Office of the
Inspector General

October 26, 2011

MEMORANDUM FOR JOHN BERRY
                Director

FROM: PATRICK E. McFARLAND
                 Inspector General

SUBJECT: Fiscal Year 2011 Top Management Challenges

The Reports Consolidation Act of 2000 requires the Inspector General to identify and report annually the top management challenges facing the agency. We have divided the challenges into two key types of issues facing the U.S. Office of Personnel Management (OPM) – environmental challenges, which result mainly from factors external to OPM and may be long-term or even permanent; and internal challenges, which OPM has more control over and once fully implemented will likely be removed as a management challenge.

The three listed environmental challenges facing OPM are due to such things as increased globalization, rapid technological advances, shifting demographics, national security threats, and various quality of life considerations that are prompting fundamental changes in the way the Federal Government operates. Some of these challenges involve core functions of OPM that are affected by constantly changing ways of doing business or new ideas, while in other cases they are global challenges every agency has to deal with.

The six internal challenges included in this letter represent OPM's development of new information systems, the need to strengthen controls over its information security governance, overhauling the retirement claims process, stopping the flow of improper payments, improving controls over interagency agreements within Human Resources Solutions, and the internal controls over financial management reporting for the Revolving Fund and Salaries and Expenses Accounts.

Inclusion as a top challenge does not mean we consider these items to be material weaknesses. In fact, the areas of Background Investigations (as part of the Revolving Fund material weakness reported in the Office of the Inspector General's Federal Managers' Financial Integrity Act Management Assurance letter) and Information Security Governance remain the only challenges related to the reported material weaknesses.

The remaining challenges are issues which demand significant attention, effort, and skill from OPM in order to be successfully addressed. However, there is always the

possibility that they could become material weaknesses and have a negative impact on OPM's performance if they are not handled appropriately by OPM management. We have categorized the items included on our list this year as follows:

Environmental Challenges

- Strategic Human Capital;

- Federal Health Insurance Initiatives; and,

- Background Investigations.

Internal Challenges

- Information System Development;

- Information Security Governance;

- Financial Management System and Internal Controls: Revolving Fund and Salaries and Expenses Accounts;

- Improving Internal Controls over OPM's Human Resources Solutions Vendor Management Branch Operations;

- Stopping the Flow of Improper Payments; and,

- Overhaul of Retirement Claims Processing.

We have identified these issues as top challenges because they meet one or more of the following criteria:

1) The issue involves an operation that is critical to an OPM core mission;
2) There is a significant risk of fraud, waste, or abuse of OPM or other Government assets;
3) The issue involves significant strategic alliances with other agencies, the Office of Management and Budget, the Administration, Congress, or the public;
4) The issue is related to the President's Initiatives; or,
5) The issue involves a legal or regulatory requirement not being met.

The attachment to this memorandum includes written summaries of each of the challenges that we have noted on our list. These summaries recognize OPM management's efforts to resolve each challenge. This information was obtained through our analysis and updates from senior agency managers so that the most current, complete and accurate characterization of the challenges is presented. I would also like to point out that we have removed the challenge shown below that was on this list last year:

- Radiology and Imaging as a specific Federal Employees Health Benefits Program (FEHBP) challenge has been removed from the list based on OPM's efforts to reduce the impact of this challenge through annual contract negotiations with the FEHBP carriers that encourage management of radiology and imaging benefits. This awareness has resulted in the increased use of pre-authorizations, which ensure medical necessity, as well as an opportunity to provide alternative diagnostic choices.

This year, we have added a discussion under Federal Health Insurance Initiatives concerning OPM's challenges in offering healthcare to the Indian and Tribal communities. New challenges added this year include Human Resources Solutions Vendor Management Branch operations, Stopping the Flow of Improper Payments, and Overhauling Retirement Claims Processing.

I believe that the support of the agency's management is critical to meeting these challenges and will result in a better government for the American people. I want to assure you that my staff is committed to providing any audit or investigative support needed and that they strive to maintain an excellent working relationship with your managers.

If there are any questions, please feel free to call me, at 606-1200, or someone from your staff can contact Michael R. Esser, Assistant Inspector General for Audits, or Michelle B. Schmitz, Assistant Inspector General for Investigations, at 606-1200.

Attachment

FISCAL YEAR 2011 TOP MANAGEMENT CHALLENGES
U.S. OFFICE OF PERSONNEL MANAGEMENT

ENVIRONMENTAL CHALLENGES

The following challenges are issues that will in all likelihood permanently be on our list of top challenges for the U.S. Office of Personnel Management (OPM) because of their dynamic, ever-evolving nature, and because they are mission-critical programs.

1. STRATEGIC HUMAN CAPITAL

In May 2010, President Obama issued a Memorandum, *Improving the Federal Recruitment and Hiring Process*, beginning the Administration's comprehensive government-wide initiative to address major, long-standing impediments to recruiting and hiring the best and the brightest into the Federal civilian workforce. We are pleased to say that OPM has made substantial progress in addressing its human capital challenges, including:

- Working with agencies by holding training sessions to ensure that best practices are developed and used throughout government;
- Working with agencies and the Chief Human Capital Officers Council to identify skill gaps in mission-critical occupations, conduct workforce planning, and implement strategies to close gaps;
- Creating a diversified workforce with various experiences, perspectives, and backgrounds by hiring more Americans with disabilities, hiring more Veterans, and promoting diversity and inclusion;
- Reducing the hiring time by 15 percent to 105 days;
- Issuing proposed regulations to help recruit and hire students and recent graduates under the *Pathways Program*;
- Creating shared registers for entry-level Information Technology Specialists and Budget Analyst positions;
- Improving communications with applicants throughout the hiring process;
- Releasing USAJOBS 3.0 in October 2011 to provide enhanced search capabilities and applicant tools, and a common repository for applicant resumes, as well as government-wide analytical reports for use by agencies, OPM, and the Office of Management and Budget (OMB); and,
- Launching USAJOBSRecruit to provide tools and guidance, and encourage development of best practices within the Federal recruiting community in a web-based platform.

Much progress has been made, but with the aging Federal workforce, OPM must help agencies to recruit and retain the right people with the skills needed to achieve their goals. OPM is charged with helping agencies to identify and close skills gaps, being responsive to changing applicant and worforce needs, and developing performance measures that will monitor organizational efficiency, effectiveness, and progress.

2. FEDERAL HEALTH INSURANCE INITIATIVES

OPM continues to face challenges it must address in order to ensure the Federal Employees Health Benefits Program (FEHBP) contracts with insurance carriers that offer comprehensive health care benefits at a fair price. However, with the passing of the Affordable Care Act (ACA), OPM's roles and responsibilities related to Federal health insurance have been expanded significantly. Under ACA, OPM has been designated as the agency responsible for implementing and overseeing the multi-state plan options which start in 2014, as well as expanding FEHBP coverage to certain Indian tribes, Tribal organizations, and urban Indian organizations. In addition, the Department of Health and Human Services reached out to OPM to administer the Pre-Existing Condition Insurance Plan (PCIP). The following highlights these challenges and current initiatives in place to address them.

A. Federal Employees Health Benefits Program

The ever-increasing cost of health care is a national challenge. For the upcoming year, the average FEHBP premium increase is 3.8 percent. This is a significant reduction from the calendar year (CY) 2011 increase of 7.3 percent. However, it is a continuing challenge for OPM to keep premium rate increases in check.

As the administrator of the FEHBP, OPM has responsibility for negotiating contracts with insurance carriers covering the benefits provided and premium rates charged to approximately eight million Federal employees, retirees, and their families. The FEHBP must utilize industry best practices and ensure quality healthcare for enrollees while controlling costs. This includes exploring creative ways to control costs and utilization of benefits, such as increased use of wellness initiatives and global purchasing of pharmacy benefits. These challenges may require legislative, regulatory, procurement and contracting, and administrative changes.

OPM believes that the following initiatives will help ensure that the FEHBP continues to offer enrollees quality health care services at fair and reasonable premium rates.

1. Program-wide Claims Analysis/Health Claims Data Warehouse

The challenge for OPM is that, while the FEHBP directly bears the cost of health services, it is in a difficult position to analyze those costs and actively manage the program to ensure the best value for both Federal employees and taxpayers. OPM has not routinely collected or analyzed program-wide claims data. The Health Claims Data Warehouse (HCDW) project is an initiative to collect, maintain, and analyze data on an ongoing basis. The data will be derived from health and prescription drug claims under the FEHBP. The HCDW will allow OPM to understand the drivers of cost increases and model the potential effects of health system reform or environmental changes on Federal employees. This warehouse will also strengthen OPM's ability to strategically shape future benefits design by

better positioning the agency to negotiate effectively with the FEHBP carriers to keep premium increases below industry-wide levels.

During FY 2011, OPM began the processes necessary to implement this searchable and secure database for claims information, which included the following:

- Hired additional project staff to build analytical capacity and the organizational infrastructure;
- Entered into a memorandum of understanding with the Office of the Inspector General (OIG) to assist OPM in developing and implementing the HCDW. The OIG will host it within our IT environment. This approach will save OPM significant setup time and costs, as well as ongoing operating costs;
- Implemented a risk management plan which establishes the processes and procedures for dealing with risks associated with the HCDW. It focuses on the processes and procedures the team will follow to identify, categorize, manage, document, track, and close risks throughout the project lifecycle;
- Developed the Systems of Records Notice that was approved by OMB and published in the Federal Register;
- Purchased the hardware and software necessary to establish the HCDW within the OIG's IT framework;
- Started using an interim HCDW environment which was established by the OIG. The interim environment will be used until the hardware and software associated with the actual data warehouse is configured and implemented; and,
- Continued to develop data use needs for the HCDW requirements document. A thorough completion of this step will ensure that the completed warehouse will have the capability to allow analysts to effectively analyze costs and provide adequate management support for the FEHBP.

It is important to note that developing and maintaining a health claims data warehouse of this magnitude presents its own complex challenges [including managing multiple data formats and feeds; large size; security; data validation and verification; flexibility (health care is a dynamic industry); etc.].

2. Prescription Drug Benefits and Costs

Increases in drug costs continue to be a major contributor to the rapid growth in health care costs, with drugs now accounting for about 30 percent of all FEHBP costs. Of continuing concern to our office are the pharmacy benefit managers (PBMs), who administer drug benefits for the FEHBP carriers. The FEHBP carriers, not OPM, negotiate the pricing of these pharmacy benefits. Consequently, the PBM contracts in effect for contract years 2010 and prior lack transparency, which limits our ability to audit and provide adequate oversight of this high cost benefit. This lack of transparency makes it impossible for OPM to ensure that FEHBP enrollees are receiving quality benefits at a fair price. However, all PBM contracts that become effective after contract year 2010 will be required to meet the

transparency standards outlined in FEHBP Carrier Letter #2010-04. Specifically, these standards require:

- Pass-through transparent pricing in carrier contracts with PBMs;
- PBM's profit under the contract must be tied to clearly identifiable sources;
- PBM's administrative fees must be clearly identified to retail claims, mail claims, and clinical programs, if applicable; and,
- Contracts and other documentation supporting charges to the carrier must be fully disclosed to and auditable by the carrier or its agent and the OIG.

To encourage cost savings, OPM's CY 2012 FEHBP benefit and rate call letter outlined an expectation for all carriers to expand their programs to provide benefits for appropriate substitutions for higher-cost drugs such as lower or no copayments for generic drugs and clinically appropriate therapeutic alternatives. Carriers were also encouraged to develop programs aimed at managing the cost and use of specialty drugs. Overall, OPM expected carriers to implement prescription drug programs to reduce their CY 2012 pharmacy spending by four percent without shifting costs to enrollees.

OPM is also requiring carriers to submit information on their current pharmacy costs and current drug benefits. This information will be used to compare pharmacy costs per enrollee, across plans, and for the program as a whole with the intent of ensuring the FEHBP remains competitive.

While these short-term measures should have a positive impact on the program, OPM, through its PBM working group, continues to assess potential long term initiatives to further reduce prescription drug costs, as well as strengthen the controls and oversight of the FEHBP pharmacy benefits. The importance of this effort was highlighted in "The President's Plan for Economic Growth and Deficit Reduction," dated September 2011. The President's plan calls for the streamlining of the FEHBP pharmacy benefit contracting. Under the Administration's proposal, OPM would contract directly for pharmacy benefit management services on behalf of all FEHBP enrollees and their dependents versus the current process where each carrier negotiates its own PBM contract. This change will allow the FEHBP to more efficiently leverage its purchasing power to obtain a better deal for enrollees and taxpayers. According to the President's plan, this proposal would save $1.6 billion over 10 years.

Since current legislation prohibits OPM from contracting directly with PBMs, OPM is pursuing statutory authority language changes, which will seek to amend the current FEHBP law to permit OPM to contract directly with PBMs. As an interim step, OPM is planning to issue a request for information (RFI) with the primary objective of identifying a preferred PBM vendor, which can demonstrate cost savings, price transparency, and a breadth of clinical management programs for the FEHBP. Once identified, the selected PBM vendor will be considered the pharmacy administration preferred arrangement for management and delivery of the

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FEHBP pharmacy benefits that should be utilized by the carriers. Should the carriers want to extend the contract with their PBM, they will be required to demonstrate a better overall value than that presented by the preferred PBM identified through this RFI. The best value will be determined by OPM and will include both quantitative and qualitative attributes.

An overarching component of this challenge is for OPM is to ensure that the changes do not adversely impact FEHBP enrollees' health and safety while realizing true program savings.

3. Tribal Healthcare – FEHBP Participation

The ACA also incorporated the *Indian Health Care Improvement Reauthorization and Extension Act of 2009*. This Act allows certain Indian tribes, Tribal organizations, and urban Indian organizations to purchase FEHBP coverage. This access to Federal insurance provides a new option for many tribes to purchase coverage for employees who might otherwise have difficulty accessing affordable insurance coverage in the private market.

Implementation of the ACA presents a unique set of challenges for OPM. From a policy perspective, OPM must determine the:

- Scope of coverage;
- Employer and employee contributions to premiums;
- Process by which the tribes will elect to participate in these programs;
- Process by which employees will elect coverage; and,
- Circumstances for termination of coverage.

Operationally, OPM must develop and implement:

- Technical requirements for enrollment, billing, and premium collection functions;
- Outreach program and communication plan for up to 600 individual tribal organizations; and,
- Educational materials informing potential enrollees of program benefits.

To date, OPM has established a policy and technical team to implement ACA's provision allowing tribes and tribal organizations to purchase FEHBP coverage for their employees. OPM is working with the Department of Health and Human Services (HHS), the Indian Health Service (IHS), and the Bureau of Indian Affairs (BIA) to understand the needs of Tribal communities to assure effective implementation. These efforts include several letters to tribal leaders to gather information on their interest in participating in the FEHBP and to provide them with a high level understanding of OPM's implementation plan. For example, OPM is coordinating regional consultation sessions, which will allow OPM staff members to consult with Tribal representatives about issues related to the process through

which Tribal employees will be able to access FEHBP coverage. OPM staff members have also attended several tribal meetings to initiate the consultation process. To supplement this process, OPM has created a webpage that allows for real time updates and information regarding the implementation of this ACA provision.

It is evident that OPM is committed to offering Indian Tribes, Tribal organizations, and urban Indian organizations streamlined access to comprehensive healthcare coverage through the FEHBP. However, it is also clear that it will take a strong partnership between the Tribes, Tribal organizations, urban Indian organizations, HHS, IHS, BIA, and OPM for the implementation to be successful.

B. National Healthcare Operations

1. Multi-State Plan

Under ACA, OPM has been designated as the agency responsible for implementing and overseeing the multi-state plan options. In accordance with the ACA, at least two multi-state plans will be offered on each state health insurance exchange beginning in 2014. Multi-state plans (MSP) will be one of several health insurance options that small employers and uninsured individuals will be able to choose from. In total, state exchanges are expected to provide health insurance coverage for as many as 31 million Americans.

While implementing any new program represents a host of complex challenges, one of the greatest challenges will be securing sufficient resources for OPM's new national healthcare function, as well as the expanded FEHBP-eligible population. Currently, the ACA does not specifically fund OPM for its new healthcare responsibilities. In addition, ACA mandates that resources essential to the management of the FEHBP cannot be used to start up the new program.

OPM received limited FY 2011 and FY 2012 funding from HHS. With these funds, OPM established policy and operational teams to review program and policy issues related to implementing the MSP Program, as well as provided analytical support for the MSP Program.

However, full funding beyond FY 2012 is a significant challenge for the agency, as well as for the OIG, who is charged with program oversight responsibilities. Without appropriate resources, OPM will not be able to support these new activities.

2. Pre-Existing Condition Insurance Plan

As part of ACA, HHS was required to develop and implement PCIP within 120 days of enactment. This program makes health insurance available to those who have been denied coverage by private insurance companies because of a pre-

existing condition, have been uninsured for at least six months, and are U.S. citizens or are residing in the U.S. legally.

Because of OPM's experience in administering the FEHBP, HHS requested that OPM design and implement the PCIP as required by ACA. OPM administers the program through an inter-agency agreement with HHS. On January 1, 2011, OPM successfully introduced three additional plans from which PCIP participants can choose. These three plans include: Standard, Extended, and a plan that features a health savings account. Additionally, OPM conducted an open season for PCIP enrollees to choose a health plan. Also, OPM worked with the HHS Centers for Medicare & Medicaid Services to establish lower PCIP premiums in January 2011 and again in July 2011. Lastly, OPM facilitated outreach efforts to help increase PCIP enrollment.

While the implementation was successful, administering this newly created program represents an ongoing management challenge for OPM.

3. BACKGROUND INVESTIGATIONS

OPM's Federal Investigative Services (FIS), headquartered in Boyers, Pennsylvania, conducts background investigations on Federal applicants, employees, military members, and contractor personnel for suitability and security purposes. FIS conducts approximately 90 percent of all personnel background investigations for the Federal Government and processes approximately 2 million investigations per year. Agencies use the reports of investigations conducted by OPM to determine individuals' suitability for Federal civilian, military, and Federal contract employment, as well as their eligibility for access to national security classified information.

Twelve OPM and contractor background investigators and two contractor record searchers have been criminally convicted since 2007. The twelve background investigators were convicted of fabricating background investigation reports, to include reporting interviews that never occurred, recording answers to questions that were never asked, and documenting record checks that were never conducted. The two contract record searchers were convicted of documenting record checks that were never conducted.

In addition to the convictions of background investigators, in FY 2011 a Federal employee was convicted after an OIG investigation revealed that he made false statements to a FIS background investigator in order to obtain his job as a police officer. He was not eligible for the position due to a prior felony conviction. Not only did he lie about receiving various military awards, he also told the FIS background investigator that he was serving in Afghanistan and Iraq during the time period when he was actually incarcerated in a military prison.

As of the date of this memorandum, the OIG has approximately 32 open cases, at various stages of investigation, which involve FIS employees and/or FIS contractors. The OIG is monitoring an additional six cases currently under review by FIS Integrity Assurance.

FIS has an effective system of integrity assurance internal controls and works cooperatively with the OIG to bring offenders to justice. However, any fraud in background investigation reports is unacceptable from a national security perspective, so this issue requires continued close attention by OPM management and by the OIG. For the second year in a row, the OIG has identified a material weakness within its own office related to the funding limitations of the OIG to perform Revolving Fund oversight work, to include audits and investigations of FIS activities.

INTERNAL CHALLENGES

The following challenges relate to current program activities that are critical to OPM's core mission, and that while impacted to some extent by outside stakeholders, guidance, or requirements, they for the most part are OPM challenges that have minimal external influence. They are areas that once fully implemented and functioning will in all likelihood be removed as management challenges. While OPM's management has already expended a great deal of resources to meet these challenges, they will need to continue their current efforts until full success is achieved.

1. INFORMATION SYSTEM DEVELOPMENT

In two reports to Congress (GAO-06-184 and GAO-09-529), the Government Accountability Office (GAO) described significant shortcomings in OPM's ability to successfully manage large and complex information systems development projects. These shortcomings were primarily attributed to a lack of disciplined processes in several key areas, including investment management, requirements management, testing, project oversight, risk management, and information security.

In our FY 2010 Top Management Challenges memorandum, we cited three examples of system development projects that supported GAO's concerns in varying degrees: the Retirement System Modernization (RSM) Program, the Consolidated Business Information System (CBIS), and the Service Credit System. Throughout FY 2011, OPM officials have been working hard to correct known weaknesses in these three projects. OPM closed the RSM program management office and adopted a more agile, modular development approach to modernization efforts that have now gone on for 24 years. The CBIS project team focused on resolving issues that were identified during the initial operational period. It has established functional working groups and has placed a renewed emphasis on stakeholder management. The Office of the Chief Financial Officer has reported significant progress in resolving all user and system issues. This was accomplished through a dedicated effort by project management staff and end users. During the period, the Service Credit System implemented a more systematic project management approach, better change management and separation of duties, improved development, and a more rigorous testing process.

We recognize that at this point these projects are past the development stage. However, one of the consequences of system development issues is the increased costs of working through them after implementation. Identifying and resolving issues is less costly and

disruptive to users if done prior to implementation. The execution of a comprehensive and disciplined information development process will minimize post-implementation issues and their associated costs.

For the future, OPM should concentrate on lessons learned from these projects and ensure that disciplined processes in the functional system development areas are in place before embarking on new major system development projects. The inherent complexities of system development efforts will make this a continued management challenge for the agency.

2. INFORMATION SECURITY GOVERNANCE

OPM relies on IT to manage its core business operations and deliver products and services to many stakeholders. With increasing reliance on information systems, growing complexity, and constantly evolving risks and threats, information security has become a mission-critical function. Managing an information security program to reduce risk to agency operations is clearly an ongoing internal management challenge.

Information security governance is the overall framework and supporting management structure and processes that are the foundation of a successful information security program. Proper governance requires that agency management is proactively implementing cost-effective controls needed to protect the critical information systems that support the core mission, while managing the changing risk environment. This includes a variety of activities, challenges, and requirements, but is primarily focused on identifying key roles and responsibilities and managing information security policy development, oversight, and ongoing monitoring activities.

For several years, we have reported increasing concerns about the state of the agency's information security governance. In May 2009 we issued a Flash Audit Alert (FAA) to the OPM Director and the Chief Information Officer (CIO) highlighting these concerns. The primary issues outlined in the FAA included outdated information security policies and procedures and an understaffed IT security program, particularly the longstanding lack of a permanent senior agency information security official (SAISO).

The lack of policies and procedures was reported as a material weakness in the FY 2007 and FY 2008 FISMA audit reports. In FY 2009, we expanded the material weakness to include the agency's overall information security governance program and incorporated our concerns about the agency's information security management structure.

The root cause of these issues is poor information security governance, as described above, but also the Office of the Chief Information Officer's (OCIO's) perspective of its role in IT security at the agency. An IT security program can be structured with a centralized or decentralized model, although most agencies adopt a hybrid structure with characteristics of both approaches. OPM, however, has chosen to implement a highly decentralized structure with most of the responsibility for IT security in the program offices, with the OCIO responsible for policy development and oversight.

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While it is true that IT security should be a shared responsibility between the OCIO and the program offices, FISMA assigns ultimate responsibility to the CIO for developing and maintaining an effective IT security program. Our audits over an extended period of time have clearly shown that OPM's decentralized approach is not effective. Program offices, in general, do not have the expertise to properly manage an IT security program for their systems. Program offices will naturally focus limited resources on operational issues and IT security is normally a secondary concern.

In our FY 2010 FISMA report, we recommended that OPM adopt a more centralized approach to IT security. We suggested that the agency recruit a staff of information security professionals to act as designated security officers (DSO) that report to the SAISO. This model would replace the existing approach where current DSOs, most of whom have no background in IT security, report to their program offices.

In FY 2011, the OCIO made good progress in updating its IT security and privacy policies, procedures, and guidance, a permanent SAISO has been at work for over one year, and the IT security staff has been strengthened. However, the decentralized IT security structure is still in place. The OCIO directions for program office DSOs to conduct required annual security controls tests and contingency plan tests were simply ignored, and these critical elements of good IT security were not done for the majority of OPM systems. Clearly, the OCIO has limited authority over the DSO community.

Our understanding is that most program offices have rejected the proposal to consolidate DSOs under the OCIO, apparently for political and budgetary reasons. A compromise proposal to consolidate only DSOs for high-risk systems under the OCIO seemed to be acceptable, but gained no traction in FY 2011. We continue to recommend that the OPM Director provide adequate resources for the OCIO to develop a staff of professional DSOs to manage IT security for OPM systems.

3. **FINANCIAL MANAGEMENT SYSTEM AND INTERNAL CONTROLS: REVOLVING FUND AND SALARIES AND EXPENSES ACCOUNTS**

During the audit of OPM's FY 2011 financial statements, the auditors noted that deficiencies continue to exist in the operation of the Office of the Chief Financial Officer's (OCFO) internal controls over financial management and reporting, affecting the accuracy of the Revolving Fund (RF) and Salaries and Expenses (S&E) Accounts. These deficiencies are attributed to:

- OPM has not completely identified existing differences between its own internal data and the information reported by the U.S. Department of the Treasury (Treasury), resulting in an imbedded difference in its Fund Balance with Treasury (FBWT) amount; and,

- OPM has not effectively enforced procedures related to the consistent and clear documentation of the performance of Salaries & Expenses Fund reconciliations and as

outlined in the "Treasury Financial Manual" and OPM's "Cash Management Policy and Procedures."

OPM has had a long-standing issue with reconciling its RF account with Treasury. Revisions to the work instructions for reconciling the cash balances to the FBWT for the RF were made in FY 2009 to include strict deadlines for the completion of monthly reconciliations. With the implementation of CBIS, management still continues to have internal control weaknesses with FBWT reconciliations for the S&E and RF. OPM is challenged to continue to improve business processes within CBIS to address the current deficiencies.

4. IMPROVING INTERNAL CONTROLS OVER OPM'S HUMAN RESOURCES SOLUTIONS VENDOR MANAGEMENT BRANCH OPERATIONS

Developing and implementing strong internal control procedures over OPM's Human Resources Solutions (HRS) Intergovernmental fund, which provides services to other Federal agencies, has become a top management challenge during FY 2011. OPM's Vendor Management Branch (VMB) provides assisted acquisition services in addition to hands-on project management through the use of competitive fixed-price task orders. During FY 2011, it was determined that the VMB was operating under inaccurate guidance concerning the legally permissible periods for funds used in support of its interagency agreements (IAA). VMB operated under the assumption that agency funds received by OPM converted to no-year funding, despite a September 28, 2009 opinion from OPM's Office of General Counsel (OGC) to the then head of the VMB senior management team. The opinion, noted that "...funds advanced by a customer agency to OPM's RF do not become so called 'no-year money.'"

In response to the identified problem, the Director of OPM established a team of staff from HRS and the OCFO to analyze 809 open IAA/projects that were affected by VMB's inaccurate assumptions. A forensic accounting firm was also hired to assist in the analysis. OPM has expended a large amount of personnel and budgetary resources to address the problem within this RF activity. To further address the issues in HRS, the Director made several senior management changes. A new Associate Director and Deputy Associate Director were named to help strengthen the VMB's internal control procedures. During the third and fourth quarters of FY 2011, the new management team made a number of improvements within the VMB. All VMB staff has received appropriations law training, new policies and procedures have been developed for the IAA process, and VMB staff is receiving training on the new policies and procedures.

The challenge for the new management team will be to effectively implement the new internal control procedures while maintaining the high level of service that VMB has provided its customer agencies in the past.

5. STOPPING THE FLOW OF IMPROPER PAYMENTS

Over the last few years, the subject of improper payments by Federal agencies has received increasing attention from elected officials. The Administration and Congress have

determined that the amount of improper payments Government-wide is unacceptable. In FY 2010, OMB identified OPM's *Civil Service Retirement and Disability Fund* (CSRDF) as being susceptible to significant improper payments. The CSRDF paid out on average $120 million in improper payments annually in the last five years to deceased annuitants and survivors.

The Administration and Congress have recently taken steps to reduce wasteful spending and streamline Government processes, including the *Improper Payments Elimination and Recovery Act* (IPERA), signed into law by the President on July 22, 2010. IPERA is designed to cut waste, fraud, and abuse by Federal Government agencies due to improper payments. Agencies shall report on improper payments and progress in reducing them in their annual *Agency Financial Report* and *Performance and Accountability Report.* Agencies shall discuss the causes of the improper payments, actions planned or taken, and the results of the actions taken to address those causes.

A report on improper payments to deceased annuitants from the CSRDF was issued by our office on September 14, 2011. Through a working group of members from our office, OPM's Retirement Services, Retirement Policy, and the OCFO, progress has been made to identify ways to minimize improper payments. Through the working group, Retirement Services and the OCFO have implemented 10 of the 14 recommendations that improve internal controls and help reduce improper payments. However, four recommendations still need attention. They are:

- Tracking Undeliverable IRS Form 1099Rs;
- Establishing a Working Group to Improve Program Integrity;
- Capitalizing on Technology; and,
- Recovering Funds Escheated to the States.

Even though OMB has not placed the CSRDF in the high risk category (because its improper payments fall below 2.5 percent of the fund's total disbursements), OPM must pursue aggressive and effective strategies for the integrity of the CSRDF, especially for the sake of the taxpayer.

6. OVERHAUL OF RETIREMENT CLAIMS PROCESSING

The timely issuance of full annuity payments to annuitants has been a long-standing challenge for OPM. Processing the retirement claims of Federal employees is a mission-critical OPM program. With the closure of the RSM project, OPM is now challenged with overhauling the retirement claims process to better serve the Federal retirees, employees, and its customer agencies.

With a backlog of retirement cases pending adjudication and 125 days on average to process a retirement claim, OPM is clearly challenged with finding new ways to get annuitants their payment faster and with more accuracy. Currently OPM must issue annuitants an interim partial payment upon retiring, representing a portion of the estimated

final benefit. Only when OPM receives all retirement records from the employing agency is a final benefit payment determined.

Since the failed implementation of "RetireEZ" in FY 2009, several key outcomes were accomplished that will assist in overhauling retirement claims processing:

- Established a secure retirement data warehouse;
- Imaged 10 million retirement records for over 1 million Federal employees;
- Developed a retirement data standard for Federal agencies to share a single set of retirement information across the government;
- Implemented standard electronic data feeds for 35 percent of Federal Government employees; and,
- Extended the current OPM retirement calculator to Federal agencies.

With missing documentation being one of OPM's major challenges to overcome in retirement claims processing, the above outcomes should help improve the timeliness and accuracy of the initial benefit payment to annuitants.

Retirement claims are expected to increase over the next several years and it is important that OPM meets the challenge of overhauling the retirement claims process to better serve the Federal workforce.