



UNITED STATES OFFICE OF PERSONNEL MANAGEMENT

Washington, DC 20415

November 7, 2013

Office of the  
Inspector General

MEMORANDUM FOR KATHERINE ARCHULETA  
Director

FROM: PATRICK E. McFARLAND  
Inspector General

A handwritten signature in black ink that reads "Patrick E. McFarland".

SUBJECT: Fiscal Year 2013 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 addressed, 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 must face.

The five internal challenges included in this letter are OPM's development of new information systems, the need to strengthen controls over its information security governance, stopping the flow of improper payments, the retirement claims process, and the procurement process for benefit programs.

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 are the only challenges related to the reported material weaknesses.

The remaining challenges, while not currently considered material weaknesses, are issues which demand significant attention, effort, and skill from OPM in order to be successfully addressed. 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;
- Stopping the Flow of Improper Payments;
- Retirement Claims Processing; and,
- Procurement Process for Benefit Programs.

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 key initiatives of the President; 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 are presented.

This year we have added a discussion to address OPM's challenge with the procurement process in the benefit programs. I would also like to point out that we have removed the following challenge from last year's discussion:

Financial Management System and Internal Controls: Revolving Fund and Salaries and Expenses Accounts - The Office of the Chief Financial Officer (OCFO) resolved the long-standing issue related to the Fund Balance with Treasury (FBWT) reconciliation by taking the following steps:

- Performing monthly reconciliations, starting in July 2011, of the Government-Wide Accounting (GWA) activities with those in the General Ledger (GL). The reconciliations identified discrepancies between the GL and the GWA at the transactional level.
- Recording all cash receipt and disbursement activities by month-end, including identification of potential improvements in work processes.
- Performing a daily reconciliation for payment schedules since August 2011, and a cutoff schedule has been in use since September 2012. Additionally, more staff resources have been dedicated to the process.

I believe that the support of the agency's management is critical to meeting these challenges and will result in a better OPM for our customer agencies. I also want to assure you that my staff is committed to providing audit or investigative support as appropriate, and that they strive to maintain an excellent working relationship with your managers.

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

Attachment

**FISCAL YEAR 2013 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*, resulting in the launch of the largest reform of the Federal hiring process in over 30 years. OPM continues to make strides in addressing its human capital challenges in the following areas: hiring reform, the Veterans Employment Initiative, and closing skill gaps.

*Hiring Reform*

OPM continues to work collaboratively with Federal agencies represented on the Chief Human Capital Officers (CHCO) Council to ensure Job Opportunity Announcements (JOAs) are written in plain language, no longer require Knowledge, Skills, and Abilities narratives, and have been reduced to 2-3 pages in length. Ninety-four percent of JOAs now allow candidates to apply using a resumé.

In addition, OPM and the CHCO Council working group further refined the performance metric used to calculate the time to hire by establishing standardized guidelines to use a weighted average for the calculation. OPM believes that a weighted average is a superior calculation as it takes into account the volume of each agency's hiring. The 2012 weighted time to hire average was 87 days, a 6.5 percent improvement over the 2011 average of 93 days. The number of agencies with an average of 80 days or less has doubled, while the number of agencies with an average of more than 121 days was reduced by 38 percent. OPM continues to monitor on a quarterly basis, the time to hire Government-wide and for agency specific mission critical occupations as they work to reach the goal of hiring a Federal employee within 80 days. Through OPM's and the CHCO Council's improved guidance, agencies have achieved better integrity and validation of the data reported. However, there is still work that needs to be done in order to get more agencies to meet the time to hire goal of 80 day or less.

*Veterans Employment Initiative*

During fiscal year (FY) 2012, for the second consecutive year, the highest percentage of veteran new hires was achieved by the Federal Government in the last 20 years. The success of the initiative can be attributed to OPM's leadership through its Veterans Services

Group, which spearheaded the development of an Executive Order-directed Federal infrastructure that was created to improve the opportunities for veterans and transitioning military service members seeking Federal employment.

In addition, the implementation of the Government-wide Veterans Recruitment and Employment Strategic Plan guided agency efforts in eliminating barriers affecting veteran's employment in the Federal Government. In conjunction with the strategic plan, the Feds Hire Vets ([www.fedshirevets.gov](http://www.fedshirevets.gov)) website has been the "one stop location" to provide easy access to Federal employment-related information for veterans and transitioning military Service members. The veteran's employment initiative also required the establishment of Veteran Employment Program Offices in the 24 CHCO agencies as well as a Government-wide marketing program on the value of America's veterans. The challenge for OPM is to continue to ensure that Federal agencies respect and apply veterans' preference laws, rules, and regulations while using the tools that have been made available.

### Closing Skill Gaps

OPM, in coordination with the CHCO Council, chaired an interagency working group of action officers (Integrated Product Team (IPT)) who identified and are subsequently working to close skills gaps across the Federal government. The group has worked to define Government-wide competencies including the establishment of a clear, transparent, and replicable process for institutionalization in the future. OPM continues to partner with the Chief Management Officer Council, the Office of Management and Budget, and agencies to collaborate on the IPT findings and to implement strategies to close skills gaps.

During FY 2013, OPM designated senior Federal leaders from within the top occupations that have current and emerging skills gaps (IT/Cyber, Auditor, Economist, Human Resources, Acquisition and STEM (functional group)) to serve as Sub Goal Leads (SGLs) to design effective strategies for skills gap closure in their occupations. OPM, in collaboration with the SGLs, identified four areas of opportunity for how to address skill gap closure: recruitment, retention, development, and knowledge management.

OPM continues to make progress in closing critical skill gaps in the Federal workforce to help agencies recruit and retain the right people with the skills needed to achieve their goals. The current challenge for FY 2014 and FY 2015 will be to re-evaluate the selected Government-wide and agency specific Mission Critical Occupations (MCOs) and Mission Critical Competencies (MCCs) to determine which occupations and competencies should remain as Government-wide MCOs and MCCs. OPM must also identify new occupations and competencies that warrant attention. With the aging Federal workforce, OPM must be able to help agencies identify and close skills gaps, being responsive to changing applicant and workforce needs and continuing to monitor organizational performance measures in 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. In addition, with the passing of the Affordable Care Act (ACA), OPM's roles and responsibilities related to Federal health insurance have been expanded significantly. Under the ACA, OPM has been designated as the agency responsible for implementing and overseeing the multi-state program plan options, which start in 2014. The following highlights these challenges and current initiatives in place to address them.

### **A. Federal Employees Health Benefits Program**

The ever-increasing cost of healthcare is a national challenge. For the upcoming year, 2014, the average FEHBP premium increase is 3.7 percent, which is slightly higher than last year's increase of 3.4 percent. 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. OPM must also adjust to changes in the healthcare industry's premium rating practices. 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 healthcare 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, because 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.

The HCDW project is managed by OPM's Planning and Policy Analysis (PPA) office. In FY 2011, PPA entered into an Economy Act agreement with the OPM

Office of the Inspector General (OIG) to implement and operate this system, using the OIG's existing data warehouse system used to conduct OIG audits and investigations as a platform. The purpose of this collaboration was to allow PPA to access health care data that the OIG had already collected, and to capitalize on the OIG's expertise in this area. In return, PPA would provide resources to help further develop processes and systems.

In FY 2013, PPA decided to discontinue this arrangement and develop its own system. PPA is working with OPM's Office of the Chief Information Officer (OCIO) to build the hardware platform for its system. PPA has also engaged a contractor to build the data structures and analytical tools to run within the HCDW. We have agreed to provide carrier data updates to PPA in the future. Development efforts are in process, but have been delayed until early FY 2014.

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 (healthcare is a dynamic industry); etc.] Based on our observations and participation in this project, we have concerns that PPA and its contractors do not fully understand the dynamic nature and complexities of a project of this nature. OPM senior leadership will need to closely monitor this effort.

## **2) Prescription Drug Benefits and Costs**

Increases in drug costs have been and continue to be a major contributor to the rapid growth in health care costs over the last few years. Currently, pharmacy claims account for approximately 30 percent of FEHBP premiums. 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, prior to contract year 2011, these contracts lacked transparency, which limited our ability to audit and provide adequate oversight of this high cost benefit. This lack of transparency also made it impossible to ensure that FEHBP enrollees were receiving quality benefits at a fair price. However, effective January 1, 2011, any renewing PBM contract must 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 OPM OIG.

In its most recent FEHBP call letter (*Letter No. 2013-04, dated March 21, 2013*), OPM called on participating health plans to focus on ways to further reduce pharmacy spending through ensuring the safe and clinically effective use of prescription medications. To accomplish this objective, OPM called on participating health plans to consider the following in their 2014 benefit proposals:

- Synchronizing benefit designs so that enrollees can make meaningful comparisons between health plans.
- Keeping overall pharmacy trend at or below the industry growth rate for 2014.
- Having a generic dispensing rate of at least 80 percent for the FEHBP as a whole for 2014.
- Engaging enrollees in discussions about clinically effective medications that can be offered at a lower cost through the use of step therapy.
- Recommending benefit and administrative changes related to specialty drugs that will be respectful of member needs. Recommended changes should also be geared toward maintaining a specialty drug trend of 22 percent or less.
- Migrating toward a minimum four-tier prescription drug benefit structure with common definitions to help members understand pharmacy benefits and serve as an effective incentive to utilize generic and preferred brand name drugs.
- Proposing narrower or preferred pharmacy networks to achieve greater savings on prescription drugs with minimal member disruption.

While these short-term measures should have a positive impact on the program, we would encourage OPM to continue evaluating the relative costs and benefits of direct contracting for PBM services in order 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 initially 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 and would allow OPM to 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. It is our understanding that this provision is also included in the President’s 2014 budget package.

However, a continued stumbling block to achieving this objective is the current legislation, which prohibits OPM from contracting directly with PBMs. OPM has proposed statutory authority language changes, which seek to amend the current FEHBP law to permit OPM to contract directly with PBMs. While the language has been included in OPM’s FEHBP Modernization initiative, it has yet to receive the necessary approvals required to allow for a change to the law. That being said,

OPM should position itself and gain the expertise it will need to implement this contractual change should the proposed statutory language become law.

Ultimately, any changes implemented to the FEHBP's pharmacy benefits will need to meet the challenge of ensuring that the changes do not adversely impact FEHBP enrollees' health and safety while realizing true program savings.

### **3) Medical Loss Ratio Implementation and Oversight**

OPM implemented a new requirement for all Community-Rated carriers participating in the FEHBP in 2013, except those using a traditional rating methodology. Each Community-Rated carrier is held to a specific medical loss ratio (MLR), as determined by OPM. Simply put, Community-Rated carriers participating in the FEHBP must spend the majority of their FEHBP premiums on medical claims and approved quality health initiatives. If a carrier does not meet or exceed the MLR, it risks returning the excess premiums in the form of a rebate to the FEHBP. As with any change, this new premium rate-setting methodology will have its share of challenges.

As the implementation of this new requirement continues, OPM must be prepared to:

- Provide guidance on complex rate-setting issues and set consistent limits;
- Address new issues and provide clear, consistent guidance to all carriers;
- Update data tracking systems to account for all of the intricacies within the MLR process;
- Process additional rate submissions as this new requirement is expected to attract new carriers to the FEHBP;
- Ensure that carriers under the MLR system continue to provide high quality health benefits for federal employees; and,
- Administer the new policy consistently with the highest quality while preventing fraud, waste, and abuse.

To implement the change to MLR, OPM performed the following activities:

- Collected and analyzed historical FEHBP-specific MLR data for 2011 and 2012. OPM used this data to determine if the MLR standards established in the rate guidance were appropriate.
- Administered a pilot program during the 2012 contract year where plans could voluntarily opt into the new MLR requirements.
- Released guidance on the administration of the FEHBP MLR process.

Fundamentally, MLR will be an added responsibility that OPM will need to focus resources on so that the change is properly implemented with minimal disruption to the community rating process and the program, as a whole.

#### **4) Health Benefit Carriers' Fraud and Abuse Programs**

Under the FEHBP, participating health benefit carriers are required to operate a program designed to detect and eliminate fraud and abuse by employees, subcontractors, health care providers, and individual FEHBP members. This fraud and abuse (F&A) program must have the following components: (1) an anti-fraud policy statement; (2) written action plan and procedures; (3) formal training; (4) fraud hotlines; (5) educational programs; (6) technology; (7) security; and, (8) patient safety. By failing to have a comprehensive and effective F&A program, fraud and abuse may go undetected, resulting in increased health care costs, as well as potentially impacting the safety of FEHBP members.

Recent OIG audits have identified systemic weaknesses in health benefit carrier F&A programs. The carriers were not in compliance with the applicable FEHBP contract clauses and FEHBP Carrier Letters relating to the F&A programs. Specifically, carriers have not referred and/or reported all potential fraud and abuse cases and patient safety issues to OPM and the OPM OIG. Also, carriers have not implemented procedures to refer and/or report fraud and abuse issues within their contracted pharmacy benefits managers. Furthermore, the audited carriers could not accurately report the actual recoveries, savings, and cost avoidance achieved as a result of their F&A programs. As a result, the OIG could not determine whether the F&A programs administered by these carriers are a benefit to the FEHBP with respect to the costs and overall savings. The pervasiveness of these weaknesses is significant enough to believe that this could be a program-wide concern.

OPM recognizes the importance of FEHBP carriers having comprehensive, effective F&A programs and is benefiting from enhanced collaboration with the OIG and the carriers in light of recent audit findings in this area. In fact, at OPM's request, the OIG gave an F&A program presentation at the annual FEHBP Carrier Conference in March 2013.

Currently, OPM is examining its practices and a broad range of industry procedures to strengthen its existing fraud and abuse program. Steps they are taking include:

- Establish and communicate to FEHBP carriers a set of minimum standards to protect Federal funds and detect instances of fraud and abuse through an update of carrier letters, ensuring that procedures and programs are aligned with current industry standards.
- Clarify carriers' FEHBP F&A reporting requirements through an update of carrier letters.
- Join the Healthcare Fraud Prevention Partnership (HFPP). This collaborative arrangement allows public and private organizations to share information and best practices to improve fraud detection and prevent incorrect payments. OPM will become a communicative participant in the endeavor and will recommend that FEHBP carriers participate as well. This

will allow OPM to stay abreast of changes in industry standards and work effectively with stakeholders.

- Work with the National Healthcare Anti-Fraud Association (NHCAA) to establish accreditation standards for fraud investigators within the FEHBP. NHCAA is a public/private partnership similar to HFPP that provides data sharing services for private insurers and government entities, and education for individual fraud/abuse investigators.
- Continue to work collaboratively with the OIG, sharing reports, questionnaires, and special projects, as well as engaging in consistent oversight of all carrier fraud and abuse programs. OPM plans to seek OIG counsel on appropriate reporting, report analysis to maximize carrier accountability, and fluctuations in the industry to ensure their programs remain current and relevant.

Efforts thus far have confirmed inconsistencies, reporting discrepancies, and the need for clarification of some carrier requirements. OPM enhanced the review of carriers' annual reports and solicited corrective action plans to address deficiencies. OPM has also facilitated carrier-OIG communications to resolve open fraud-related audit recommendations. OPM continues to draft updated guidance to carriers, seek to develop reasonable standards that might lead to a form of accreditation, and refine the measures by which carrier F&A programs can be shown to be a benefit to the FEHBP.

As is evident by the measures identified above, OPM appears committed to continue to work collaboratively to address this important challenge facing the program. However, OPM must continue to evaluate this issue and implement controls (including contract changes, as appropriate) which will hold all FEHBP carriers accountable for operating an effective fraud and abuse program. Effective F&A programs will result in significant FEHBP savings and, more importantly, protect FEHBP members.

## **B. Affordable Care Act (ACA)**

Under the ACA, OPM is 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 for small employers and uninsured individuals to choose. 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 MSP function, as well as the expanded FEHBP-eligible population. Currently, the ACA does not specifically fund OPM for its new healthcare responsibilities. In addition, the ACA mandates that resources essential to the management of the FEHBP cannot be used to start up and manage the new program.

Over the past three fiscal years, OPM received limited funding through an arrangement with the Department of Health and Human Services (HHS), which received ACA funding from Congress. With these funds, OPM established policy and operational teams to review program and policy issues related to implementing the Multi-State Plan Program (MSPP), as well as provided analytical support for the MSPP. However, full funding beyond FY 2013 is a significant challenge for the agency, as well as for the OIG, which is charged with program oversight responsibilities. Without appropriate resources, OPM will not be able to support these new activities.

Even with adequate resources, implementation of the ACA presents a unique set of challenges for OPM. Since this is a totally new and complex program, OPM must:

- Develop a thorough understanding of complex laws and regulations governing the ACA, as well as State healthcare.
- Develop and implement regulations, policies, and contracts supporting the MSPP.
- Work cooperatively with Administration Officials, Congress, and other Federal agencies/departments responsible for implementing the ACA.
- Initiate an outreach program with all stakeholders.
- Develop a short-term and long-term organizational structure to support the MSPP.
- Design and implement an internal control structure and management information system to ensure that MSPP goals and objectives are met, as well as to ensure compliance with all laws, regulations, and guidance.
- Create a comprehensive oversight program.

To meet the goal of making MSPP health insurance options available for enrollment by October 2013, OPM has accomplished the following:

- Published the final MSP application on January 18, 2013, in FedBizOpps. Healthcare issuers who want to offer their plan in the MSP Marketplace apply using the MSP online application portal.
- Published the final MSP rule on March 11, 2013, in the Federal Register. The final rule establishes standards for issuers to join the MSP Marketplace, including standards relating to (1) a level playing field; (2) phased expansion; (3) rates and benefits; and (4) internal appeals and external review.
- Given presentations on MSP implementation to members of Congress, States, issuers, minority and small business groups, and public advocacy groups.
- Continued to participate in inter-agency workgroups to implement the ACA.
- Reviewed and commented on several HHS regulations to determine their impact on the MSPP.
- Negotiated provisions in the regulations to facilitate successful implementation of the MSPP.
- Reviewed applications submitted by issuers to offer a plan on the MSP Marketplace.

- Conducted contract negotiations with issuers to offer a plan(s) on the MSP Marketplace.
- Compiled and transmitted information on each applicable state-level issuer to HHS for the Federally Facilitated Marketplace via the Health Insurance Oversight System; to states that intend to operate their own exchange but utilize the prescribed HHS templates via the System Electronic Rate Filing Form; and directly to those states who will operate their own marketplace.
- Met routinely with OPM's OIG to (1) discuss internal control structures; (2) provide status reports; (3) get feedback on the proposed regulations and contract; and (4) discuss oversight concerns.

Implementing and administering this new 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 95 percent of all personnel background investigations for the Federal Government and processes approximately 2 million background investigations per year. Agencies use the background 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.

FIS has an active Integrity Assurance group 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 and monitoring by OPM management.

Of particular concern is FIS's dependence on one of its contractors, US Investigations Services, LLC (USIS). USIS currently holds two contracts with OPM. Under the Fieldwork contract, USIS investigates and reviews background investigation cases. Under the Support contract, USIS reviews and closes cases, including the cases USIS itself completes under the Fieldwork contract<sup>1</sup>. In our opinion this creates a conflict of interest.

Furthermore, USIS is currently under investigation by the OIG. We are limited in the information we can share at this time, due to the ongoing investigation. However, our preliminary findings suggest that between March 2008 and September 2012, USIS willfully failed to perform in accordance with the terms of their Fieldwork contract with OPM. This is very troubling considering that, according to the June 2013 Senate Testimony of

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<sup>1</sup> According to FIS, since 2011 the only field work cases reviewed by USIS under their Support contract have been the lower complexity National Agency Checks with Law and Credit and Access National Agency Checks with Inquiries.

Associate Director Merton Miller, approximately 45 percent of FIS's overall contract workload is assigned to USIS.

As mentioned above, FIS is responsible for all background investigations in the federal government and conducts approximately 95 percent itself or through the use of contractors. The remaining five percent have been delegated to certain Federal agencies (the Federal Bureau of Investigation, the Central Intelligence Agency, the Department of Homeland Security, and the U.S. Agency for International Development to name a few). FIS also needs to continue to ensure these delegated agencies maintain a high level of quality assurance. Several of the agencies who have recently been audited by FIS were found to be lacking a true quality assurance program; therefore, the quality of those background investigations are at risk.

### **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 addressed 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**

OPM has a history of troubled system development projects. Past examples include the retirement modernization project, the Consolidated Business Information System financial management system, the Service Credit system, and the USAJOBS 3.0 website. While the problems that occurred during the implementation of these systems have been corrected, the fundamental control weaknesses remain. In our opinion, the control weaknesses relate to the lack of central oversight, policy, and institutional knowledge of proper system development and project management.

Our primary concern is that all of these systems were developed independently of agency-wide requirements or guidance – because no current guidance existed at OPM. Most system development projects at OPM are initiated and managed by OPM program offices with little oversight or interaction with the Office of the Chief Information Officer (OCIO). These program office managers do not always have the appropriate background in project management or information technology systems development.

The OCIO recently published a new system development life cycle (SDLC) policy, which is a significant first step in implementing a centralized SDLC methodology at OPM. However, policy alone will not improve the historically weak SDLC management capabilities of OPM – further action will be needed.

The new policy is currently only applicable to OPM's 11 major information technology (IT) investments and is not actively enforced for other IT projects. However, it is imperative that the OCIO make it a priority to enforce this new policy on all system development projects. The Service Credit system was an example of a system development project that did not meet the criteria of a major investment, but when it failed there were serious consequences for the agency – not financial in nature, but impactful to stakeholders and embarrassing in terms of media exposure and political scrutiny.

The new SDLC policy incorporates several OIG recommendations related to a centralized review process of system development projects. We also recommended, in our prior audits, that the OCIO develop a team with the proper project management and system development expertise to oversee new system development projects. Through this avenue, the OCIO should review SDLC projects at predefined checkpoints, and provide strict guidance to ensure that program office management is following OPM's SDLC policy and is employing proper project management techniques to ensure a successful outcome for all new system development projects.

Although the OCIO generally agrees that it should oversee all development projects, resource limitations continue to prohibit the implementation of a centralized project oversight team. In the interim, the OCIO is providing training to project managers through a Project Management Community of Practice designed to provide guidance on best practices in systems development.

## **2. INFORMATION SECURITY GOVERNANCE**

OPM relies on information technology 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 many years, we have reported increasing concerns about the state of the OPM'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 Federal Information Security Management Act (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. In the last three years, the OCIO has updated policies and created a viable information security group headed by a permanent SAISO.

However, the decentralized nature of OPM's IT security program continues to be a root cause of many of the recurring instances of non-compliance with FISMA requirements. An IT security program can be designed 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, while the OCIO is responsible for policy development and oversight.

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, have neither the expertise nor the interest in properly managing 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 suggested that OPM adopt a more centralized approach to IT security. We recommended that the agency recruit a staff of information security professionals to act as designated security officers (DSO) that report to the SAISO. However, throughout FY 2011 and FY 2012, the OCIO continued to operate with a decentralized IT security structure that did not have the authority or resources available to adequately implement the new policies.

In August 2012, the OPM Director issued a memorandum to Associate Directors and Office Heads notifying them that IT security responsibilities would be centralized under the OCIO effective October 1, 2012. The OCIO developed a plan to hire a team of Information System Security Officers (ISSO) to centrally manage the agency's IT security program. The OCIO hired three ISSOs in FY 2013, but these three individuals are only able to manage the security for approximately one-third of OPM's major applications. Additional ISSOs are required to manage the remaining systems, but the OCIO does not currently have the resources available to hire these individuals.

Once the ISSO team is fully staffed, we expect to see an improvement in compliance with FISMA requirements. Nevertheless, the issue will continue to be a significant internal management challenge pending successful implementation of the centralized DSO plan.

### 3. STOPPING THE FLOW OF IMPROPER PAYMENTS

The Administration has aggressively pursued waste, fraud, and abuse across government programs during the last few years. One of the key initiatives has been the reduction of improper payments. OPM continues to make progress in efforts to reduce the extent and rate of improper payments and to recover an increasing percentage of improper payments. These efforts have been led by OPM's Improper Payments Working Group (IPWG) and are detailed below.

- OPM developed and updated a comprehensive Improper Payment Plan that detailed goals and major actions designed to reduce improper payments for the Retirement Program and the FEHBP, and to recover an increasing percentage of retirement payments to deceased annuitants. OPM will fully assess and report against major actions noted in the plan as they are completed and in the FY 2013 Agency Financial Report (AFR). The IPWG will also continually review and update the plan as needed.
- OPM improved its process for annual reporting on improper payments in the FY 2012 AFR, and is in compliance with the Improper Payments Elimination and Recovery Act of 2010. Improvements included additional details on the causes of improper payments and corrective actions to reduce them, as well as improved review of factual information included in the AFR. In addition, OPM issued detailed policies and procedures in June 2013 for its annual AFR reporting.
- OPM made progress with actions to assist the Department of Treasury in recovering improper payments to financial institutions. For instance, the Office of the Chief Financial Officer (OCFO) initiated a process for hard copy check cases in which it requests information from banks about the debtor who initially cashed the check. The OCFO is also sending letters to financial institutions and the last withdrawer or joint account holder requesting the return of funds after the annuitant or the survivor's death.
- Retirement Services (RS) established a Data Mining Working Group (DMWG) in November 2012 to identify areas in the Retirement program where fraud, errors, or delays in reporting could result in improper payments to deceased annuitants. Subject matter experts from RS met, analyzed, and discussed potential opportunities to use existing data within, or in conjunction with, RS's annuity roll to identify improper payments. The DMWG provided recommendations on potential sources of data mining.
- Healthcare and Insurance (HI) continues its focus on identification and resolution of audit findings during the OIG draft report phase, to increase health carriers' understanding, response, and concurrence with findings. HI contracting officers are also enhancing the use of corrective action plans to further address internal control weaknesses identified in the OIG audits. The rate of improper payments trended downward for the FEHBP in FY 2013.

OPM made a number of improvements in its efforts to reduce improper payments across all of its programs; however, improper payments to deceased individuals continue to receive attention from outside the agency. Between FYs 2006 and 2010, OPM identified an annual

average of \$120 million in improper payments to deceased annuitants. During FYs 2011 and 2012, the average dropped to \$105.5 million. It is important to note that this entire amount does not represent egregious long-term improper payments. Much of it comes from improper payments that are identified and recovered in a matter of a few months. These are often the result of a retiree passing away before the retirement payment is made for that month, or because the deceased's family takes a month or two to report the death. These overpayments are often recovered in full. The bigger concern is when an annuitant's death is not properly reported or detected and annuity payments continue for many years, resulting in high dollar overpayments. These payments are frequently taken by a relative or guardian of the deceased annuitant who failed to report the death.

Since issuing a report in September 2011, *Stopping Improper Payments to Deceased Annuitants*, the OIG has worked closely with OPM on ways to identify and prevent improper payments to deceased annuitants. A task force was formed comprised of high level executives, including the Chief Operating Officer, the Chief Financial Officer, the Associate Director for Merit System Audit and Compliance, and the Associate Director of Retirement Services. This group spearheaded efforts to develop a strategic plan for stopping improper payments, including payments to deceased annuitants. This strategic plan was finalized in January 2013, with the understanding that it would be updated annually.

It was reported in OPM's FY 2012 Annual Financial Report that the outstanding balance of overpayments to deceased annuitants decreased from \$102.9 million to \$86.1 million, a 16 percent reduction in one year. However, we have identified three areas that continue to hinder RS's ability to adequately address this problem:

- OPM's Improper Payments Strategic Plan does not identify measurable goals/milestones for the RS's Retirement Inspections office, which is the primary office responsible for identification and prevention of improper payments to deceased annuitants through on-going matches and surveys, and fraud tips.
- A failure to adequately plan and complete special projects to identify improper payments - the best example of this is the current 1099-R Project. It has not yet progressed to include systematically researching dates of death, which is needed to verify whether the person is indeed deceased and to calculate the improper payment, if applicable. This step must be taken in order to identify and recover improper payments. The current 1099-R Project began with the 2009 tax year forms, which were mailed in January 2010. Over 33,000 forms were returned undeliverable. Three years later, OPM still has not completed this work. Moreover, although OPM has received and collected the returned Forms 1099-R mailed in January 2011, January 2012, and January 2013, it has not taken any further action on these forms. The lack of a comprehensive, carefully designed plan with milestones and deadlines to complete the project has contributed to the failure to produce results.
- A failure to properly recover improper payments and refer cases to the OIG where fraud was suspected. In a memorandum dated July 31, 2012, the OIG informed Associate Director Kenneth Zawodny that the Office of Investigations (OI) had

noted a significant decline in suspected fraud referrals from RS and that the majority of the referrals submitted to the OIG in 2012 were too old to investigate because they had been dropped for death more than five years previous to the referral. The OIG observed that in cases where fraud was suspected, there was a pattern of delayed reclamation and delayed referral to the OIG. This pattern continued in FY 13. Retirement Inspections referred 12 suspected fraud cases to the OIG in FY 13; 10 of those referrals (83percent) were too old to investigate because the statute of limitations had already passed or was imminent.

OPM is challenged to address these preceding issues to improve its proactive improper payment detection and prevention efforts.

#### **4. RETIREMENT CLAIMS PROCESSING**

OPM is responsible for processing in excess of 100,000 retirement applications a year for Federal employees. The timely issuance of full annuity payments to annuitants has been a long-standing challenge for OPM. In January 2012, OPM released and began implementation of a strategic plan to reduce the unacceptable backlog of retirement claims, with the goal of adjudicating 90 percent of retirement cases within 60 days starting in July 2013.

While significant progress was made in reducing the backlog, OPM did not meet its goals as a result of two main factors: 1) OPM received an influx of over 20,000 cases from the United States Postal Service for early retirements and buyouts; and 2) a reduction in funding associated with sequestration, which resulted in the temporary termination of overtime hours used to process claims.

Despite these challenges, OPM has been able to keep pace with incoming applications. OPM's inventory of claims as of September 2013 was 17,719, representing a 57 percent decrease from the inventory of one year prior, which was 41,176. At the end of July 2013, processing time dropped to an average of 91 days from 136 days as of December 31, 2012, representing a decrease in average processing time of 45 days.

OPM remains committed to providing accurate and timely processing of retirement claims. RS continues to take important steps to meet the challenge of reducing the backlog of retirement claims and improving its claims processing times by implementing its strategic plan, which includes four key areas: people, productivity and process improvements, partnering with agencies, and progressive IT improvements.

Based on the current budget environment and historic workload, OPM modified future projections and estimates the elimination of the backlog to a consistent workload by March 2014. However, this projection assumes future budgetary alignment. Without proper resources, OPM's ability to reduce the backlog to an acceptable level and to meet its goal of processing 90 percent of retirement claims in 60 days is in jeopardy. In addition, if OPM does not receive funding for its IT initiatives, the ability to achieve sustained progress in meeting its processing goals will be severely impacted.

## 5. PROCUREMENT PROCESS FOR BENEFIT PROGRAMS

As the Federal Government's human resources agency, OPM administers insurance benefits for millions of Federal and United States Postal Service employees and annuitants and their eligible family members. To achieve this purpose OPM works to facilitate access to high-caliber healthcare and insurance programs, including health services; dental and vision benefits; flexible spending accounts; life insurance; and long-term care programs. However, our audits of the BENEFEDS benefits portal, the Federal Employees Dental and Vision Insurance Program (FEDVIP), the Federal Long Term Care Insurance Program (FLTCIP), and the Federal Flexible Spending Account Program (FSAFeds) raised several concerns regarding how these benefit programs are procured by OPM. Specifically, our concerns encompass the following areas:

- Lengthy periods of performance awarded under the contract term and numerous options exercised to extend the performance periods;
- Contracting methods utilized under the procurements; and,
- Processes followed for contract modifications.

The procurement process for the above-mentioned special benefit programs differs from the process utilized for OPM's other benefit programs (i.e., the FEHBP and the Federal Employees' Group Life Insurance Program [FEGLI]). Most of these special benefit programs have set periods of performance (at least seven years with options to extend), requiring a re-competition at the end of this period. The FEHBP and FEGLI contracts, on the other hand, are not re-competed, but roll over from one year to the next and are modified as needed. The FEHBP and the FEGLI contracts also incorporate the Federal Employees Health Benefits Acquisition Regulations (FEHBAR) for the FEHBP and the Life Insurance Federal Acquisition Regulations (LIFAR) for the FEGLI. The FEHBAR and the LIFAR were established to supplement the Federal Acquisition Regulations (FAR), the regulations governing most Government acquisitions, for acquiring and administering a contract(s) for the Federal employees' health and life insurance programs. Conversely, with the exception of the FSAFeds contract, which is a FAR contract, the BENEFEDS, FEDVIP, and the FLTCIP programs are not FAR procurements, but incorporate certain FAR clauses, as needed. Because of these differences, it is critical that OPM fully understands and takes into account the following:

- The need for timely re-competitions of these special benefit programs. For example, the BENEFEDS and FSAFeds contracts have been extended numerous times to maintain program continuity while other programs were re-competed. The result of these extensions to the FSAFeds contract is that the program's period of performance has now exceeded a 10-year period, which we believe is disadvantageous to the Government because of the constant changes in the market for this type of benefit and a lack of built-in competition for enrollees that is inherent in other benefit programs administered by OPM (i.e., the FEHBP and the FEDVIP).

- The importance of selecting the most appropriate contracting method for the benefit program being procured. For example, the contracting method selected for the FSAFeds program (which is a FAR contract) was fixed-price with prospective price redetermination. However, FAR 16.205-3 cites limitations for using this type of contracting method, and we believe that a firm fixed-price contracting method would have been more appropriate for these programs.
- The importance of following each program's contractual requirements for extensions and modifications. For example, our reviews of the special benefit programs found that OPM has a history of modifying contract terms and not documenting the justification for the modification, that the contract's price redetermination clause was not followed in cases where prices were re-determined, or that FAR 17.207(d)(2), the exercise of options clause, was not followed when exercising contract options.

To meet these challenges on future program procurements, we encourage better coordination between OPM's Contracting Office and the Federal Employees Insurance Operations group so that there is an understanding of the available procurement methods, selection of the most appropriate procurement method, and that the contractual requirements are followed from the development of the request for proposal until the contract is re-competed.