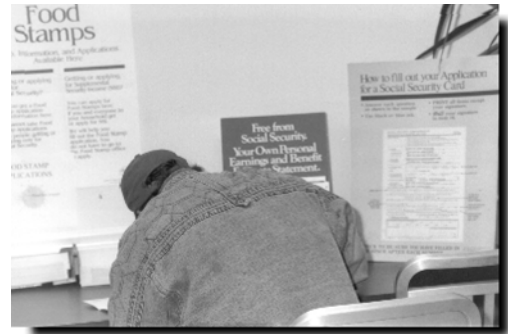
Medicare: Being a primary public contact point for the Centers for Medicare and Medicaid Services (CMS), SSA provides key services to the Medicare program. SSA staff determine and answer questions regarding Medicare eligibility, maintain the computerized records of Medicare eligibility, and collect Medicare premiums through withholdings from Social Security payments. Annually, SSA devotes about 1,485 workyears to supporting these workloads and funds for these services are drawn from the Medicare trust fund. In addition, Administrative Law Judges in SSA's Office of Hearings and Appeals provide hearings and adjudicate disputed appeals of Medicare reimbursements.



Medicaid: In 32 States and the District of Columbia, eligibility for SSI benefits confers automatic entitlement to Medicaid. Thus, the SSI eligibility determination made by SSA saves a significant number of workyears for these States. SSA also provides information and referral services in support of Medicaid and is directly funded by the States and CMS.

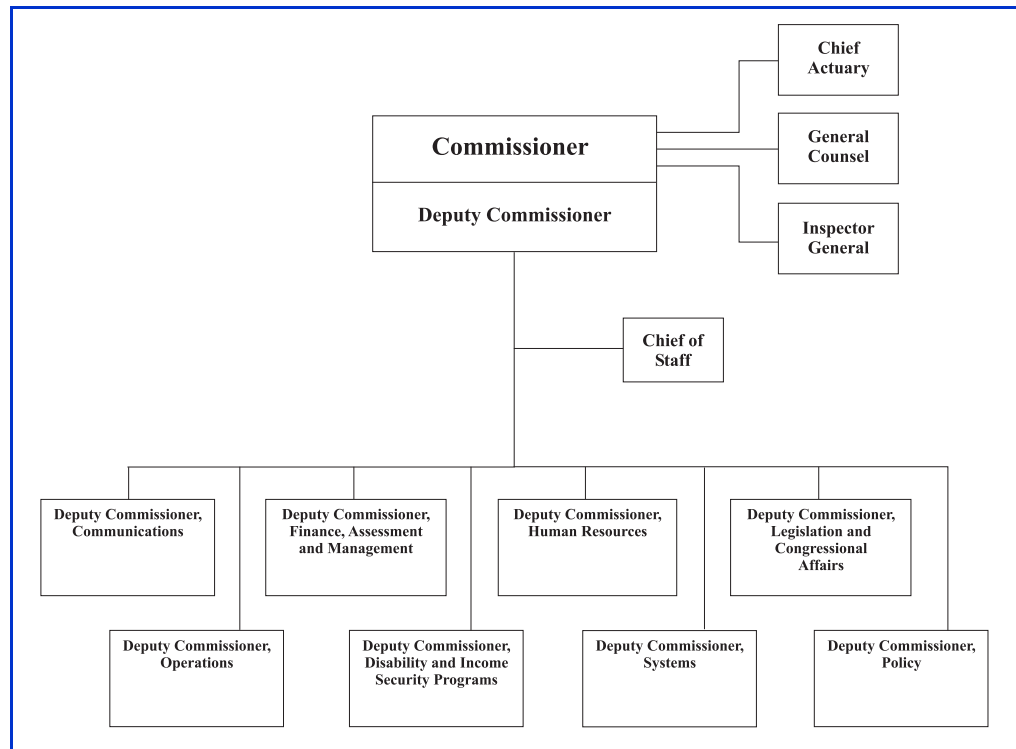
Railroad Retirement: SSA provides services in connection with entitlement to benefits from the Railroad Retirement Board (RRB). SSA takes the applications, determines jurisdiction and coordinates benefit payments with the RRB. The latter organization, as required by statute, issues a combined monthly benefit payment when a retiree is entitled to both Railroad and Social Security retirement benefits due to having worked for both the railroad and other industries prior to retirement. SSA reimburses the RRB for OASI and DI benefits paid on SSA's behalf. In addition, SSA arranges an annual financial interchange with the Railroad Retirement Trust Fund to place the Social Security trust funds in the same position they would have been in had railroad employment been covered by Social Security.

Food Stamps: SSA assists the Department of Agriculture by providing information about the food stamp program and taking food stamp applications for qualified OASI, DI and SSI claimants. In FY 2001, SSA processed 19,176 food stamp applications and recertifications.



State and Local Programs: SSA regularly provides information from Social Security records needed to make eligibility and payment decisions for a variety of State and local welfare programs, and provides automated data exchanges with over 100 State and Federal agencies.

Agency Organization

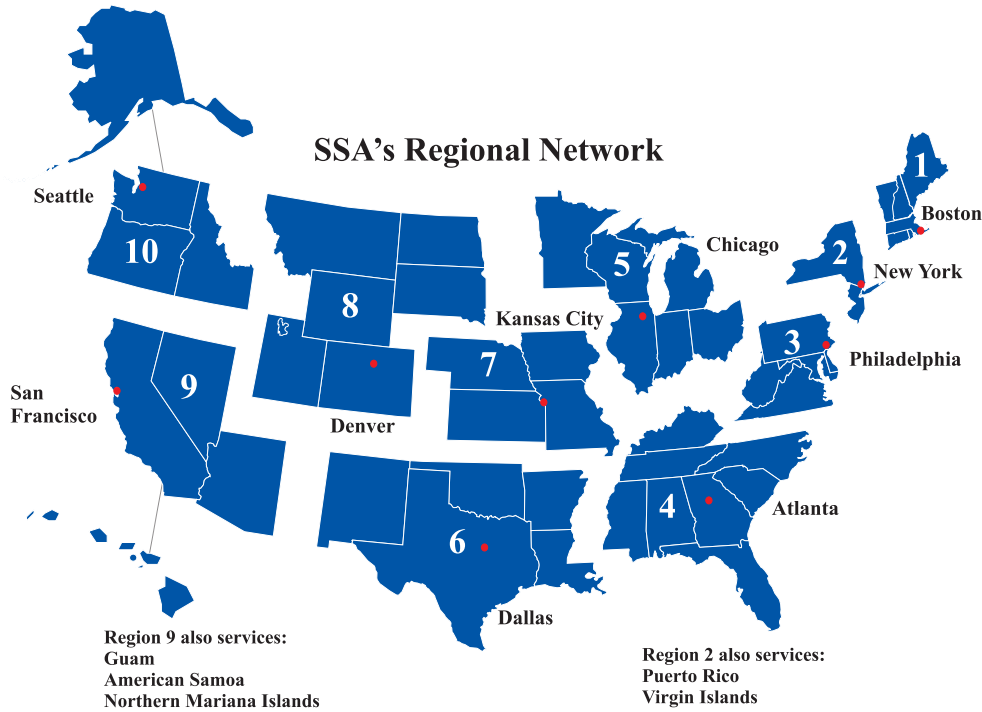


SSA's organization features centralized management of the national Social Security programs and a decentralized nationwide network of 10 Regional Offices overseeing 1,337 field offices (FO), 138 hearings offices, 36 teleservice centers, 7 processing centers and 1 data operations center.

SSA's unique organizational structure is designed to provide responsive, swift and accurate world-class service to the public. All components within SSA's central office perform a supporting role to SSA FOs by providing uniform directions, guidance and material resources needed by the FOs. By integrating services for all the programs we administer, we are able to enhance efficiency, avoid duplication of effort and increase opportunities to provide one-stop service to the public.

FOs are located in cities and rural communities across the nation and are the Agency's main physical point of contact with beneficiaries and the public. Additionally, the Social Security disability program depends on the work of 54 Disability Determination Services which include all 50 States, the District of Columbia, Guam and Puerto Rico.

To meet the needs of non-English-speaking persons, SSA recruits bilingual individuals to serve as a public contact for persons visiting SSA field offices and calling SSA's 800-number telephone service. During FY 2001, 15 percent of the Agency's new hires were bilingual. At year end, SSA had public contact employees who could provide service in English and at least one of 23 other languages.

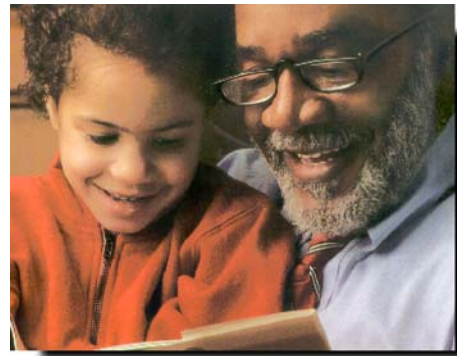


Major Issues Facing SSA

SSA's Performance and Accountability Report summarizes the Agency's achievements in administering its programs and managing the resources entrusted to it. In addition to the retrospective information provided by the report, we believe a full picture of the Agency's and the program's status must also consist of a discussion of those current issues with possible major impact on future operations. These issues include long-term program financing, as well as human resource challenges, stewardship responsibilities and fair and equitable administration of our programs.

Long-Term Program Financing

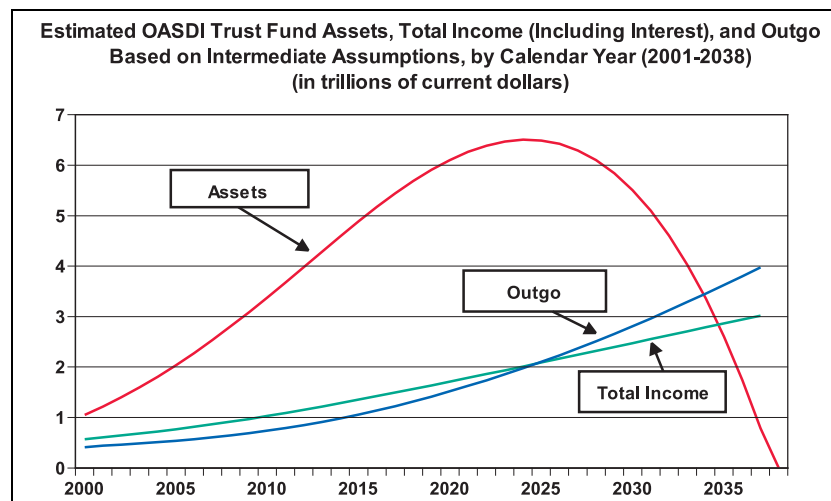
The Social Security program has helped provide economic security for American workers and their families for more than 60 years. However, the program faces serious financial challenges over the next several decades. Addressing Social Security's long-term financing shortfall is essential because of the important role Social Security plays in the lives of so many people. At the end of 2000, 45.4 million people were receiving monthly Social Security benefit payments. And these benefits keep many Americans out of poverty. For example, in 1999, only about 8 percent of Social Security beneficiaries



age 65 or older fell below the poverty line. But without Social Security, approximately 48 percent of those over age 65 would have been in poverty. Social Security is the major source of income for two-thirds of all retirees. For one-third, it's virtually all of their income.

Social Security is more than just a retirement program, however. About one-in-three Social Security beneficiaries is not a retiree. Approximately 7 million are survivors of deceased workers, and 6.7 million are disabled workers and their families.

The Scope of the Financing Shortfall



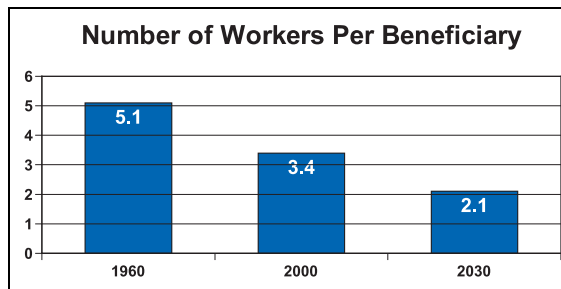
Currently, Social Security tax revenues exceed benefit payments, and the system is building large trust fund reserves to help finance the retirement of the baby boom generation. Under current estimates, benefit payments will begin to exceed taxes in 2016, and Social Security will start using annual Trust Fund interest to help pay benefits. Starting around 2025, Social Security will need to use the Trust Fund reserves themselves to help pay benefits; by about 2038, the Trust Fund reserves will be exhausted. At that time, it is estimated that current Social Security tax receipts will provide sufficient funds to meet only about 73 percent of benefit obligations.

The Demographic Challenges Facing Social Security

Social Security is basically a pay-as-you-go system, whereby Social Security taxes collected from today's workers and their employers pay the benefits of today's beneficiaries. But changing demographic factors—including increased longevity and lower birth rates—are straining the system's financing.

Americans are living longer, healthier lives. In 1946, 11 million Americans were 65 or older. Today, there are 35 million older Americans, and that number will double in the next 30 years. Life expectancy also continues to rise. In 1940, life expectancy for a 65-year-old was 12 1/2 years; today, it's 17 1/2 years, and by 2030, it is projected to be about 19 years.

At the same time, birth rates are lower. The result of these demographic trends is a continued decline in the ratio of workers to beneficiaries. In 1960, there were about 5 workers per beneficiary; today there are 3.4 workers per beneficiary, and that ratio is projected to decrease to about 2 workers per beneficiary by 2030 (see chart to the right), placing a strain on the pay-as-you-go system.



Social Security Strengthening and Modernization Initiatives

President Bush stated in his Inaugural Address that “We will reform Social Security and Medicare, sparing our children from struggles we have the power to prevent.” To meet this commitment, on May 2, 2001, President Bush signed an Executive Order creating the President’s Commission to Strengthen Social Security. President Bush listed six principles to guide the Commission’s reform efforts:

- Modernization must not change Social Security benefits for retirees or near-retirees.
- The entire Social Security surplus must be dedicated to Social Security only.
- Social Security payroll taxes must not be increased.
- The Government must not invest Social Security funds in the stock market.
- Modernization must preserve Social Security’s disability and survivors components.
- Modernization must include individually controlled, voluntary personal retirement accounts, which will augment the Social Security safety net.

On July 24, the Commission issued an interim report on its findings, and is scheduled to issue a final report by the end of the calendar year with recommendations to preserve Social Security while also providing for personal savings and investment accounts.

Disability Program Issues

Disability Process Management Improvement

SSA strives to deliver the highest levels of service by making fair, consistent and timely eligibility determinations and decisions at all adjudicative levels. However, applicants and beneficiaries sometimes find the current process complex, fragmented, confusing, impersonal and time consuming. Some also perceive the process as one in which different decisions are reached on similar cases at different levels of the administrative review process, thus some applicants must maneuver through multiple appeals steps before they receive a final decision.

To remedy these concerns and perceptions, the Agency announced a plan to test revisions to the disability eligibility determination process. The plan is a combination of initiatives that have demonstrated significant promise through testing and piloting over the last few years. It includes all levels of eligibility determination, beginning with the Disability Determination Services (DDS) in each State which perform initial disability determinations and going all the way through the hearing and appeal processes.

The DDS initiatives include the following:

- Providing more complete development and improved explanations of how the disability determination was made in order to enhance the quality of determinations.
- Enhancing the role of the State agency medical or psychological consultant to function as a true consultant in the disability determination process by providing information and advice to the disability examiner deciding the case.
- Providing the claimant with an increased opportunity to interact with the disability decisionmaker earlier in the process and to submit further information.
- Testing the elimination of the reconsideration step in order to streamline the process.

These initiatives were combined to form a new disability claims process for which the Agency has developed a prototype in 10 States.

Throughout this prototype, the Agency will further analyze and refine its improvements to the disability process. The Agency is continuing to gather and analyze data.

Similarly, SSA implemented the Hearings Process Improvement (HPI) plan. This includes: a national workflow model that combines pre-hearing activities so that fewer handoffs occur; early case screening and analysis; early claimant contact through pre-hearing conferences; certification of cases as ready-for-hearing; processing time benchmarks for critical steps within the process; group-based accountability for case processing from start to finish; and improved automation and data collection.

SSA is currently undertaking a broad scale evaluation of all aspects of the new hearing process. The Agency is closely monitoring progress, soliciting and considering feedback about the process from within and outside the Agency. A Steering Committee, in consultation with the Social Security Advisory Board, is responsible for leading the evaluations of HPI and has multi-component representation, including employee representatives.



The final step in the administrative appeals process rests with the Appeals Council and its Administrative Appeals Judges. The Appeals Council level of review represents an important link between the administrative appeals process and the judicial system. When a claimant requests the Appeals Council to review a hearing decision, the Appeals Council considers the evidence of record, any new and material evidence submitted to it which relates to the period on or before the date of the Administrative Law Judge's (ALJ) hearing decision, and the ALJ's findings and conclusions.

The Appeals Council Process Improvement (ACPI) plan is designed to provide high quality service to more claimants in less time. The plan includes a series of short-term initiatives designed to reduce the number and age of cases pending at the Appeals Council, and longer term structural and technological improvements designed to enable the Appeals Council to keep pace with future requests for review.

Implementation of the ACPI plan began in March 2000. The number of requests for review pending at the Appeals Council has declined from a high of nearly 156,000 in January 2000 to less than 95,355 by the end of September 2001. The average time to process a case has declined from 556 days to 447 days during that period, and more than 12 percent of all request for review actions processed in FY 2001 have been processed within 105 days.

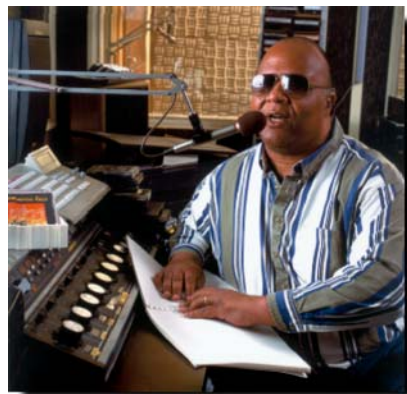
These disability management initiatives are progressing at different rates. The DDS initiatives seem to be proceeding as planned, but we do not yet have the complete data needed to assess their success and future direction. HPI results have been uneven. ACPI is making good progress, but longer-term improvements have not yet been initiated. Formal evaluation of these initiatives, to validate initial expectations with actual results, is in progress and will provide additional opportunities for improvement.

The Supreme Court has accepted an appeal by SSA on a case that could have far-reaching implications for the Social Security Disability Insurance (SSDI) and SSI programs. The case, called *Barnhart v. Walton* (No. 00-1937), addresses two issues: Whether a claimant is entitled to SSDI or SSI based only on a medical condition that has lasted or can be expected to last for at least 12 months, even though the inability to do substantial gainful activity has not lasted and can not be expected to last for 12 months; and whether some people who go to work (or become able to go to work) before we decide their claims can be found to be disabled and entitled to a "trial work period." We expect a decision by the summer of 2002.

Return to Work

The Ticket to Work and Work Incentives Improvement Act of 1999 provided a number of new programs and initiatives for disabled beneficiaries. Return to Work is part of the President's New Freedom Initiative--and a priority for the Administration.

In early 2002, we expect to begin a three-year national rollout, a few States at a time, of the "Ticket to Work and Self-Sufficiency" program (Ticket program). Return-to-work service providers, called Employment Networks, will give beneficiaries greater access to rehabilitation and employment services. Employment Networks will be paid only if the beneficiary leaves the disability rolls due to work or meets certain work-based milestone criteria specified in regulations. The law also makes it easier for beneficiaries who leave the disability rolls because they return to work to receive benefits again if they become unable to



continue working because of their medical condition. They will have five years to request reinstatement without having to file a new application.

A program of cooperative agreements in each State and territory, called the Benefits Planning Assistance and Outreach program, helps beneficiaries understand SSA's work incentives, become aware of any benefits of other programs for which they may be eligible, and gain employment. SSA has funded cooperative agreements with 117 organizations, providing complete coverage across the United States. The law also provides for payments to State Protection and Advocacy systems for the purpose of providing services, including information and advice about obtaining vocational rehabilitation and employment services, and advocacy that a disabled beneficiary may need to secure or regain gainful employment.

Another provision of the law enables Social Security Disability Insurance beneficiaries who return to work to be eligible for expanded Medicare coverage. The provision extends Part A premium-free coverage from 39 months to 93 months after the end of the trial work period for most SSA disability beneficiaries who work as long as the individual still has a disabling impairment. Without this provision, disability beneficiaries might otherwise have to decide between working or keeping the health care coverage they need. The law also provides States the option of expanding Medicaid coverage for working disabled or blind SSI beneficiaries; SSA and the Centers for Medicare and Medicaid Services are encouraging States to adopt these expansions in medical care.

As mandated in the legislation, SSA has created a new field office position, called the Employment Support Representative (ESR), to provide front-line work incentives consultation to beneficiaries and others in the disability community. A pilot of the position was conducted in FY 2001. Information from the pilot will be used to guide the rollout of the ESR position.

Another pilot project explores a unique continuing disability review process for youth aged 16-25 that will assist SSA in evaluating their work potential. This initiative is part of a developing Youth Employment Strategy (YES) which will be a major inter-agency effort to make the school-to-work transition more effective for youth and young adults. A significant part of YES will establish a youth research initiative to test improvements in the delivery of services and in the efficacy of alternative service payment systems. As a first part of that research, in 2000, SSA awarded a cooperative agreement to perform a three-year test of a hospital-based program for youth in transition in Washington, D.C.

Finally, SSA is developing two demonstration projects that are required by the Ticket legislation. The \$1-for-\$2 Benefit Offset demonstration project is intended to provide beneficiaries with the support necessary to return to work and achieve financial independence. This demonstration will remove the "cliff" effect that cuts off cash benefits to beneficiaries who work and, after completion of a trial work period, earn above the substantial gainful activity level. The benefit offset will gradually reduce benefits by \$1 for every \$2 earned above a specified level to make it easier for beneficiaries to reenter the workforce. The second project, the Early Intervention demonstration, will provide return-to-work services before awarding benefits to applicants with impairments that reasonably may be presumed disabling. The intent of this project is to avert long-term benefit receipt in those instances where it appears rehabilitation may produce a better outcome.

In addition to initiatives generated by the Ticket legislation, SSA is conducting the National Study of Health and Activity (NSHA), a national survey intended to provide critical data on the prevalence of disability among people of working age. Its major goals are to provide information on the number and characteristics of people potentially eligible for Social Security DI on the basis of their impairment, the factors that enable people with disabilities to remain in the workforce, the number of people who would be induced to apply for DI benefits under a \$1-for-\$2 benefit offset and the effect of increasing the age for full or reduced retirement benefits on the DI program. The results of the pilot study are being analyzed, and further refinement and testing will be concluded early in 2002. If the tests are successful, the main study will be initiated later that year.

Commitment to World-Class Service



The American public has come to expect continually improved service from SSA and other Federal agencies. To meet that expectation, SSA is committed to continuing to provide responsive, world-class service to the public. We have many initiatives under way that will improve service to the public. But we recognize that changes in people's preferences, emerging technologies and other factors will result in modifications to the way we deliver service in the future.

To support our service commitments and to keep pace with rapidly changing technology, SSA has taken steps to significantly upgrade and refresh our systems infrastructure. Employee desktop computers are being

replaced every three years. We're also upgrading our computer network, telecommunications and security infrastructure. Taken together, these enhancements will allow us to better serve the public whether they choose to contact us in person, over the phone or via the Internet.

The following discussions are just some of the examples of the initiatives under way to improve our service to the public.

SSA's Service Vision

As the baby boom generation approaches retirement over the next few years, SSA faces dramatic increases in workloads and significant losses within an expert workforce looking to retirement. At the same time, people in all age groups are relying upon and demanding the convenience of world-class electronically-based service. The challenge is daunting.

We created a long-range vision of service to guide how we will manage our work and provide service a decade from now. Our *Service Vision* includes key features such as efficient, one-stop shopping, and reduced burden and cost for our partners in business and government to share information and to coordinate service delivery. It envisions substantial increases in efficiency through e-Government. We are currently working to develop the detailed plans and the cross-cutting human capital and e-Government strategies that will serve as the roadmap for achieving the service vision of the future.

This long-term service vision and the related performance objectives and strategies in the Agency Strategic Plan will drive our near-term initiatives toward long-term goals.

Electronic Service Delivery

SSA's website, *Social Security Online*, provides the American public with one-stop shopping for information and services regarding the Social Security programs. Using state-of-the-art tools, SSA seeks to improve the interaction between our organization and the public, regardless of where and how that interface takes place. We are committed to continuing our legacy of providing personalized service by ensuring that our electronic service delivery channels are as satisfying to each individual as our traditional methods. Electronic Service Delivery is one of the governmentwide management and performance initiatives in the President's Management Plan.

Social Security Online began by providing electronic access to information products. We then added over 65 SSA forms and 4 Internal Revenue Service forms available for downloading. The emphasis now is on the availability of transactional services on the website.



FY 2001 has been very active for *Social Security Online*; six applications have been added or enhanced. The *Benefit Eligibility Screening Tool* helps individuals determine eligibility for benefits. The *Internet Social Security Benefit Application (ISBA)* is an evolution of the retirement claim (IRIB) implemented last year and now enables a spouse to file. *Password Services* allows ISBA filers, and selected others, to obtain a password to access the new post-entitlement applications: *Check Your Social Security Benefit* to view current account information; *Internet Change of Address* which also permits phone number changes; and *Start or Change Direct Deposit*.

As we continue to add new services, there are many challenges to overcome. These include training of our workforce, integration of varying authentication mechanisms, and enhancing our partnerships with other government organizations. Privacy and security are still significant considerations as we add more transactional services to the website. We continue to consult with privacy/security experts on our plans for new applications. In addition, the Agency has established a methodology for research and development efforts, to test the potential impact of new electronic services technologies in the SSA environment.

We are focusing on better ways to collect feedback, gain more insight into user concerns and address usability issues. We are working on a comprehensive redesign of *Social Security Online* to provide easier access to information and online services. To fully support our electronic services, SSA recognizes the need to build a robust software development environment and hardware infrastructure.

Building the Internet Service Delivery Mechanisms

This year SSA will begin to rapidly increase the number of its services delivered directly to the American people. The Internet will be the primary method for delivering those services. Although SSA already has a significant number of Internet-based services available, the planned increase in both the quantity of those services and their use will need to be supported by up-to-date software development practices and by a technical infrastructure appropriate for a large-scale operation.



SSA's strategy centers on building Internet services that link to its existing business processes and core systems. This will allow SSA to address the new technical and organizational challenges on a priority basis as their character and magnitude become known while still satisfying current system needs in the more traditional manner.

These plans will require significant information technology funding for a step-by-step upgrade of networks, computing capacity, software, application development tools, staff training and experienced contractor support. This solution will provide the Agency with a reliable infrastructure and the ability to keep pace with the rapid changes in this area of technology.

Electronic Payment Services

SSA is the leader in electronic payment delivery throughout the Federal Government. Currently, 75 percent of benefit payments are made electronically. SSA programs have experienced considerable growth in electronic payment delivery in recent years. Specifically, in December 1995, 60 percent of all OASDI and 26 percent of SSI benefit payments were made by direct deposit. As of June 2001, the OASDI participation rate had risen to 79 percent and the SSI participation rate to 50 percent.

To achieve this success, SSA has aggressively pursued its direct deposit strategy to convey to beneficiaries the advantages of using direct deposit; i.e., direct deposit is safe, convenient and reliable. In FY 2001, SSA implemented a pilot to allow beneficiaries to enroll in direct deposit over the Internet.



Direct Deposit Public Information Material

SSA was the first Federal agency to make cross-border payments with the start of its International Direct Deposit (IDD) service in 1987. Since 1987, SSA has expanded its IDD services to 37 countries providing fast and economical electronic payment delivery to over 134,000 beneficiaries living in foreign countries.

SSA has partnered with the Department of the Treasury to implement an Electronic Transfer Account (ETA) program for beneficiaries who do not have an account at a Federally insured financial institution or who cannot obtain one. The ETA program will ensure recipients an account at a reasonable cost and with consumer protections comparable to other accounts at the financial institution. The ETA program, which became operational in 1999, continues to expand its number of participating financial institutions, and now has over 10,000 providers nationwide.

Market Measurement Program

SSA's ability to deliver quality service is based in part in knowing the public's expectations. Through our Market Measurement Program (MMP), we routinely collect information from the public as well as SSA's workforce and other interested parties through regularly scheduled satisfaction surveys and detailed studies. This information helps us decide where to best focus our limited resources and make improvements in areas that will have the greatest positive impact on satisfaction.

Feedback obtained through the MMP has guided us to:

- Focus significant resources to improve 800-number telephone service since we know that:
(1) The public is showing an increasing preference for dealing with SSA by telephone, and
(2) overall satisfaction with SSA is significantly influenced by how quickly the public gets through to us by telephone;
- Respond to individuals who told us they would be more satisfied if they could complete business in one contact by implementing a new immediate claims taking capability for people who call our 800-number and want to file certain claims; and
- Undertake efforts to improve our notices since notice clarity is continually identified as one of the most important aspects of public service.

Using MMP data, we continue to identify and address such service problems and issues. We are looking at ways to expedite the data collection process, to conduct more special studies, and to broaden our focus to include more employee and other interested party issues. The employee focus is particularly important because research has shown a direct link between high employee engagement and employee retention, productivity and public satisfaction.

Human Resource Challenges

Human Capital Management

Human Capital Management is a governmentwide initiative in the President's Management Plan, and the General Accounting Office (GAO) has also designated Human Capital Management as a high-risk area governmentwide. SSA established a multi-faceted response to this challenge as a result of our analysis of our own public and employee base. Our Agency faces explosive workload growth as the baby boom generation ages and becomes more prone to disabilities. At the same time, we face our own internal "retirement wave," with the projected loss of more than 38,000 SSA employees to retirement and other attrition over the next decade.



We have identified the occupations in SSA that will experience the most serious losses as employees retire in increasing numbers. To fill the gaps, we have implemented various career development programs to advance the skills of employees and prepare them for leadership and other key positions. In addition, we have established a Future Workforce Transition Plan, a 5-year plan for transitioning from the workforce we have today to the workforce we will need in the future. The plan contains a wide range of actions we are implementing in order to meet our future needs.

Our human capital strategies include a number of initiatives to broaden the capabilities of our current employees, improve employee retention and effectively replace those employees that do leave. We are implementing recruitment strategies that will help us attract top-quality applicants, lead them to a decision to join the SSA workforce and create "brand loyalty" for SSA as an employer.

Retirement Wave Update

Our original “Wave” study was released in October 1998. The purpose was to develop a methodology and report on retirement attrition projections for a mature workforce. In order to do that, we tracked actual retirements from past retirement eligible pools to establish historical retirement patterns. We then applied the historical retirement pattern to current eligible workers, and also prospectively to future eligible employees.

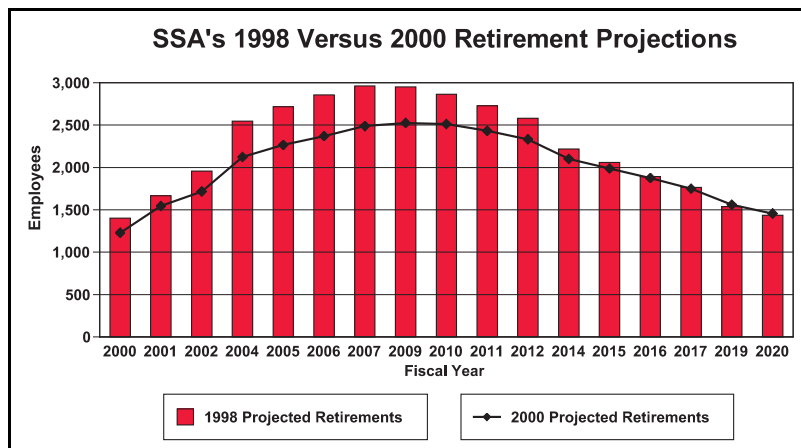
What we found in our 1998 study was a retirement wave that peaked between 2006 and 2010, with about 2,900 estimated annual retirements between 2000 and 2010.

The Agency responded by:

- Replacing early out and regular attrition losses by hiring direct service employees;
- Redeploying staff employees to direct service positions;
- Implementing three national and numerous regional and component-level developmental programs that included over 1,200 employees; and
- Developing the Human Resource Transition Plan for the Workforce of the Future.

Our latest study used current workforce statistics to improve our analysis, added disability retirements and refreshed our projections. We are working to improve our early out projections and exploring a model to project total attrition.

Early out retirements 1998 through 2000 have impacted the original projections. The effect of employees taking early out retirement is the flattening of the “Wave’s” peak compared to our 1998 projections. Early outs have allowed us to hire new employees and have them benefit from knowledge transfer from veteran employees still on the job.



Our current projections now show different retirement patterns. Examples are:

- While the “Wave’s” peak remains essentially the same, 2007 through 2010, there are about 400 to 500 fewer employees projected to retire each year during the peak period;
- About 23,000 employees or 37 percent of our current workforce of about 62,000 employees will take regular or disability retirement between now and 2010.

Training and Career Development



We have begun a number of initiatives designed to address this challenge from several perspectives. In response to the anticipated significant loss of knowledge and experience in the Agency's managerial ranks, we have revitalized and expanded our career development programs and management training. We are implementing learning strategies that will harness new technologies to better ensure we get the right training to the right person, at the right time. For example, we are extensively utilizing distance learning systems that employ live instruction and/or web-based delivery to train both new and seasoned employees in their offices or at their workstations.

Another integral part of this effort involves being able to better identify skills gaps, determine the best way to close those gaps and develop new learning initiatives that will improve performance. We are addressing this need by developing a Learning Management System that will enhance employee awareness of training needs and opportunities, improve access to training and pay particular attention to training accessibility for employees with disabilities. One part of this strategy is the creation of our new Online University, which is designed to foster a culture of continuous learning by allowing employees access to Agency-sponsored training at home or other external sites.

As can be seen, creation of the proper learning environment for our employees in which they can be highly skilled and performing is an ever-evolving process to which we are fully and actively committed.

Stewardship

SSI Management Improvement

The SSI program provides benefits to approximately 6.6 million needy beneficiaries who are aged, blind or disabled. Like other means-tested programs that respond to changing circumstances of individuals' lives, the SSI program presents challenges to ensure that it is administered efficiently, accurately and fairly. "Sustain Management and Oversight of Long-Standing, High-Risk SSI Issues" is designated a major management challenge by GAO.

In October 1998, SSA issued the first management report on the SSI program, detailing the Agency's aggressive plans to improve payment accuracy, increase continuing disability reviews (CDR), combat fraud and collect overpayments. Two initiatives key to improvement have been executed--new computer matches and processing more redeterminations.

Since October 1998, SSA has conducted computer matches with wage and unemployment compensation data and with nursing home admission data. Both are considerably more complete and timely than the matches they replaced. From 1997 to 2001, there has been a significant improvement in the efficiency of these matches. Wage errors detected through our quarterly match quadrupled, from about 100,000 to about 400,000. The monthly nursing home match increased detection of nursing home admissions detected per year from 2,700 to 75,000.

SSA has had similar success in matches with correctional facilities. In FY 2001, these matches resulted in the suspension of benefits to 61,545 prisoners ineligible for SSI benefits while in a correctional institution. The sharing of this prisoner information with other Federal benefit paying agencies significantly improves fraud prevention and detection capability governmentwide.

In addition to computer matches, SSA is pursuing real time access to a variety of databases. This access will enable SSA field offices to detect inconsistencies and changes in income and resource allegations, significantly improving SSA's ability to prevent payment errors and enhance its ability to detect those errors that do occur.



While computer matches have and continue to provide extraordinary opportunities for improved management of benefit payments, the redetermination of eligibility for benefits and the CDR processes remain two of the most powerful tools available to SSA for improving the accuracy of SSI and DI payments.

Initiatives are underway to increase the effectiveness of these processes. In FY 2002, SSA will test a new redetermination form that could lead to improved selection criteria. Statistical modeling and other types of analysis are being pursued to improve selection methodologies for CDRs and ensure SSA can remain current with CDR processing.

Zero Tolerance for Fraud



One of our strategic goals is “to ensure the integrity of Social Security programs, with zero tolerance for fraud and abuse.” To achieve this goal, SSA initiated an aggressive anti-fraud program to: 1) Eliminate wasteful practices that erode public confidence in the Social Security system; 2) vigorously prosecute individuals or groups who damage the integrity of the programs; and 3) change programs, systems and operations to reduce instances of fraud.

SSA's National Anti-Fraud Committee, under the leadership of top SSA executives, continues to oversee the implementation and coordination of SSA's strategies to eliminate fraud. Regional Anti-Fraud Committees coordinate anti-fraud strategies at each of our regional offices and identify new projects at the local level. Best practices are shared among the regional committees and with the national committee.

Recent Progress In Combating Fraud

We have major initiatives under way to address fraud, waste and abuse. By moving forward with these agencywide initiatives, we will provide our employees with additional tools and demonstrate our commitment to the integrity of our programs.

Social Security Number Fraud

Essential to SSA's ultimate goal of preventing fraud is ending the Agency's dependence on documents that can be easily counterfeited or misused in an attempt to acquire a Social Security number (SSN). SSA has identified three basic types of fraud related to the SSN: when someone illegally obtains a number or uses someone else's number; when someone uses fraudulent documents to establish an entirely new identity; and when someone assumes another person's identity (identity theft).

Current initiatives aimed at eliminating these opportunities for fraud include:

- The formation in late September 2001 of an Emergency Enumeration Response Team. The group's initial focus has been on developing recommendations for near-term changes to strengthen the integrity of the process. We expect to implement the changes within 3 months.
- One of the changes is the elimination of driver's licenses as a reason for issuance of a non-work SSN.

- Another change will lower the age tolerance from age 18 to age 12 for the use of mandatory interview procedures in field offices. All applicants for original SSNs over the age of 12 will require a face-to-face interview with an SSA Claims Representative, and the birth record presented as evidence of age will be verified with the custodian of records before issuance of an SSN.
- SSA is also taking the lead in establishing an interagency taskforce with the Immigration and Naturalization Service (INS) and the Department of State (DOS) to focus specifically on issues involving the enumeration of non-citizens. The taskforce will discuss the possibility of accelerating an Enumeration at Entry process that will have INS and DOS collecting SSN data for non-citizens as part of the immigration process.
- We are also making continuing changes to the Modernized Enumeration System to help prevent fraud. For example, software changes planned for 2002-2003 will interrupt issuance of an SSN card where abnormal circumstances exist.

Representative Payees

SSA has a Key Initiative plan in place to address "Critical Projects to Improve the Representative Payment Program." This plan includes projects to improve the representative payment program through a better informed public, a more reliable payee investigation and selection process and a more meaningful payee monitoring program.

Prisoners

With the support of Federal, State and local entities, SSA has made significant progress in ensuring that incarcerations are reported timely and accurately and that benefits are suspended accordingly. Over the past few years, SSA has more than 3,110 reporting agreements in place representing 5,983 facilities, including local correctional and mental facilities, the Federal Bureau of Prisons and all State prisons. These agreements cover 99 percent of the inmate population in the United States and have resulted in hundreds of millions of program savings over the last few years.

Fugitive Felons

As a result of the Personal Responsibility and Work Opportunity Reconciliation Act of 1996, fugitive felons and parole or probation violators are not eligible for SSI payments for any month during which they are fleeing to avoid prosecution, or custody or confinement after conviction, or are violating a condition of parole or probation. SSA and the Office of the Inspector General (OIG) are actively pursuing matching agreements to facilitate electronic matching of warrant information with Federal, State and local law enforcement agencies to identify these individuals. We currently have matching agreements with the Federal Bureau of Investigation (FBI), the FBI's National Crime Information Center, the U.S. Marshal's Service, several State agencies and metropolitan police departments, in addition to local fugitive felon programs in each State.

Cooperative Disability Investigations Units

The purpose of the Cooperative Disability Investigations (CDI) program is to develop evidence of material fact sufficient to resolve allegations of fraud or similar fault in the disability program. A typical CDI unit consists of an OIG Special Agent, SSA employees and/or state DDS employees, State or local law enforcement agency personnel and an administrative assistant. The first CDI units began operation in 1998. There are currently 13 units and depending on the availability of funds, 20 CDI units should be in place by the end of FY 2003.

Administrative Sanctions

We successfully implemented the administrative sanction provisions of the Foster Care Independence Act of 1999 nationwide. These provisions allow SSA to impose periods of nonpayment of benefits under OASDI and ineligibility for cash benefits under SSI on individuals who knowingly furnish inaccurate or incomplete information for claims for OASDI and SSI benefits.

Critical Infrastructure Protection

Background

The SSA Critical Infrastructure Protection program resulted from the issuance of Presidential Decision Directives (PDD) 62, 63 and 67 which were to prepare the United States for new physical and cyber threats to our national infrastructure. Physical threats have always existed, however, the rapid growth and massive interconnectivity of the Internet around the world linked with our growing dependency on E-Systems have led to a new cyber threat.



On October 16, 2001, the President signed an executive order establishing the “President’s Critical Infrastructure Protection Board.” The protection program authorized by this order consists of continuous efforts to secure information systems for critical infrastructure. SSA’s Critical Infrastructure Protection program will fully comply with the executive order and will ensure that SSA maintains adequate levels of security for information systems, including emergency preparedness communications systems, for programs under its control.

PDD-63 calls for a national level effort to assure the security of increasingly vulnerable and interconnected infrastructures of the United States, and provides for a protection plan for national assets from both physical and cyber attack. The national initiative is supported by the Critical Infrastructure Assurance Office, and the SSA effort is supported by our agencywide Critical Infrastructure Protection (CIP) Workgroup.

SSA has constructed a CIP Plan, which created a comprehensive program Agency approach, addressing physical security, continuity of operations and information systems security. SSA was the first agency to perform a complete “Project Matrix” analysis of all Agency assets and generate a full list of assets in order of criticality.

All assets identified as critical are being subjected to a vulnerability assessment to identify vulnerabilities, threats which could exploit these vulnerabilities, estimates of the likelihood and documentation of the expected risk. Efforts to remedy any weaknesses identified are under way.

A large proportion of all initiatives were cyber-security initiatives. Many of SSA’s systems were reviewed and/or subjected to penetration testing to strengthen and improve information systems security--both at SSA and at State DDSs. The Continuity of Operations plan required by PDD-67 is a major component of the SSA CIP Plan. It establishes a plan to enable the Agency to continue essential functions during an emergency.

Financial Accounting System Replacement



SSA plans to acquire software and support services to replace its existing Financial ACcounTing System (FACTS). Mandates to reinvent Government, to improve the quality of Government services and the need to replace aging systems have impacted the operation of FACTS.

SSA has assembled a comprehensive set of governmentwide and Agency-specific functional and technical requirements that the replacement system must meet upon implementation as the Agency system of record. These requirements were used as commercial off-the-shelf software system evaluation criteria in a market survey begun on March 20, 2000 to identify the Joint Financial Management Improvement Program certified financial systems which could best meet SSA's needs. Of the systems offered by the vendor community at that time, a smaller subset was judged capable of meeting SSA's requirements. SSA is currently in the process of selecting the replacement software and is seeking a best value solution.

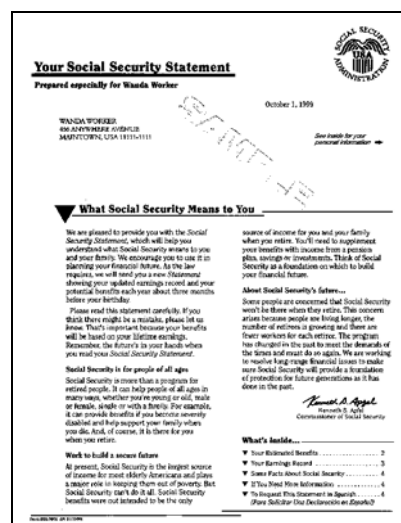
The projected implementation date for the replacement system is October, 2003. The proposed financial system will provide substantial benefits, including:

- Improving Business Processes through adoption of commercial [best] practices, cost efficiencies from integration, workflow, self service and e-business;
- Reducing labor cost for data transfers, data entry/update, report generation, and data verification and control, increasing decentralization of data input and enhancing field access to reports and on-line information; and
- Improving service to internal and external users, such as use of the web for doing business with SSA, reducing administrative and cost burden on business partners and ensuring continued support for the Agency accounting system of record.

Public Understanding

Over the coming decade, SSA will face significant challenges in its efforts to strengthen public understanding of Social Security programs. Through our communication activities, we will continue to educate the public about basic Social Security facts, the value of the programs, and how the programs are financed. Our objective is that, by 2005, 90 percent of all Americans will be considered knowledgeable about Social Security.

Our public education campaign is aggressive and proactive. Our strategic communications for FY 2001 includes six major strategies: (1) To establish SSA as preferred and most reliable source for information about Social Security; (2) to continue use of the *Social Security Statement* as centerpiece for mainstream communications; (3) to engage the community in helping us reach diverse populations; (4) to tailor communications tools and tactics to audience; (5) to effectively use both traditional and emerging technologies to reach the broadest spectrum of the public; and (6) to strengthen internal communications.



To meet our objectives, we will need to respond to communications issues arising from fundamental changes in our society and technology. These include:

- Providing the public useful information related to the future of Social Security. The public must be able to look to SSA for factual information about the program and its financing principles if citizens are to actively participate in national discussions about the future of Social Security. In the words of the Social Security Advisory Board, “SSA has a responsibility to communicate in an authoritative, credible, accurate and accessible manner with two important groups: first, the nearly 147 million workers who pay the taxes needed to finance the Social Security system; and second, the 44 million individuals who are currently receiving Social Security benefits.”
- Increased racial/ethnic diversity of the American population. The Census Bureau estimates that, by 2050, more than one-third of the population will be post-1970 immigrants and their descendants, and the vast majority of these immigrants will be from Latin America and Asian nations. As American society becomes increasingly multi-cultural, SSA will need to engage in more minority outreach, particularly with non-English media, and use innovative methods to get the right message to the right audience in a way that can be understood and used.
- Intensified concerns about retirement among the “baby-boom” generation. Today, the more than 80 million members of the “baby-boom” generation are beginning to think about retirement. SSA anticipates that these individuals will increase their demands for financial planning information, including information about the income-replacement value of Social Security benefits and cost-of-living adjustments. Broad public concern about financial security in retirement and in other life stages presents an opportunity for SSA to work with other government agencies and the private sector, including bank and investment firms and the life insurance industry, to develop cooperative education/information vehicles to assist financial planning.
- Increased technological change. The communications revolution has not only changed the way we distribute information, it has changed the way we do business. SSA must continue to develop new ways to serve the public through technology, including expanded use of the Internet to give, exchange and use information to do more of the Agency’s work. SSA must effectively communicate through the Internet and market our Internet services in ways that will make full use of its public-service potential.

Educating the public is important, because we must help the public understand, in a personal way, how Social Security fits within an individual’s financial planning for the future. We must help individuals know what benefits Social Security provides--and does not provide--and help them know when and how they can apply for those benefits.

Other Management Challenges

The Reports Consolidation Act of 2000 requires that, annually, the Inspector General (IG) prepare a statement that summarizes what he considers to be the most serious management and performance challenges facing the Agency and his assessment of the Agency's progress in addressing those challenges. SSA then reviews that list of “major management challenges” and works with the IG to address our mutual concerns. All topics on the IG's list are discussed in this Major Issues Facing SSA section of the MD&A except for the Earnings Suspense File which is discussed in the Programmatic Information section of this report on page 205. In addition, the General Accounting Office has identified similar major management challenges which SSA addresses each year in the Annual Performance Plan. The complete list of the IG’s Major Management Challenges may be found in this report following the auditor’s report on the FY 2001 financial statements.