

# **OFFICE OF INSPECTOR GENERAL**

## **Management Information Report**

### **Management and Performance Challenges Facing the Railroad Retirement Board**

**Report No. 18-03  
December 11, 2017**



**RAILROAD RETIREMENT BOARD**

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## Introduction

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This statement has been prepared pursuant to the Reports Consolidation Act of 2000 and the requirements of Office of Management and Budget (OMB) Circular A-136, which require that the Inspectors General identify what they consider the most serious management challenges facing its respective agency and briefly assess the agency's progress in addressing those challenges.

Congress created the railroad retirement system more than 80 years ago. The Railroad Retirement Act (RRA) created a nationwide retirement system for railroad workers to provide income security in their old age. Over the years, the program has been expanded to include disabled workers, spouses and divorced spouses of retired workers, widows, children, and parents of deceased railroad workers. In 1938, Congress enacted the Railroad Unemployment Insurance Act (RUIA) which added a nationwide system of unemployment insurance, and later a program of sickness insurance. During fiscal year 2016, the Railroad Retirement Board (RRB) paid about \$12.3 billion, in retirement and survivor benefits to approximately 553,000 beneficiaries and approximately \$133 million in unemployment and sickness benefits, to approximately 33,000 claimants.<sup>1</sup>

RRB also administers aspects of the Medicare program and has administrative responsibilities under the Social Security Act and the Internal Revenue Code. In fiscal year 2016, RRB automatically enrolled more than 27,100 beneficiaries for Medicare. At the end of 2016, approximately 465,300 persons were enrolled in the Part A plan, and 445,900 of those persons were also enrolled in Part B.<sup>2</sup>

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<sup>1</sup> United States Railroad Retirement (RRB), *An Agency Overview*, (Chicago, IL: January 2017).

<sup>2</sup> RRB, *2017 Annual Report*, (Chicago, IL).

Our identification of challenges facing RRB management is based on recent audits, evaluations, investigations, and current issues of concern to the Office of Inspector General (OIG). RRB OIG identified the following seven major management challenges facing RRB during fiscal year 2017.

<b>Most Serious Management and Performance Challenges Facing RRB as of October 1, 2017 (as identified by the Inspector General)</b>	
<b>Challenge 1</b>	<i>Program Integrity to Strengthen Disability Programs</i>
<b>Challenge 2</b>	<i>Information Technology Security and System Modernization</i>
<b>Challenge 3</b>	<i>Management of Railroad Medicare</i>
<b>Challenge 4</b>	<i>RRB's Continued Noncompliance with Improper Payments Elimination and Recovery Act and Assessing Payment Accuracy</i>
<b>Challenge 5</b>	<i>Human Capital Management</i>
<b>Challenge 6</b>	<i>Material Weaknesses Related to Financial Statement Reporting and the Control Environment</i>
<b>Challenge 7</b>	<i>Lack of RRB Oversight of the National Railroad Retirement Investment Trust</i>

We provided RRB these management challenges for inclusion in its fiscal year 2017 Performance and Accountability Report. Subsequently, the RRB provided written comments, which are reprinted in Appendix I. In its written comments, RRB described actions implemented and approaches taken to improve the functions and operations of the agency to address the challenges identified.

Throughout the management challenges, we included various actions the RRB has taken as they relate to these challenges. However, these actions do not always meet the intent of the OIG recommendations nor do they always address the weaknesses that remain. As responsible public stewards, RRB management must implement an effective control system to ensure that all agency programs are managed efficiently. While RRB management provided expansive comments and rebuttal, our assessment of the major challenges facing RRB remain unchanged. Throughout the report, we address instances in which we felt RRB's response was particularly inaccurate or incomplete.

## **Challenge 1 – Program Integrity to Strengthen Disability Programs**

There are two types of disability awards administered by RRB, the occupational disability annuity and the total disability annuity. A railroad employee is considered to be occupationally disabled if a physical or mental impairment permanently disqualified them from performing his or her regular railroad occupation (even though the employee may be able to perform other kinds of work). Occupational disability annuities are payable to qualified applicants at or after the age of 60 with 10 years of service, or at any age if the employee has at least 20 years of service. According to RRB's 2017 Annual Report, in fiscal year 2016, occupational disability annuities totaling approximately \$852 million were paid to approximately 21,000 annuitants.<sup>3</sup> The approval rate for occupational disabilities was approximately 98 percent in fiscal year 2016 and has remained relatively consistent for months in fiscal year 2017 for which data has been reported. A total disability annuity is payable, regardless of age, to employees with at least 10 years of service but requires that the applicant be unable to perform any substantial gainful activity in the U.S. economy. In fiscal year 2016, total disability annuities totaling over \$254 million were paid to approximately 10,300 railroad annuitants.

The occupational disability program remains the subject of sustained scrutiny by Congress, OIG, and the Government Accountability Office (GAO) as a result of continued program vulnerabilities and ineffective oversight from RRB. The inability of RRB to effectively manage the disability program leaves over \$1 billion in annuity payments at increased risk.

In 2007, OIG initiated a joint investigation with the Federal Bureau of Investigation that identified a far reaching occupational disability fraud scheme perpetrated by a number of Long Island Rail Road (LIRR) retirees, doctors, and disability facilitators. This case was prosecuted by the U.S. Attorney's Office for the Southern District of New York. All 33 people charged in connection with the LIRR disability fraud scheme have either pled guilty (28 individuals) or been convicted at trial (5 individuals). OIG estimates that 700 individuals may have been involved in this fraud scheme and investigations are ongoing.

Through the LIRR investigation and subsequent work, significant deficiencies were identified within the occupational disability program and OIG has made numerous recommendations for improvement through audits, OIG Alerts, and investigative activity. Further, according to a 2009 GAO audit of RRB's occupational disability program, "a nearly 100-percent approval rate in a federal disability program is troubling, and could indicate lax internal controls in RRB's decision-making process, weaknesses in program design, or both."<sup>4</sup>

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<sup>3</sup> RRB, 2017 Annual Report.

<sup>4</sup> Government Accountability Office (GAO), *Railroad Retirement Board: Review of Commuter Railroad Occupational Disability Claims Reveals Potential Program Vulnerabilities*, GAO-09-821R (Washington D.C.: September 9, 2009).

The OIG remained so concerned by RRB's failure to address deficiencies in its occupational disability program that in February 2014, the Inspector General (IG) issued a seven-day letter alerting RRB of its concerns and outlined particularly serious or flagrant problems, abuses, and deficiencies relating to the occupational disability program.<sup>5</sup> The IG urged the agency to institute substantial and meaningful corrective actions.

In May 2015, the U.S. House of Representatives Committee on Oversight and Government Reform's Subcommittee on Government Operations convened a hearing to examine if RRB was doing enough to prevent fraud in its occupational disability program and to assess RRB's process for determining which workers are eligible for benefits.<sup>6</sup> In testimony, the IG detailed the systemic deficiencies within RRB's occupational disability program, as well as several key OIG recommendations aimed at addressing these deficiencies.

In addition, in August 2015, an RRB contractor issued a report titled, *Benefit Payment Program Fraud Prevention/Detection Assessment/Advisory Services*, which provided an overview of RRB's control procedures for its four major benefit paying programs, including disability. This report outlined six vulnerabilities related to the disability program that could limit RRB's ability to identify and prevent fraud and payment errors in the program, such as lack of monitoring of providers who submit medical evidence; lack of analytic monitoring and screening of applicants; limited electronic data collection; limited use of continuing disability reviews; reviews for occupational disability only cases; gaps in employer provided vocational information; and inadequate accountability and information for medical providers. Although the Mathematica report did not make recommendations, the vulnerabilities listed are similar to concerns outlined in OIG and GAO reports.

As a result of the IG's seven-day letter, Congressional Hearing, the contractor's report, oversight by OMB, and recommendations by GAO and OIG, RRB established a Disability Program Improvement Plan (DPIP) to track improvements to its disability program. RRB's DPIP consists of 18 initiatives with related tasks assigned, aimed at improving program integrity within RRB's disability program.

In addition to the DPIP, RRB hired a Chief Medical Officer, to assist in providing medical guidance to the disability program's adjudication staff. However, the position of Chief Medical Officer is currently vacant after being filled for ten months.

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<sup>5</sup> RRB Office of Inspector General (OIG), *Seven-Day Letter to Congress* (Chicago, IL: February 10, 2014).

<sup>6</sup> U.S. House of Representatives Committee on Oversight and Government Reform's Subcommittee on Government Operations Hearing, *Is the Railroad Retirement Board Doing Enough to Protect Against Fraud?* (Washington D.C.: May 1, 2015).

These enhancements to the disability program, if thoroughly implemented, could have generated improvements in program integrity. However, foundational flaws and a culture seemingly entrenched in defending its disability program at the expense of strengthened program integrity have resulted in little meaningful improvement or change.

While the current DPIP indicates progress being made in its implementation, further review of the plan indicates that due dates are being changed without the original due date being noted and, more concerning, tasks are being labeled as closed when no more action is anticipated on the task but not necessarily when the task has been implemented. For example, under Initiative #6, *Enhancing the Application Process by Reviewing and Revising, Application Forms and Related Publications*, tasks under Recommendation 4, tasks 11 through 16, were to be completed on various days between September 30, 2015 and May 31, 2017. In the latest version of the DPIP, the new current due dates for the same tasks are listed as TBD (to be determined). Additionally, previous versions of the DPIP showed Recommendation 6 with due dates for various tasks; however, the latest version was updated to show later due dates for those same tasks. Further, under Initiative #1, *Additional Specialist Consultative Exams (SCE)/Functional Capacity Examination (FCE)*, the DPIP states that this initiative and subsequent tasks are closed. However tasks 26 - 28, were never implemented based on RRB's three member Board's (the Board) February 23, 2016, memorandum, in which the Board stated that the existing protocol for the use of FCEs would not be changed. The OIG's position is that the DPIP should indicate "closed-not implemented" versus "closed", which does not accurately reflect the actions taken or not taken.

The current DPIP, dated August 31, 2017, indicates that many of the initiatives were closed and specifies they were closed timely. From an oversight and program improvement perspective, the DPIP does not accurately reflect definite implementation of program improvements, which present a challenge for the Congress, as well as other oversight entities because they rely on the DPIP to reliably identify which tasks have been implemented.

The OIG also remains concerned that RRB has not taken adequate steps to assure the collection of information on disability applicants' job duties from their railroad employers. In May 2016, the IG issued an alert to the Board revisiting a critical program vulnerability previously identified by OIG. Specifically, the alert reiterated that RRB's continued failure to verify self-reported job information with a third party (i.e., railroad employers) during the occupational disability adjudication process jeopardizes program integrity and does not comply with RRB regulations.<sup>7</sup>

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<sup>7</sup> OIG Alert Number 16-03, *Systemic Vulnerability within the Railroad Retirement Board's Occupational Disability Program*, (Chicago, IL: May 11, 2016).

In 2016, RRB published their intent to replace the current job verification forms (G-251a and G-251b) with a singular version.<sup>8</sup>

While this form has undergone extensive revisions as part of the DPIP, language in the Federal Registrar stated twice that completion of this form is voluntary. This is incongruent with RRB regulations that state RRB “shall also consider the employer’s description of the physical requirements and environmental factors relating to the employee’s regular railroad occupation, as provided by the employer on the appropriate form.” This, among other third party verifications, is an important program integrity step that RRB has not fully implemented. In 2016, about 19 percent of disability determinations included an employer provided form. From January through August 2017, employers provided job description information in approximately 30 percent of cases, with about 35 percent providing the information in August 2017 (the month with most recently reported data).<sup>9</sup> An increase in submission of this information is promising, but until RRB makes this information mandatory and based on the individual’s specific job duties, it cannot fully assess an applicant’s eligibility.

In addition, in September 2017, the IG issued an alert to the Board regarding the Occupational Disability Certification Form RL-8A.<sup>10</sup> This alert restated the IG’s concerns with the Board’s inaction to enact an annual eligibility questionnaire that requires a certified response from all disability annuitants. In August 2017, RRB’s Office of Programs issued Procedure Transmittal 17-65, *New Disability Forms RL-8/RL-8A and Revised Form G-254*, which detailed RRB’s newly enacted annual occupational disability certification procedure. Subsequently, the Office of Programs issued Informational Bulletin 17-27, *Form RL-8A – Occupational Disability Certification Annual Release Notification*, stating that it has, based on very specific and limited RRB developed criteria, identified 229 occupational disability cases that will be subject to the RRB’s new procedure. Out of these 229 cases, 77 will receive Continuing Disability Reviews and 152 will receive the new *Occupational Disability Certification* (Form RL-8A).

This newly developed certification procedure only covers approximately one percent of RRB’s 21,000 occupational disability annuitants. Because the criteria for inclusion in the certification were so narrowly drafted, most occupational disability annuitants are not subject to continued review.

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<sup>8</sup> Form G-251 is the “Vocational Report” where the disability applicant self reports all information related to their disability. Forms G-251a and G-251b are the “Job Information” forms that are sent to the employer to verify the job information submitted by the applicant on form G-251. In 2016, the RRB proposed to combine the G-251a and G-251b into one form, a revised G-251a, to be sent to the railroad employer to verify the job information reported by the applicant on Form G-251.

<sup>9</sup> The 35 percent includes submission of the G-251a and “Other (Employer Job Description)”, as reported by RRB.

<sup>10</sup> In November 2016, OIG recommended that proposed Form RL-8A be amended to gather additional information regarding medical improvement including whether the annuitant requires continued treatment/medications. This recommendation was not implemented despite the fact that 20 CFR § 220.179, Exceptions to Medical Improvement, lists an annuitant’s failure to follow, without good cause, prescribed treatment which would be expected to restore their ability to engage in substantial gainful employment as a potential reason to terminate an annuitant’s disability.

This new annual disability certification procedure as well as the eight year timeframe in which it took to implement, is a continuation of concern to the IG. The perfunctory nature of RRB's Form RL-8A, combined with its limited use, undermines RRB's ability to proactively mitigate fraud and abuse in its disability program.

Another program improvement that has not been fully implemented is action to prevent occupational disability adjudications based on the simple task standard or one job aspect for railroad employees. In May 2015, OIG issued an alert to the Board recommending improvements to the disability program. One of the recommended improvements was that RRB should formalize and implement procedures clarifying that an occupational disability application should be assessed against an applicant's permanent inability to perform the essential functions of their regular railroad occupation and not just a single task or function.<sup>11</sup> RRB implemented a portion of the recommendation by agreeing to provide refresher training to disability examiners to clarify that occupational disabilities should be awarded only to applicants whose conditions are such that they are unable to perform their regular railroad occupation. However, the portion of the recommendation pertaining to formalizing procedures so that an occupational disability application is not assessed based on inability to perform just a single task or function, was not fully implemented. The action taken—to review the disability procedures and verify that they do not include allowing an individual to be found occupationally disabled or unable to perform a nonessential job task or function—rather than formalizing and implementing procedures clearly stating this, did not effectively address the IG's recommendations and does not leave claims examiners unequivocal guidance should they face such a situation.

OIG remains significantly concerned with RRB's inaction regarding the recovery of potentially fraudulent payments made to LIRR annuitants. Specifically, OIG has recommended RRB use its fraud or similar fault authority to collect payments made to annuitants based on fraudulent or misleading information. After the LIRR fraud was uncovered and prosecutions were ongoing, RRB terminated benefits of annuitants who applied using medical documentation supplied by specific healthcare providers convicted of fraud. The annuitants were subsequently allowed to reapply with new medical information and more than 80 percent did. This resulted in an approval rate of over 90 percent for the terminated LIRR beneficiaries who refiled.

In addition, as of August 2017, only \$399,147 of the approximately \$5.9 million in court ordered restitution related to the LIRR convictions had been returned to RRB. It remains imperative that RRB use every avenue to recover payments lost due to fraud or similar fault and to prevent the continued abuse of its occupational disability program. Allowing individuals to commit fraud against the program, with no repercussions, only encourages future fraud and abuse of the program.

As responsible public stewards, RRB management must effectuate comprehensive and meaningful procedural and cultural change to ensure that disability benefits are adjudicated accurately; awarding benefits only to those who are eligible after an

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<sup>11</sup> OIG Alert Number 15-05, *Recommended Improvements to the Disability Program*, (Chicago, IL: May 8, 2015).

independent and thorough review of the application and all required supporting documentation. RRB should not simply take applications at face value, but assess the veracity of the information by validating with appropriate third parties. Further, RRB must work to ensure programmatic improvements, even those requiring legislative changes, are made expeditiously.

If implemented properly, the OIG's prior recommendations provide valuable steps to improve program integrity. Without these changes, RRB's propensity to inaccurately adjudicate disability applications will continue to cost taxpayers millions in unwarranted expenses annually.

RRB's culture has been to focus on paying benefits quickly, which increases the likelihood of abuse in the disability program and creates an environment that leaves the program susceptible to fraud and abuse. This type of culture can result in weakened internal controls, which allows fraud and abuse to continue and; not protecting the program for those who may truly need it in the future. Concentrating on paying benefits quickly instead of accurately does not support RRB's fiduciary responsibility to the railroad community, in ensuring the correct benefit amounts are being paid to the right people.

## **Challenge 2 – Information Technology Security and System Modernization**

With information technology (IT) security risks developing constantly, federal agencies, including RRB, are challenged as to how to modernize and maintain their systems in a secure environment. RRB is incorporating new technologies and enhancing existing ones, as well as implementing new systems to effectively strengthen and improve IT security projects and their overall modernization efforts. While OIG commends RRB for these efforts, there are still concerns that these efforts are not robust enough to adequately address innate risks involving IT security and developments.

RRB is continuing the effort and the process of undertaking major IT initiatives in the coming years, such as:

- modernization of RRB legacy systems;
- implementation of “Office in the Cloud” plan, technology offering a virtual office to a mobile workforce; and
- imaging system expansion for disability records.

The RRB considers these major IT developments initiatives as critical because the cost and resources needed to maintain the systems in the legacy environment are unsustainable. Additionally, RRB's desire is to mitigate cybersecurity risk; improve fraud prevention and detection abilities; and support a more effective, efficient, and leaner workforce.

Because of the difficulty in IT projects, acquisitions and modernization, GAO has continually included IT in its High Risk Series Report.<sup>12</sup> GAO reports that federal IT investments too frequently fail or incur cost overruns and schedule slippages, while contributing little to mission related outcomes; often suffering from a lack of disciplined and effective management, such as project planning, requirements definition, and program oversight and governance. In addition, GAO testified that the federal government has spent billions of dollars on these failed IT investments.

The RRB has embarked on a legacy systems modernization that is one of the largest IT projects ever undertaken by RRB and estimates the project to cost \$15.7 million. This modernization of the legacy systems is essential to sustaining agency operations. This project is expected to take several years during which approximately 12 million lines of code are to be translated to more modern computer language, followed by a systems reengineering project. However, based on a review of the fiscal year 2018 Capital Plan, the existing mainframe at RRB will reach the end of its useful life before the legacy systems modernization project is complete.

The Capital Plan states that RRB is to utilize the National Information Technology Center for its mainframe operations, temporarily, until the legacy systems modernization project is completed.

In fiscal year 2017, RRB contractors and subcontractors completed the code and data conversion of the Mainframe Taxation system. Additionally, approvals of the requisitions for Legacy Systems Modernization Services were coordinated and resulted in funding of \$718,418 for the project. RRB “Office in the Cloud Plan,” cloud technology for a mobile workforce, has long term considerations of cost and data access, as well as the risks involved in operating in a cloud environment. These types of projects of such size, length, security and costs can come at significant risks of cost overruns and can result in project failure, which are concerns of the OIG.

In a June 2017 audit report, OIG reported on information security at RRB.<sup>13</sup> The audit included testing the effectiveness of the information security policies, procedures, and practices of a representative subset of the agency's information systems; assessing the effectiveness of RRB's information security policies, procedures, and practices; and preparing a report on selected elements of the agency's information security program in compliance with OMB's fiscal year 2016 Federal Information Security Management Act (FISMA) reporting instructions. The audit determined that while RRB is continually making progress with the implementation of an information security program that fulfills the requirements of FISMA, they have yet to accomplish the task. RRB has not produced a fully effective security program with related information security policies, procedures, and practices. OIG issued 36 detailed recommendations related to the FISMA requirements not being achieved.

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<sup>12</sup> GAO, *High Risk Series: Progress on Many High-Risk Areas, While Substantial Efforts Needed on Others*, GAO-17-317 (Washington DC: February 2017).

<sup>13</sup> RRB OIG, *Fiscal Year 2016 Audit of Information Security at the Railroad Retirement Board*, OIG Audit Report No. 17-06 (Chicago, IL: June 16, 2017).

With IT projects creating a challenge for RRB, as well as a vast majority of other federal agencies, it is critical that a secure environment be established to strengthen and improve IT security. Cybersecurity is crucial because of the continual development of security and privacy risks that threaten agencies. As such, IT security oversight must be effective and efficient, as the environment's security is vital and essential to an agency's operations. Additionally, RRB's management of the secure environment and identification of vulnerabilities and threats to the environment, are crucial in the agency accomplishing its objectives and mission.

### **Challenge 3 – Management of Railroad Medicare**

Social Security Administration legislation in 1972 gave the RRB direct legislative authority to administer certain provisions of the Medicare program for Qualified Railroad Retirement Beneficiaries and active Railroad employees.<sup>14</sup> These provisions included enrollment, premium collection, and selection of a carrier to process Medicare Part B claims nationwide. RRB is responsible for administering its contract with Palmetto GBA, its Part B carrier. In fiscal year 2016, RRB withheld approximately \$600 million in premiums, and Palmetto processed about \$847 million in payments for services covered by Medicare Part B. Since 1983, the Centers for Medicare and Medicaid Services (CMS) has reimbursed RRB for Medicare program related work performed. This reimbursement was approximately \$30.9 million in fiscal year 2016.<sup>15</sup>

In 2016, OIG conducted an audit to determine if RRB's cost allocation plans and Medicare reimbursement calculations were accurate and supported in accordance with federal requirements. The audit determined that the controls to ensure the plans and reimbursement calculations were accurate and supported were not adequate and RRB's Medicare cost allocation policies and procedures were not effective in preventing errors. Labor costs were reimbursed based on management's professional judgment and indirect costs had not been formally approved by CMS. These weaknesses resulted in unsupported Medicare direct costs totaling approximately \$30.4 million and unsupported indirect costs ranging from \$9.5 million to \$33.8 million for fiscal years 2010 through 2014.<sup>16</sup>

The audit resulted in 26 recommendations to address the weaknesses identified. RRB's management concurred with 10 of the 26 recommendations. OIG was concerned by the significant nonconcurrence from RRB management and conducted subsequent discussions, but RRB management made no revisions in its official responses to the audit report.

Most of RRB's nonconcurrence was with recommendations that would require retroactive assessments of the accuracy of reimbursements received from CMS and

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<sup>14</sup> The Centers for Medicare & Medicaid Services (CMS), a branch of the Department of Health and Human Services (HHS), is the federal agency that runs the Medicare Program.

<sup>15</sup> RRB, *2017 Annual Report*.

<sup>16</sup> RRB OIG, *Railroad Retirement Board Did Not Calculate Reimbursed Medicare Costs In Accordance With Federal Requirements*, OIG Audit Report No. 16-10 (Chicago, IL: August 22, 2016).

have the potential to cause a violation of the Antideficiency Act.<sup>17</sup> OIG and RRB also have a fundamental disagreement on the applicability of and RRB's compliance with OMB Circular A-87. This circular established principles and standards for allowable cost reimbursements between governmental units that RRB was required to follow, based on its agreement with CMS.

OIG believes that RRB should take all necessary steps to implement these recommendations in order to assure the accuracy of prior and future reimbursements. In December 2015, RRB reported that a miscalculation had occurred resulting in its Medicare beneficiaries paying an incorrect reduced variable rate. At that time, RRB indicated it was not planning to collect any underpayments. After communication with OIG, RRB ultimately identified that 2,251 beneficiaries had underpaid premiums totaling approximately \$6 million. RRB reimbursed CMS for the underpaid premiums in June 2016. On November 21, 2016, RRB made a final decision to process a mass adjustment and write-off the beneficiaries' debts under Board Order 17-15. RRB told OIG it used the authority granted under Section 7(d)(1) of RRA to adjust Medicare premiums due to agency error and set the beneficiaries' premiums at the amount collected.

In addition, OIG is concerned that Railroad Medicare is not using the CMS Fraud Prevent System (FPS). Implemented in July 2011 by CMS, FPS is utilized by CMS to assist in reducing improper Medicare payments.<sup>18</sup> While FPS has been integrated with CMS contractor systems that process claims, it has not been integrated with the payment processing system used for Railroad Medicare claims. In 2016, Railroad Medicare was approved for onboarding to FPS, with implementation planned for December 2016 or January 2017. However, in October 2017, we were notified this onboarding still had not taken place.

The Railroad Medicare Program continues to be a challenge for RRB and a significant concern to OIG. Designated as a high risk area by GAO in 1990 due to its size, complexity, susceptibility to mismanagement and significant volume of improper payments; Medicare oversight is vital to its success.<sup>19</sup> OIG is concerned that RRB's Medicare program modernization plan has not been effective and recommends that RRB continue to improve controls and provide effective oversight over approximately \$847 million in Railroad Medicare payments made on behalf of its beneficiaries.

### RRB Management's Comments & Our Response

In RRB management's comments to this challenge, it reiterated that it believes the OIG's cost allocation audit was fundamentally flawed because the guidance used as the basis for review, OMB Circular A-87 (revised May 10, 2004), *Cost Principles for State*,

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<sup>17</sup> The Antideficiency Act is codified in several sections of title 31 of the United States Code (USC) including 31 USC 1341(a), 1342, 1349-1351, 1511(a), and 1512-1519.

<sup>18</sup> GAO, Medicare Fraud Prevention: CMS Has Implemented a Predictive Analytics System, but Needs to Define Measures to Determine Its Effectiveness, GAO-13-104 (Washington, D.C.: October 2012).

<sup>19</sup> GAO-17-317.

*Local, and Indian Tribal Governments*, provides guidance for grant recipients at the state, local and Indian tribal government level, of which RRB is not.

RRB is not a grant recipient, state, local or Indian tribal government. However, as it has done before, RRB management continues to intentionally omit a key fact—RRB’s Interagency Agreement with CMS requires that charges for services provided by the RRB will be based on actual, allowable costs as defined in A-87.<sup>20</sup> As such, the criteria used as the basis for the audit was appropriate and our findings in that audit are valid and require immediate action from RRB.

#### **Challenge 4 – RRB’s Continued Noncompliance with Improper Payments Elimination and Recovery Act (IPERA) and Assessing Payment Accuracy**

Since 2015, OIG has reported that RRB was not in compliance with the IPERA of 2010, which amended the Improper Payments Information Act of 2002 (IPIA).<sup>21</sup> In May 2015, OIG issued an audit report to assess RRB’s fiscal year 2014 compliance with IPERA. The audit determined that RRB was not in full compliance with IPERA reporting requirements.<sup>22</sup> Specifically, RRB did not comply with the risk assessment requirements because it did not assess risks for all of the programs that it administers. As a result, OIG was unable to assess compliance for the publication requirement for improper payment estimates for all of the programs and activities identified as susceptible to significant improper payments under the risk assessment. The audit also reported that improvements were needed for the RRA program and the Railroad Unemployment Insurance Act (RUIA) program, to ensure completeness of reported amounts for the RRA, as well as the accuracy of the reported improper payment amounts for the RRA and the RUIA programs. This includes the understatements and insufficient supporting documentation. RRB developed a risk assessment plan in response to the OIG’s determination that RRB was not in compliance with IPERA.

In May 2016, OIG determined that RRB remained noncompliant with IPERA for the second consecutive year, for the risk assessment requirement.<sup>23</sup> Specifically, risk assessment documentation did not meet the minimum requirements specified in OMB guidance.

OIG also determined that improvement was still needed to ensure the accuracy of reported improper payment amounts for RRA and RUIA programs because both programs reported understated amounts of approximately \$12 million and \$904,000. In addition, OIG identified other improper payment reporting deficiencies, which made RRB’s improper payments report incomplete.

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<sup>20</sup> Federal Management Circular 74-4 was reissued in 1981 as OMB Circular A-87 and codified as 2 CFR Part 225 in 2005. OMB has consolidated and streamlined its guidance located at 2 CFR Part 200.

<sup>21</sup> Public Laws 111-204 and 107-300.

<sup>22</sup> RRB OIG, *Audit of the Railroad Retirement Board’s Compliance with the Improper Payments Elimination and Recovery Act of 2010 in the Fiscal Year 2014 Performance and Accountability Report*, OIG Audit Report No. 15-06 (Chicago, IL: May 15, 2015).

<sup>23</sup> RRB OIG, *Audit of the Railroad Retirement Board’s Compliance with the Improper Payments Elimination and Recovery Act of 2010 in the Fiscal Year 2015 Performance and Accountability Report*, OIG Report No. 16-07 (Chicago, IL: May 13, 2016).

In May 2017, OIG issued a report on RRB's compliance with the IPERA that resulted in six recommendations.<sup>24</sup> For the third year of noncompliance with IPERA, OIG recommended corrective actions needed for improvement and implementation to ensure proper compliance with IPERA guidance.

The audit disclosed that two of the risk assessments prepared by RRB were not in accordance with the OMB guidance. In addition to not being in compliance with the risk assessments, improvement was needed to ensure that improper payment amounts are accurately being reported for the RRA and the RUIA programs. OIG found that some of the improper payment methodologies applied to the RRA and RUIA programs were not in accordance with OMB guidance, which creates a risk for RRB in not identifying all improper payments. OIG determined that improper payments for the RRA program were understated by approximately \$19 million. Furthermore, the OIG found that the records used by the agency to support the RUIA program improper payment data was not always maintained and updated in accordance with agency guidelines. The audit resulted in six recommendations to management outlining the corrective actions needed because of noncompliance for the third year with IPERA as specified in OMB issued guidance. Two of the six recommendations were: the revision of the projection methods used for the underpayment component of the reported overall improper payment amount for the RRA program; and improvement of RRB documentation used to support the RUIA reported improper payment data to ensure that it is maintained and updated in accordance with agency guidance.

In response to the six recommendations, RRB Management concurred with three and did not concur with the remaining. The Bureau of Fiscal Operations (BFO) did not concur with the recommendation outlining the corrective actions required for the third year of noncompliance with IPERA. Management stated that the risk assessments were revised to comply with OMB guidance prior to the issuance of this audit report, however, the OIG's determination of noncompliance remained unchanged. The Office of Programs did not concur with the recommendation for revision of projection methods used for the underpayment component of the overall reported improper payment amount for the RRA program. Management stated that it believes that its current methodology is more accurate in applying improper payment percentages than previous methodologies used.

OIG considers the projection method as stated in the finding is the most accurate estimation process for initial and post underpayment accruals and believes that with Management's nonconcurrence, improper payments will continue to be understated and inaccurately reported. RRB asserts that it is compliant with OMB IPERA guidance due to their methodologies being approved by OMB and supported by two of the RRB Office of General Counsel legal opinions, with which OIG disagrees.

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<sup>24</sup> RRB OIG, *Audit of the Railroad Retirement Board's Compliance with the Improper Payments Elimination and Recovery Act of 2010 in the Fiscal Year 2016 Performance and Accountability Report*, OIG Report No. 17-05 (Chicago, IL: May 12, 2017).

Lastly, the Office of Programs did not concur with the recommendation for improvement of RRB documentation used to support RUIA reported improper payment data to ensure that it is maintained and updated in accordance with agency guidance. Although RRB management did not concur, they have reported that they have taken corrective measures. OIG has yet to evaluate the corrective actions and are unable to evaluate their sufficiency.

Fiscal year 2016 was the third consecutive year that RRB was deemed noncompliant for the same programs or activities, and IPERA guidance states that the agency must submit reauthorization proposals for each discretionary program or activity that has not been in compliance for three or more consecutive years, or proposed statutory changes to bring the program or activity into compliance. IPERA compliance continues to remain a challenge for RRB given that the policies and procedures developed for IPERA risk assessments were incomplete. This directly impacts the risk assessments prepared for the various programs that it administers. The OIG's concern is that RRB is not being proactive when it comes to improper payments and compliance with IPERA guidelines, which continues to result in the underreporting of improper payments.

In August 2017, OIG published an audit report “Improvements Needed for the Program Evaluation Process at the Railroad Retirement Board” that resulted in 21 recommendations for deficiencies in the process.<sup>25</sup> The audit was conducted to determine the adequacy of RRB program evaluation process as it relates to its reviews of accuracy and integrity of benefit payments. The audit identified numerous weaknesses and areas where improvements were needed. The audit report correlates RRB’s vulnerabilities in assessing payment accuracy with the continuation of RRB being in noncompliance with IPERA.

The audit found deficiencies in the adequacy of the program evaluation process used in assessing the accuracy and integrity of RRA benefit payments and determined that improvements were required in several areas. The areas where corrective action is needed are as follows:

- quality assurance sample universe selection process, reported sample results, supporting documentation, and related policies and procedures;
- documented internal controls, and tests of controls;
- completeness of samples to include cases without recent adjudicative actions;
- efficiency in the manner that data is compiled and reviewed that supports reported accuracy rates;
- agency actions to ensure that they are in compliance with agency policies and procedures;
- validation of performance measures prepared by other RRB organizational units;

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<sup>25</sup> RRB OIG, *Improvements Needed for the Program Evaluation Process at the Railroad Retirement Board*, OIG Audit Report No. 17-07 (Chicago, IL: August 1, 2017).

- documented checklists that support occupational disability compensating control results; and
- ongoing training for Program Evaluation Section claims specialists.

A reliable and accurate program evaluation process is imperative for identifying improper payments and their root causes, so action may be taken to prevent improper payments in the future.

### RRB Management's Comments & Our Response

RRB asserts that it is compliant with OMB IPERA guidance and the definition of improper payments because their methodologies were approved by OMB and based on two RRB Office of General Counsel legal opinions, which support this determination. We disagree with this conclusion.

Under IPIA, an improper payment is “any payment that should not have been made or that was made in an incorrect amount (including overpayments and underpayments) under statutory, contractual, administrative, or other legally applicable requirements.” RRB continues to assert that certain payments it makes, which are subsequently determined to be erroneous because of additional information being reported, are not improper. This conclusion is incorrect and counter to the legal definition of an improper payment and OMB guidance. One fundamental purpose of improper payment identification and reporting is to identify the root causes of improper payments in order to prevent them in the future. By disregarding these improper payments, RRB does not place adequate attention on identifying the root cause of such improper payments and minimizing them in the future. We disagree that the RRB’s improper payment definition and methodology for RRA and RUIA underpayment cases is in compliance with OMB guidance and IPIA.

### **Challenge 5 – Human Capital Management**

Human capital management is the process to acquire, train, and manage the skills of the workforce to advance an organization’s mission and goals. As part of its human capital management process, an agency must continually review its plans to retain employees and elevate the skills of the existing employees allowing them to effectively contribute to the organization. Succession planning is key to the continuing and uninterrupted operations of an agency.

In July 2017, Office of Personnel Management (OPM) issued a human capital (HC) management evaluation of RRB.<sup>26</sup> The evaluation was conducted because of two critical human capital challenges that RRB is facing; an increasing retirement eligibility rate due to an aging workforce and high field office turnover rates. In addition to assessing RRB’s response to these two challenges, OPM assessed compliance with legal and regulatory HC program requirements, evaluated whether HC programs are operating

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<sup>26</sup> U.S. Office of Personnel Management, *Human Capital Management Evaluation Railroad Retirement Board* (Washington DC: July 19, 2017). RRB has until December 2017 to reply with its comments to this report.

efficiently and effectively, and identified any strengths or vulnerabilities in RRB's HC programs. The areas covered included workforce planning, talent management, results oriented performance culture, and leadership and knowledge management.

OPM found that several RRB HC practices were noncompliant, lacked measures of effectiveness, and exposed RRB to risks of prohibited personnel practices and other regulatory violations. The deficiencies were largely due to weakened accountability practices in RRB talent and performance management programs.

This was a result of outdated policies and current management-labor practices, which created conflicts with legal and regulatory requirements, including merit system principles. OPM stated that RRB needs to take concrete steps towards modernizing processes, implementing efficient practices, and more effectively managing its greatest assets, a loyal and high-quality workforce.

RRB, like most federal agencies, is confronted with a significant portion of its workforce currently eligible to retire or eligible in the near future. RRB's Bureau of Human Resources estimated that, by fiscal year 2018, almost 30 percent of personnel will be eligible for retirement, with approximately 50 percent having 20 years or more of service.<sup>27</sup> In addition to retirement among personnel, RRB has experienced high turnover in its leadership. The agency is overseen by a three member Board, including a Chairman. The Office of Chairman has been vacant for two years since the retirement of the Chairman on August 31, 2015.

In addition to the Chairman retiring, RRB has experienced multiple retirements and separations of its senior executive staff. One major priority for the agency's leadership will be to ensure the transfer of knowledge to guarantee continuing and uninterrupted operations of the agency.

With succession planning, an agency can identify potential leaders with the skills and abilities to fill vacant positions or develop them for advancement to vital roles in the organization. In developing a successful succession plan, the strategy must ensure that employees are consistently being developed to move into key roles.

In September 2011, OIG reported that RRB had identified staff attrition as an ongoing concern.<sup>28</sup> The report also stated that these changes would impact every aspect of the agency's operations, to include senior level management. While RRB has a Human Capital Management Plan and Succession Plan, it has not been funded. Also, while the plan identified RRB's need to maintain and replace employees, the impact of declining budgetary resources was not considered.

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<sup>27</sup> RRB, *2017 Annual Report*.

<sup>28</sup> RRB OIG, *Office of Inspector General's Proposal to Improve Business Efficiency at the Railroad Retirement Board*, (Chicago, IL: September 21, 2011).

OIG concluded that RRB management should enhance the plan by evaluating the possibility of staff and financial reductions and then by establishing a contingency plan to address staff and funding necessities for plan readiness.

While attrition presents a significant challenge, it also presents a unique opportunity for RRB to change its culture. RRB's culture focuses on paying benefits quickly, increasing the likelihood of erroneous payments in its benefit programs; a foundational flaw that leaves RRB's program susceptible to fraud and abuse. One way to make significant and timely change to an agency's culture is through the introduction of new personnel who provide new ideas and talents, different views, and a willingness to question the status quo.

RRB should take advantage of its attrition and turnover to recruit and train new employees to assist the agency in promoting new perspectives. With the incorporation of new employees, the addition of innovative and different viewpoints are presented along with new skills and approaches, which can alter the agency's culture.

#### RRB Management's Comments & Our Response

In RRB management's comments to challenge 5, Human Capital Management, RRB stated that our statement that OPM had conducted its audit because of the employee turnover rate and aging workforce at RRB was incorrect. However, in its report, OPM stated that "RRB is faced with two critical human capital challenges: an increasing retirement eligibility rate due to an aging workforce, and high field office turnover rates." They went on to say that "[p]artly because of these two challenges, OPM decided to conduct a human capital (HC) management evaluation this year." Additionally, OPM stated that the evaluation also served to assess RRB's compliance with legal and regulatory human capital program requirements, evaluate whether human capital programs are operating efficiently and effectively, and identify any strengths or vulnerabilities in its human capital programs.

#### **Challenge 6 – Material Weakness Related to the Financial Statement Reporting and the Control Environment**

OIG is mandated to audit RRB's consolidated balance sheet, as well as the related statements of net cost, changes in net position, budgetary resources, the statement of social insurance, the statement of changes in social insurance, and the related notes to the financial statements. RRB management's responsibility is the preparation and fair presentation of said financial statements in accordance with accounting principles generally accepted in the United States of America. Upon RRB's completion of these financial statements, OIG is responsible for expressing an opinion on the financial statements, which are based on the audit being conducted in accordance with the auditing standards generally accepted in the United States of America.

OIG reported a material weakness for financial reporting for fiscal years 2014, 2015, and again in 2016. During the 2016 audit, OIG continued to identify material transactions that were recorded without sufficient supporting documentation, which were a result of RRB's management not implementing corrective actions to address prior OIG recommendations. In addition, OIG found numerous transactions, representing approximately \$14.2 billion that did not have adequate supporting documentation when they were recorded and approved in RRB's financial reporting system. Once notified, Bureau of Fiscal Operations staff provided the missing documentation for validation, but did not update the official records to include the missing documents. After subsequent communication between OIG and BFO management, a revision was made in BFO procedures allowing additional documentation to be added without altering any aspect of the previously recorded transactions. BFO also revised other sections of its procedures in an effort to address the OIG's recommendations relating to this material weakness. However, the determination by OIG was that the actions taken were not sufficient and additional corrective actions are needed to address these internal control deficiencies.

The material weakness for financial reporting, which includes ineffective controls and a lack of communication with the National Railroad Retirement Investment Trust's (NRRIT) auditor, continues to exist. The lack of communication with NRRIT's auditor has resulted in the OIG's continuous rendering of a disclaimer opinion for RRB's financial statements since 2013. This lack of cooperation and communication has prevented OIG auditors from obtaining sufficient appropriate audit evidence regarding RRB's financial statements.

OIG reported a new material weakness. Specifically, in fiscal year 2016, OIG determined that RRB's control environment may have a detrimental effect on RRB's financial statements.

OMB issued guidance defining management's responsibility for ensuring that an organization is committed to sustaining an effective control environment.<sup>29</sup>

The guidance explains five principles of the control environment and, if one principle is ineffective, management would be unable to conclude that the control environment is effective. The material weakness that OIG reported is based on an ineffective control principle, the enforce accountability principle, which states that management should hold individuals accountable for their internal control responsibilities. RRB management does not concur with this assessment and has not taken the necessary corrective actions to address several significant matters. As such, we are concerned that ongoing noncompliance with applicable laws, regulations, and authoritative guidance could impact the reliability of financial reporting at RRB and at governmentwide levels. In addition, RRB management does not always communicate matters of audit significance with RRB OIG auditors and RRB management had not responded to numerous requests to reconsider its determinations and to discuss most of the matters detailed in

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<sup>29</sup> Office of Management and Budget, *Management's Responsibility for Enterprise Risk Management and Internal Control*, M-16-17 (July 15, 2016).

this finding. According to the American Institute of Certified Public Accountants (AICPA) guidance, inadequate two-way communication could indicate an unsatisfactory control environment, thereby impacting the risk of material misstatements.<sup>30</sup>

NRRIT was established in 2001 by the Railroad Retirement and Survivors' Improvement Act 2001 (RRSIA). NRRIT's sole purpose is to manage and invest railroad retirement assets. The RRSIA authorizes NRRIT to invest railroad retirement assets in a diversified investment portfolio in the same manner as those of private sector retirement plans.

One of the most significant concerns involves ownership of NRRIT net assets. NRRIT's net assets represented \$25.1 billion or approximately 80 percent of the total assets reported for fiscal year 2016. Approximately \$1.4 billion was transferred in 2016 from NRRIT to the U.S. Treasury for the payment of railroad retirement benefits throughout the year. RRB indicated that it has no ownership interest in NRRIT in its assertion that NRRIT should be classified as a disclosure entity for financial statement reporting purposes under new Federal Accounting Standards Advisory Board's Statement of Federal Financial Accounting Standards 47 (SFFAS 47), *Reporting Entity*.

OIG disagrees with RRB's assertion and believes that NRRIT should be classified as a consolidating entity. The classification determination ultimately decides whether NRRIT's net assets will continue to be included in RRB and governmentwide financial statements beginning in fiscal year 2018 when SFFAS 47 becomes effective.

Based on RRB's classification of NRRIT as a disclosure entity, the net assets would not be included, there would only be a footnote reference to NRRIT. If classified as a consolidating entity, the net assets would still be included in the financial statements. OIG is concerned with RRB's assertion that it does not maintain legal ownership to NRRIT held net assets.

Other OIG concerns, many of which are discussed in this document, are (1) lack of action or formal written response for our audit recommendation associated with NRRIT communication portion of the material weakness for financial reporting, (2) a change in the social insurance valuation date that will result in NRRIT savings of approximately \$200,000 in contract services expenses, which represents less than .3 percent of NRRIT's annual total expenses but will increase the workload for RRB's Bureau of the Actuary and Research, (3) lack of corrective action and acknowledgement for inaccurate Medicare cost reimbursements and nonadherence with applicable authoritative guidance, and (4) RRB management's inaccurate improper payment definitions, which continue to result in understated reported improper payments. In 2016, we noted one additional concern regarding the planned reclassification of a system from a major application to a minor one, however; management ultimately did not make this change.

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<sup>30</sup> American Institute of Certified Public Accountants (AICPA), AICPA Professional Standards, *The Auditor's Communication with Those Charged with Governance*, AU-C Section 260 (New York, NY: June 1, 2016).

The material weakness in control environment does not only apply to financial statement reporting, but is found in other areas. In April 2017, OIG issued a report related to RRB's compliance with the Federal Travel Regulation (FTR).<sup>31</sup> This audit was conducted to determine if RRB was in compliance with the FTR and implemented and enforced adequate internal controls. The audit revealed that RRB did not always comply with the FTR because internal controls were not always enforced or adequate. OIG made 19 recommendations that related to improving, strengthening, enforcing, and conducting training on RRB's travel policies and the travel management system.

In this report, there were several significant findings related to the Board whose travel policies and procedures for their staff tend to be less stringent and much less likely to be enforced. These policies and procedures, titled "Board Orders", allowed Board Members and subordinate staff to approve travel for themselves, their respective staff, and to authorize their own travel vouchers. Agencies are permitted to establish their own travel policies and procedures as long as they are compliant with the FTR. However, because so many of these findings related to the Board's travel, it further brings into question the agency's leadership and their contribution to the RRB's weakened control environment.

GAO's internal control standards state that the oversight body and management should demonstrate a commitment to integrity and ethical values. One attribute of this principle is "Tone at the Top," which contributes to the design, implementation, and operating effectiveness. This principle conveys that management should demonstrate the importance of integrity and ethical values through their directives, attitudes, and behavior. Agency management, who is ultimately responsible for setting the tone at the top, should demonstrate and communicate these values that will create a culture by which all employees will adhere.

#### RRB Management's Comments & Our Response

In RRB management's comments on challenge 6 regarding the financial reporting material weakness, RRB stated that they reject the characterization that "...transactions, representing approximately \$14.2 billion, did not have adequate supporting documentation when they were recorded and approved..." They went on to say [t]hat statement is patently false." In addition, RRB stated that the supporting documentation for the referenced transactions was not missing but in fact, available for review in hardcopy and was promptly provided upon request.

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<sup>31</sup> RRB OIG, *Audit of the Railroad Retirement Board Did Not Always Comply with the Federal Travel Regulation*, OIG Audit Report No. 17-04 (Chicago, IL: April 11, 2017).

RRB excluded from its response that, according to its Accounting Procedures Guide, supporting documentation is required to be input into FMIS by the preparer of the transaction before being provided for review. As such, the information not being in FMIS is in direct conflict with its stated procedures. Further, when we sought the supporting documentation, RRB took up to 17 days to respond. We do not deem this as the documentation being promptly provided. Given that RRB procedures require documentation be in FMIS before review, the documentation was not in FMIS, and RRB took up to 17 days to provide the documentation; we disagree that our statement was “patently false,” as the evidence supports our finding.

In the RRB management’s comments on challenge 6 regarding the OIG’s determination of a control environment material weakness, RRB disagreed with the OIG assertion. RRB management stated that the material weakness for the control environment is unfounded due to insufficient evidence and stated that the OIG did not provide evidence that management’s accountability enforcement mechanisms were evaluated.

OIG disagrees that the material weakness is unfounded and stands by the documented finding regarding this matter and the numerous examples that support the material weakness. RRB management cites a portion of the Government Accountability Office’s *Standards for Internal Control in the Federal Government* regarding accountability mechanisms, such as performance appraisals and disciplinary actions. These are examples of accountability enforcement, not the only type of accountability measures. Deficiencies can be noted because management does not take necessary corrective actions. The oversight body is to oversee evaluation of the significance of the deficiency to ensure that it has been properly considered.

As previously stated, RRB management has not taken the necessary corrective actions to address the high level, monetarily significant matters detailed in our finding that could impact protection of customer trust funds and reliability of financial reporting for the RRB.

### **Challenge 7 – Lack of RRB Oversight of the National Railroad Retirement Investment Trust**

NRRIT was established by the RRSIA to manage and invest railroad retirement assets. As a tax-exempt entity, NRRIT is independent of the Federal government and authorized to invest the federal assets entrusted to it in a diversified investment portfolio in the same manner as private sector retirement plans. NRRIT is also responsible for transferring funds to RRB to pay benefits that are not funded through current tax receipts from railroad employees or employers. Approximately \$25.1 billion in assets were invested by NRRIT on behalf of railroad retirees and their families at the end of fiscal year 2016.<sup>32</sup>

OIG continues to express concerns that the oversight of NRRIT is inadequate. OIG contends that oversight and transparency of NRRIT could be improved if independent

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<sup>32</sup> RRB, *Performance and Accountability Report, Fiscal Year 2016* (Chicago, IL: November 2016).

performance audits were conducted in full compliance with GAGAS, along with IT audits, independent investigations, financial evaluations, and risk assessments, as appropriate and equivalent with Employee Retirement Income Security Act (ERISA) covered plans.<sup>33</sup>

The following outlines the specific challenges related to NRRIT.

### Performance Audits

NRRIT has commissioned four external reviews since its creation, with the first being in 2004 and the most recent in 2012, but has not established an objective and independent policy for conducting performance audits. There is no indication that the reviews commissioned by NRRIT were performed in accordance with GAGAS, which provides a framework for conducting high quality audits. NRRIT also self-selects the areas to be audited, which is a major concern. Other comparable federal programs, such as the Pension Benefit Guaranty Corporation's single-employer insurance program and the Thrift Savings Plan, are subjected to externally initiated and conducted performance audits by one or more independent oversight organizations. In contrast, to these entities, NRRIT selects the objective and scope of its reviews.

OIG believes NRRIT's self selection of review decreases the independence of the reviews and prevents thorough oversight to fully protect RRB assets held by NRRIT. OIG opposes any arrangement that allows NRRIT to control the performance audits. It is also the OIG's opinion that a statutory amendment requiring performance audits would have greater effectiveness, since NRRIT could not opt to alter the policy without legal justification.

In May 2014, GAO publicly released a report on RRB's oversight and communications with NRRIT and the periodic performance audits that NRRIT elected to authorize, but had no written requirement to conduct.<sup>34</sup> GAO reported that the four external reviews commissioned encompassed a wide range of issues including, the accuracy of monthly reports, compliance with NRRIT investment manager hiring policies, processes to ensure accuracy of financial recordkeeping and internal controls, the adequacy of due diligence procedures and the role of non-traditional investments but that these performance reviews differed from comparable entities in scope and frequency. GAO reported that the large majority of state pension plans and two federal programs they reviewed that manage investment assets are the subject of performance audits that are initiated and conducted by an external entity, and some of these audits have addressed issues including ethics and conflicts of interest, that the NRRIT commissioned audits have not included. Forty-two of the fifty state plans are subject to performance audits conducted by an external auditor, such as the Auditors General or equivalent, which reviews their plan annually; while other plans are audited less frequently. Both federal

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<sup>33</sup> GAO, *Government Auditing Standards, 2011 Revision*, GAO-12-331G (Washington, D.C.: December 2011).

<sup>34</sup> GAO, *Retirement Security, Oversight of the National Railroad Retirement Investment Trust*, GAO-14-312 (Washington DC: May 2014).

plans reviewed are also subject to externally initiated and conducted performance audits.

While the report did not contain any formal recommendations, it did list options for enhanced NRRIT oversight including:

- granting the OIG authority to conduct performance audits, which would ensure that these reviews are initiated and performed independent of NRRIT;
- requiring periodic audits with external input on scope, which would ensure NRRIT performance audits continue; and/or
- establishing an office of internal audit, which could ensure performance audits are independently initiated and conducted.

After the release of the GAO report, NRRIT signed a Memorandum of Understanding (MOU) with RRB in October 2014 to delineate responsibilities and procedures for (i) Financial Audits and (ii) Performance Assessment Evaluations with respect to assets held by NRRIT.

This MOU states that “performance reviews should be regularly scheduled every three years beginning in calendar year 2015, with the understanding that additional reviews could be scheduled, if warranted.”<sup>35</sup>

Although the MOU clearly states that NRRIT has agreed to these performance reviews, there has been no indication that any NRRIT performance reviews have been initiated since the signing of the MOU in 2014, and the MOU does not require them to be performed. GAO’s options could be adopted through either formal agreement between the key parties or through mandating ERISA compliance legislation.

#### Disclaimer of Opinion on RRB Financial Statements

As a result of OIG’s lack of access to NRRIT’s auditor, it has issued a disclaimer of opinion for fiscal years 2013 through 2016. OIG is required by law to audit the financial statements of RRB, and NRRIT is a significant component of RRB. In order to comply with the AICPA group financial statement auditing standard, OIG contacted NRRIT requesting direct communication with, and cooperation from, their auditor.<sup>36</sup> To date, there has been no communication or cooperation from NRRIT’s auditor, directly or indirectly.

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<sup>35</sup> Memorandum of Understanding between National Railroad Retirement Investment Trust and the United States Railroad Retirement Board signed in October 2014.

<sup>36</sup> AICPA, AICPA Professional Standards, *AU-C Section 600, Special Considerations - Audits of Group Financial Statements (including the Work of Component Auditors)* (New York, NY: June 1, 2013 through June 1, 2016).

Because OIG cannot obtain sufficient appropriate audit evidence with respect to NRRIT, we cannot issue an opinion on RRB's financial statements. To prevent future disclaimers of opinion, it is imperative that RRB management counsel NRRIT regarding its auditor's responsibilities to comply with the AICPA's group financial statement requirements.

OIG plans to continue oversight in all areas emphasized in this letter through audits, investigations, and other follow-up activities. We encourage RRB to take meaningful action on these challenges in order to prevent fraud, waste, and abuse in the programs and operations of RRB, and to reduce improper payments in all of its programs.

Martin J. Dickman  
Inspector General

### **Management's Comments**

These are Management's Comments on the Management and Performance Challenges identified by the Railroad Retirement Board (RRB) Inspector General (IG).

#### **Challenge 1 - Program Integrity to Strengthen Disability Programs**

In response to Office of the Inspector General (OIG) recommendations and ad hoc communications, as well as the Government Accountability Office (GAO) audit findings, and internal quality assurance reviews, the RRB has taken meaningful actions to improve the critical functions of the RRB's disability program. RRB's commitment to continuously improving the quality of systems, policies, procedures and processes that support disability decisions is clear. This has been demonstrated repeatedly over the past several years and documented in prior reports. While, in some instances the RRB did not agree with specific recommendations of the OIG, the RRB remains steadfast in its approach to administering the disability programs so as to maintain or improve program integrity and protect the Trust Fund.

While the IG indicates in his statement that the challenges his office has identified are based on recent audits, evaluations, and investigations, much of the information included in Challenge 1 relates to indictments issued in 2011 and court proceedings from 2013 regarding a physician assisted fraud scheme involving annuitants who worked for the Long Island Rail Road (LIRR). The comments below regarding Challenge 1 will first address current issues related to the disability program and will then address issues specific to the LIRR fraud conspiracy.

#### ***Current Disability Program Issues***

To address concerns regarding program integrity, the RRB established a Fraud Task Force comprised of subject matter experts, senior agency officials, and representatives from the Board Offices, charged with identifying and evaluating changes to the disability program which would enhance program integrity. To assist in this mission, a Disability Program Improvement Plan (DPIP) was developed, tracking activities related to 18 separate initiatives, with multiple tasks, many of which have been implemented, such as form revisions, enhanced examiner training, use of a second level authorizer, and tracking of physicians. The IG raises concerns that the due dates on the plan sometimes change and that some initiatives are closed, without being implemented. The due dates for the various tasks are subject to change depending upon availability of agency resources and budget. Further, the DPIP is a living breathing document and continues to evolve as initiatives are discussed, considered and developed. Regular meetings are held to evaluate and review the 18 initiatives to determine if they will enhance program integrity and/or agency processes. Initiatives which have been marked as closed have either been implemented or agreed by the Board members to not be implemented after agency reviews, assessments, discussions and further analysis.

Among the forms which have been revised are those forms used to obtain job information from railroad employers. While the OIG acknowledges RRB management's extensive revisions to, and intent to replace the current job verification forms (G-251a and G-251b) with a singular version, the OIG contends that voluntary completion of the forms is "incongruent with RRB regulations...." In support of this contention, the OIG has noted that the regulations of the RRB state that the RRB "shall also consider the employer's description of the physical requirements and environmental factors relating to the employee's regular railroad occupation, as provided on the appropriate form." Omitted from the regulatory citation is the fact that the regulations provide that examiners must also consider the employee's own description, as well as other

sources, such as the Dictionary of Occupational Titles. The intent of this regulation is to identify what information disability examiners should consider if available, not to mandate that employers must provide vocational information. This is not only apparent from the logical reading of the regulation, but was also emphasized when the policy was established in 1997. As noted at the time the procedure was introduced, it was to allow for employers to “offer the applicant’s railroad employer the opportunity to **voluntarily provide** [emphasis added] information on the applicant’s job duties which may be utilized in determining the applicant’s eligibility to an occupational disability.” Determining Disability, 62 Fed. Reg. 50056 (proposed Sept. 24, 1997) (to be codified at 20 CFR 220).

Although it was never envisioned that it would be mandatory for employers to provide vocational information, the RRB appreciates a need for the adjudicating staff to have an understanding of the various railroad occupations. Consequently, staff has attended classroom and onsite-training facilitated and led by industry representatives to aide in assuring that staff has an acceptable understanding of the functions of the various railroad occupations.

In response to a suggestion from the IG, the RL-8A, *Occupational Disability Certification*, was developed and implemented. This form requires recipients to self-certify their continued entitlement to a disability annuity, by providing current information regarding their impairments and work activity. The IG is critical of the manner the RRB has implemented the form, asserting that its use is too narrow and that completion of the form should be required of all occupational disability annuitants. Including all 21,000 occupational annuitants in an RL-8A certification process as the IG suggests would be unduly burdensome and unnecessary, as well as impractical to monitor. The vast majority of disability annuitants are not working and are receiving a benefit to which they are legally entitled. Consequently, having all occupational disability annuitants complete the RL-8A would do little to enhance program integrity or deter fraud. Rather, the RRB has opted to use the form in a manner which allows for greater scrutiny of cases identified as potentially “high risk” based on the presence of certain factors.

The IG also asserts that “another program improvement that has not been fully implemented is action to prevent occupational disability adjudications based on the simple task standard for railroad employees.” RRB management disagrees. In response to OIG Alert No. 15-05, disability staff received refresher training on following the appropriate standard for occupational disability adjudication. This training included a review of how impairments are assessed to determine if an individual is disabled or not, as well as how to develop sufficient objective medical evidence to determine restrictions caused by impairments. These restrictions are then compared to essential job functions and a determination of whether the applicant can perform the job duties is made. The sequential evaluation process used in the training is found in 20 CFR 220.13(b)(2)(iv). These regulations are included in RRB’s Disability Claims Manual Part 13, along with the Independent Case Evaluation process where medical information is reviewed to establish the functional limitations of the condition. As functional limitations are established and job demands determined, the two are compared and reviewed to determine if the claimant is capable of performing the essential job duties of their regular railroad occupation. In summary, contrary to the IG’s claim that the RRB has failed to take action to assure that occupational disability annuities are not awarded to individuals based on an inability to perform a simple task, disability procedure had been reviewed to verify that it is accurate and disability staff was required to attend refresher training on the topic.

Finally, the IG continues to take exception to the grant rate within the disability program and is critical of what he describes as a culture concerned with “paying benefits quickly” with little regard to paying them accurately. However, he has provided no evidence to support his claims that the grant rate demonstrates that occupational annuities are being awarded in error and

while it is not uncommon for benefit paying agencies to focus on timeliness, statistical data reflects that benefits are certainly not being awarded quickly.

The RRB acknowledges that a high grant rate in a disability program could be indicative of problems in the decision-making process. However, as is the case with the RRB's occupational disability program, it could also be the result of a range of factors specific to the disability program. In calendar year 2015, there were approximately 97.6 percent occupational disability allowances along with approximately 79.5 percent total disability allowances under the Railroad Retirement Act. Of those granted applicants, 78.1 percent of the occupational cases and 83.6 percent of the total cases were awarded a period of disability (disability freeze) under the Social Security Act. Approximately 67 percent of the disability freezes completed by the disability post section are joint freeze cases that require coordination with SSA, thus resulting in a third party concurrence. Additional factors, which after consideration indicate that the grant rate does not reflect a problem in the decision-making process, include the average age and years of service of an RRB disability applicant, which is 58.3 years and approximately 27 years of service. This is relevant because railroad workers with 30 years of service are eligible for full age annuities as young as age 60 – as are their spouses, whereas the spouse of a disabled annuitant with less than 360 months of service is not eligible for an annuity until both parties are age 62, and that spouse annuity will be reduced for age unless the spouse defers retirement until attaining full retirement age (age 66 or 67, depending upon date of birth). In addition, the exertional level of typical railroad work for most applicants is in the moderate to high level, exacerbating the normal wear and tear on the body that occurs with aging. Also, employees who retire based on age typically retain their health insurance, whereas those who retire on disability prior to age 60 frequently do not.

Timeliness metrics are commonplace for benefit paying organizations, as are accuracy metrics. It is disingenuous for the IG to claim that the RRB's interest in the former demonstrates no concern for the latter. RRB's focus and culture clearly indicate a commitment to the quality of adjudicative decisions. RRB has set quality measures and, for three consecutive years, studied the quality of its disability determinations and acted upon findings. In fact, it is clear that the many process changes have negatively impacted the RRB's ability to timely deliver disability benefits to our deserving disabled constituents. The current timeliness goal for the Disability Benefits Division (DBD) was established in FY 2009. The performance standard requires an initial decision to approve or deny 70 percent of disability applications for benefits within 100 days of receiving the application. As indicated in the chart below, while DBD was close to achieving the performance goals in five of the eleven years, DBD has only achieved this goal three times: in FY 2008, FY 2012 and FY 2013. There was a significant drop in performance, beginning in FY 2014, after program improvements were initiated.

Customer Service Performance Indicator		FY 06	FY 07	FY 08	FY 09	FY 10	FY 11	FY 12	FY 13	FY 14	FY 15	FY 16
I-A-7 Disability Decision	Target	55.00%	63.00%	68.00%	70.00%	70.00%	70.00%	70.00%	70.00%	70.00%	70.00%	70.00%
	Actual	65.90%	69.60%	70.40%	62.50%	68.90%	67.50%	74.90%	72.50%	42.80%	31.00%	17.40%
Average Processing Time (APT)		92.1	85.3	85.5	97	90.2	92.3	84.5	87.6	132.5	179.2	248.1

The RRB strives to focus on paying the right people, in the right amounts, in a timely manner while preserving the integrity of the trust funds. Changes which have been implemented for program integrity purposes will need to be analyzed to assure that any resulting delay in the processing of applications is justified, and where no such justification is found, consideration must be given to appropriate modification.

### **LIRR Physician Assisted Fraud Scheme**

The LIRR physician assisted fraud scheme was first identified in 2007, followed by indictments in 2011 and court proceedings which took place in 2013. In total, 33 individuals either pled guilty or were convicted, including two physicians, two facilitators and 29 individuals who had been awarded an occupational disability annuity. The LIRR fraud scheme revealed systemic deficiencies in the RRB's disability program, but those deficiencies have since been addressed. The first deficiency identified was the failure of the RRB to notice that an unusually high number of disability applicants from the LIRR listed as a treating physician one of two names. This was because the RRB was not monitoring the identities of medical providers. This was initially remedied by training on how to independently identify similar situations, and then by the creation of the Disability Tracking of Physicians and Patterns (DTOPP) database. All treating source physicians are entered into DTOPP for cases adjudicated by DBD, allowing for statistically significant patterns to be identified through this database. The other systemic vulnerability identified was the failure of the RRB to notice that an unusually high percentage of applications filed with the RRB by individuals who worked for LIRR were filed on the basis of disability, rather than age and service. The RRB has addressed this issue by compiling data from a variety of existing sources so that statistically significant patterns in the filing of applications can be identified.

The IG asserts that the RRB has allowed individuals to commit fraud against the disability program with no repercussions, and in doing so, encourages future fraud and abuse of the program. Such statements are without foundation and inaccurate, as demonstrated by the following information.

The 33 individuals charged in the scheme either pled guilty or were convicted at trial. They have been ordered to make restitution and are being monitored by the Clerk of the Court. In addition, individuals who were convicted were given prison sentences and those who pled guilty were sentenced to various terms of probation. The RRB receives regular reports detailing the amount collected from each individual. The RRB's Bureau of Fiscal Operations is in contact with the Financial Litigation Unit of the U.S. Attorney's office and is receiving payments from the Court.

The IG points out that "as of August 2017, only \$399,147 of the approximately \$5.9 million in court ordered restitution related to the LIRR convictions had been returned to the RRB." As was stated in a memorandum to the IG regarding this topic, dated August 17, 2017, "With regards to recovery of funds from the named defendants, the RRB is bound by the Sentencing Orders, Forfeiture Orders, and directions from the U.S. Attorney's Office, U.S. Marshal's Office, and/or the U.S. Probation Office. The RRB's Bureau of Fiscal Operations works with the Financial Litigation Unit as well as the Clerk of the Court with respect to receiving restitution payments made by the defendants." As the IG is aware, unless otherwise directed, RRB is precluded from offsetting any restitution. Additionally, the order of precedence in the sentencing documents states, "...pursuant to 18 U.S.C. § 3664(i), all nonfederal victims must be paid before the United States is paid." In the majority of cases, there are nonfederal victims, making the likelihood of the RRB receiving a distribution from the courts low.

An additional 45 individuals admitted to participating in the fraud scheme, but were not indicted. Rather, these individuals were allowed to participate in a voluntary program in 2012, the terms of which, at the suggestion of the Department of Justice, did not require repayment of prior annuities paid. The disability annuities for these individuals have been terminated. In addition, the RRB terminated prospective annuity payments for over 700 disability annuitants in 2013. These annuities were terminated because the application was awarded, in part, based upon

medical evidence provided by one of the physicians convicted of fraud. None of these individuals whose annuities were terminated in 2013 was indicted or participated in the voluntary program referenced above.

The IG has alleged that “potential” overpayments exist for each of the 700 individuals whose disability annuities were terminated in 2013, apparently on the premise that the original decisions to award these individuals annuities were obtained by fraud or similar fault. However, there is no evidence which would support the RRB taking such action. While the fraud conviction of the physicians was deemed sufficient to call the applications into question, the convictions on their own are not sufficient evidence to establish that the original applications were awarded based upon false or misleading information

### **Challenge 2 - Information Technology Security and System Modernization**

With ever increasing Information Technology (IT) security and privacy risks, we understand your concerns to make our IT systems and processes more robust. The RRB systems modernization is an iterative and incremental approach to show success with small projects, communicate these successes across the agency to gain support, and build confidence to accomplish the remaining larger critical tasks.

Our Mission Essential Functions are performed in a legacy Mainframe environment that is costly and extremely resource heavy to protect from increasing cyber threats. Our participation in the Department of Homeland Security Continuous Diagnostics and Mitigation (CDM) program will ensure that we will address these Cybersecurity risks. The CDM deployment roll-out is currently scheduled to start in December 2017 and to complete in May 2018. We have started the incremental and iterative process to transform our legacy Mainframe software systems, and with the anticipated funding in the coming Fiscal Years we will accelerate this transformation.

Without strong project management, it is true that complex projects with large federal IT investments frequently fail or incur cost overruns. To mitigate such risks, our Legacy Systems Modernization Services contract is a Firm Fixed Price (FFP) contract. The RRB will continuously monitor, measure and perform value driven services to ensure the predictable outcome of a successful migration. To achieve this successful migration we are implementing agile principles such as breaking up multi-yearlong projects into a series of short releases focused on the most critical or Key Performance Indicators to increase the opportunity for success, as well as ensuring frequent standup meetings, or daily scrums, as an effective means to convey information, and to facilitate quick resolution of identified risks and issues.

The iterative software development model delivers value and provides confidence from early repeated success, early risk mitigation and discovery, complexity management through simplification, relevant progress tracking leading to better predictability, higher quality and less defects, early and regular process improvement, prototyping, and feedback communication loops.

We are deploying all citizen-centric digital solutions using strong authentication. These external self-service solutions are being transformed to use secure communications with Multi-Factor authentication and identity management. We also understand the necessity to block unauthorized hardware from accessing the RRB network for effective Network Protection. Our enrollment in the CDM program will assist in this purpose.

We recognize that our Cybersecurity program is still in need of improvement. Our goal is to remediate Cybersecurity risks at the earliest. We will release a comprehensive Cybersecurity

strategy to address our deficiencies by December 2017. This will supplement the risk mitigation capabilities of EINSTEIN III (E3A) that the RRB currently has in place.

The agency's risk management and privacy strategy is to prevent and detect impending attacks through continuous monitoring. By modernizing the legacy applications, we ensure that the enterprise architecture is stable for years to come, is flexible to accommodate new innovations, and enables the encryption and security aspects to keep customer data safe. Adherence to National Institute of Standards and Technology (NIST) standards for encryption and Federal Information Processing Standards (FIPS) 140-2 for Data in Transit and Data at rest ensures enterprise network security outside of the RRB network. We anticipate that with the successful deployment of the CDM initiatives by May 2018, our Cybersecurity program will be more mature to stay one step ahead of the bad guys.

### **Challenge 3 - Management of Railroad Medicare**

Bureau of Fiscal Operations Response: The RRB believes that the OIG's Cost Allocation Plan (CAP) audit was fundamentally flawed and, therefore, requested that the OIG rescind the report.

The RRB believes that the OIG's CAP audit was fundamentally flawed because the guidance used as the basis for review, OMB Circular A-87 (revised May 10, 2004), ***Cost Principles for State, Local, and Indian Tribal Governments***, provides guidance for grant recipients at the state, local and Indian tribal government level. The RRB is not a grant recipient, nor is it a state, local, or Indian tribal government. The RRB has administrative responsibility under the Social Security Act for railroad workers' Medicare coverage and certain benefit payments. The RRB performs Medicare program-related work on behalf of the Centers for Medicare & Medicaid Services (CMS), U.S. Department of Health and Human Services (HHS) and, by virtue of an agreement between the RRB and the HHS, the RRB is reimbursed for that work.

While the RRB believes the audit was fundamentally flawed, the RRB is committed to enhancing the reimbursement process. During fiscal year 2018, the RRB will work with CMS to update our *Interagency Agreement* and to streamline RRB's *Cost Allocation Plan*.

Office of Programs Response: The Inspector General (IG) correctly reports on the error with respect to the miscalculation of Medicare Part B Variable Rate Premiums for the period 1989 through 2015. Once identified, RRB automated programs were corrected to prevent any future occurrences and the over \$6 million in underpaid premiums was reimbursed to CMS. Rather than attempt recovery of the underpaid premiums from the innocent beneficiaries, the Board determined in Board Order 17-15 (issued November 21, 2016) to waive recovery and not jeopardize their Medicare enrollment due to agency's error.

In the OIG's 2017 document, "Management and Performance Challenges Facing the Railroad Retirement Board" (page 12), the OIG states, "OIG is concerned that Railroad Medicare is not using the CMS Fraud Prevent System (FPS)." The RRB and Palmetto have been pursuing CMS' FPS implementation for the RRB's Specialty Medicare Administrative Contract (SMAC) since 2015. When CMS initially developed the FPS, the CMS limited access to FPS. As CMS gained more experience, FPS was expanded to more Medicare Administrative Contracts. During the initial meeting between the RRB, Palmetto and CMS, CMS recommended that the RRB and Palmetto wait until after the FPS re-compete process was finalized and the re-bid awarded before beginning the FPS implementation process for the RRB's SMAC. On a recurrent basis, both Palmetto and the RRB have reached out to CMS for status updates. In 2016, both the RRB and Palmetto were advised that CMS had approved the RRB's and Palmetto's request to use FPS. The on-boarding to FPS was set for December 2016 or

January 2017. In 2017, both the RRB and Palmetto were advised by CMS that on-boarding to FPS for new users has been delayed until the FPS upgrade to version 2.0 was completed. Further, CMS has delayed any on-boarding to FPS for new users until the new option year begins for FPS which is April 1, 2018. Both the RRB and Palmetto will continue to work with CMS toward utilization of FPS in 2018.

**Challenge 4 - RRB's Continued Noncompliance with Improper Payments Elimination and Recovery Act and Assessing Payment Accuracy**

Office of Programs Response: Since 2015, in response to OIG recommendations, we have made improvements in our improper payments analysis and reporting. We have reevaluated and improved our methodologies to ensure all appropriate areas are included in our improper payment computations for the Railroad Retirement Act (RRA) benefit program and improved our estimation of Railroad Unemployment Insurance Act (RUIA) benefit program underpayments by changing from a judgmental sample review of 20 cases to a statistically valid sample review of 100 cases. The Medicare program is now reflected in all appropriate tables and charts in the Performance and Accountability Report. We strengthened controls to ensure the accuracy of supporting data by improving our documentation and validation processes for the RRA and RUIA analysis and updated our procedures to reflect these enhancements to ensure that improper payment reporting is prepared in accordance with all applicable improper payment authoritative guidance. The enhancements resulted in successful close out of all open audit recommendations in these areas.

As stated previously in the RRB's FY 2016 Performance and Accountability Report and the FY 2017 OIG IPERA audit response, we would like to reiterate that RRB's categorization of underpayment accruals for both the RRA and RUIA programs are in full compliance with OMB's guidance and the definition of improper payments. Based on the Office of General Counsel's (OGC) Legal Opinion L-2015-54 dated November 20, 2015 (RRA), we made some modification to the categorization of various underpayment accruals found in our Quality Assurance review cases and therefore, are now in compliance. Based on the OGC's Legal Opinion L-2016-23 dated June 17, 2016 (RUIA), we obtained verification that our methodologies for categorization of underpayment accruals were already in compliance with IPERA. We therefore disagree with the OIG's May 2016 assertion that the RRB has understated RRA improper payments by approximately \$12 million and RUIA improper payments by \$904,000; the OIG has provided no specifics or computations to substantiate this statement. We also disagree with the OIG's May 2017 assertion that we have understated RRA improper payments by \$19 million. The OIG has completed no substantial data analysis of their own for estimation of initial underpayment accrual payments and merely offers an alternative approach using the data the RRB developed. Additionally, the RRB obtained OMB approval of our RUIA methodology in February 2014 and our RRA methodology in August 2016, further confirming that we are compliant with OMB IPERA guidance.

As part of our FY 2016 IPERA analysis and reporting, we updated our risk assessment documents for the RRA, RUIA, and Medicare programs to include the nine specific risk factors developed by OMB which are likely to contribute to improper payments. The OIG has determined that these risk assessments are compliant with IPERA. During FY 2017, we updated our risk assessments to include vendor payments and employee payments, which was done prior to the issuance of the OIG's most recent IPERA audit report.

In addition to the 2017 IPERA audit, the OIG also included in Challenge #4 a discussion of their FY 2017 audit report (17-07) on the Program Evaluation Process stating, "the audit report relates the continuation and the correlation of RRB being in noncompliance with IPERA and its

vulnerability in assessing payment accuracy.” The agency annually assesses payment accuracy for both the RRA and RUIA programs and both the RRA and RUIA risk assessments have in fact been found compliant with IPERA per the OIG, therefore, this correlation is unfounded. Based on the OIG’s recommendations in audit report 17-07, the agency has agreed to make improvements in the Program Evaluation process by adding the RRA and RUIA quality assessments as assessable units in the Management Control Review process, enhancing our controls and procedures for data gathering and documentation, ensuring appropriate officials are notified of all noncompliance errors, and providing ongoing technical and fraud awareness training opportunities.

Bureau of Fiscal Operations Response: In the referenced report, the OIG contends that the RRB is non-compliant because our previously submitted risk assessments for vendor and employee payment programs were not revised to address all risk factors included in the OMB guidance.

Revisions to the referenced risk assessments were completed in accordance with OMB guidance prior to issuance of audit report 17-05. However, the OIG did not evaluate them because the risk assessments were not published in the RRB’s FY 2016 Performance and Accountability Report. The risk assessments in question were published in the FY 2017 Performance and Accountability Report.

### **Challenge 5 - Human Capital Management**

Federal agency Human Capital/Human Resources policies and practices are evaluated on a periodic basis by another regulatory Federal agency, the Office of Personnel Management (OPM). For some agencies, OPM conducts a limited audit focusing more on an agency’s hiring decisions and adherence to merit system principles (to include job postings and veterans preference). OPM also has the authority to guide, enable and assess agency strategic human capital management processes and audit an Agency’s human capital system to include reviewing RRB’s Strategic Alignment, Leadership and Knowledge Management, Results-Oriented Performance Culture, Talent Management and Accountability. This type of audit is called a Human Capital Management Evaluation (HCME).

In October 2016, OPM was on-site at RRB conducting this more detailed Human Capital Management Evaluation. OPM was last on-site at RRB in 2011. Contrary to OIG’s statement, OPM was not conducting the audit because of RRB turnover rates or our aging workforce; rather, OPM was conducting a HCME in accordance with prescribed OPM timeframes. The HCME assesses the use of personnel management authorities at RRB, adherence to merit system principles, and compliance with human capital management laws and regulations. Overall, OPM provided 15 recommended actions and 7 required actions in the audit results provided to RRB in July 2017. Many of the required actions have been resolved and some of the recommended actions have been implemented and/or were currently in practice. In addition, given some of the required/recommended actions include changes to personnel policies, practices, and other matters affecting the working conditions of bargaining unit employees, the RRB recognizes its obligation to negotiate with our AFGE union accordingly.

There are some recommended/required actions in OPM’s evaluation for which RRB takes exception. Those will be addressed in our response to OPM which will be provided to OPM in December 2017. It is important to note that RRB has never been found in violation of merit systems principles since OPM has been conducting audits of RRB.

RRB recognizes that some of its internal Human Resources (HR) policies and practices need revision to better position human capital actions and practices, maximize employee performance and ensure alignment with agency mission. We continue to revise our staffing practices and procedures to ensure compliance with OPM regulations. In addition, we continue to provide salient Federal HR training to our HR staff to ensure relevancy and currency in rules and regulations.

Since at least 2015, RRB has instituted several human resources flexibilities and authorities within the Federal environment to include reinstituting a training and development section within our HR office. RRB also implemented a Learning Management System (referred to as RRB University). Through our LMS, we have developed and published several on-line training sessions as well as purchased an on-line catalog of more than 1,500 soft skill on-line training courses to help maximize growth opportunities for our current employees in expanding their knowledge, skills and abilities. In FY 2017, RRB provided more than 22 course offerings via classroom style training sessions on such topics as FERS retirement training to written communication skills. As testament to our success in bolstering the training options offered RRB employees, the 2017 Federal Employee Viewpoint Survey indicated a 10 percent increase (63 percent positive response) to the question, "My training needs are assessed," as well as a 10 percent increase (62 percent positive response) to the question, "How satisfied are you with training you receive for your present job?" RRB is in the process of revising our Awards program as well as our Performance Management System in an effort to maximize employee performance.

Although our Human Capital and Succession plans were not fully funded, we have been able to implement key aspects of these plans ensuring continuing and uninterrupted RRB operations. In 2016, RRB implemented its first Executive Candidate Development Program (ECDP). The ECDP is a year-long competency based leadership program consisting of formal leadership training and developmental assignments. Key training is developed around the Executive Core Qualifications (ECQ). Our first graduating class took place in October 2017. In addition, we utilize the re-employment of retirees to assist in retaining the knowledge of our specialized workforce and to assist in succession planning. While it is true that in the past five years, RRB has lost key leadership personnel through attrition, currently all but one of our SES level positions have been successfully filled (either internally or externally).

#### **Challenge 6 - Material Weaknesses Related to Financial Statement Reporting and the Control Environment**

The OIG continues to report a financial reporting material weakness. The OIG asserts that the financial reporting material weakness is the result of ineffective controls and differing interpretations of NRRIT oversight legislation. The differing interpretation of NRRIT oversight legislation provides the basis for the OIG's disclaimer opinion rendered for the RRB's financial statements.

In fiscal year 2017, the OIG continues to report that a second material weakness exists and cites concerns about the RRB's accountability enforcement/control environment as support. The OIG asserts that the "...RRB's control environment may have [emphasis added] a detrimental effect on RRB's financial statements..." It's important to note that the OIG asserts a second material weakness exists, that may have a detrimental impact on RRB's financial statements, without having quantified any effect on financial reporting or provided audit results from audits of RRB's accountability enforcement mechanisms. Therefore, the RRB rejects the material weakness.

Evidence cited to support the financial reporting material weakness: We reject the characterization that "...transactions, representing approximately \$14.2 billion, did not have adequate supporting documentation when they were recorded and approved..." That statement is patently false. Supporting documentation for the referenced transactions was NOT, as the OIG states, missing. The documentation was, in fact, available for review in hardcopy and promptly provided upon request as noted in OIG report of audit 17-03, *Fiscal Year 2016 Financial Statement Audit Letter to Management*. Further, the OIG did not take exception with the accuracy or completeness of the documentation the RRB provided to support the validity of the transactions.

Due to the volume of documentation, it was not stored in electronic format within the RRB's automated financial management system. The supporting documentation was stored in a manner that complied with the Government Accountability Office guidance, *Standards for Internal Control in the Federal Government* (GAO-14-704G). Page 48 of the Federal Internal Control Standards, under the heading "Appropriate Documentation of Transactions and Internal Control," states:

"Management clearly documents internal control and all transactions and other significant events in a manner that allows the documentation to be readily available for examination. The documentation may appear in management directives, administrative policies, or operating manuals, in either paper or electronic form. Documentation and records are properly managed and maintained."

As GAO requires, the documentation was readily available for examination.

Regarding communication with NRRIT auditors as the basis for disclaimer opinion: We have reviewed the Inspector General's concern. As the Inspector General is aware, section 15(j) of the Railroad Retirement Act provides that the National Railroad Retirement Investment Trust (NRRIT) "...is not a department, agency or instrumentality of the Government of the United States and shall not be subject to title 31, United States Code." Consequently, the NRRIT is not itself subject to Federal audit requirements contained therein. Therefore, contact between the Inspector General's office and the NRRIT auditors is inconsistent with the independent status of the NRRIT under section 15(j).

Further, RRB management believes the Inspector General is not required to issue a disclaimer of opinion on the RRB financial statements. Although the Inspector General is required by law to audit the RRB financial statements, the standards of the American Institute of Certified Public Accountants (AICPA) allow auditors to express a qualified opinion, rather than a disclaimer of opinion, where possible effects of undetected misstatements do not have pervasive effect on the financial statements. The RRB does not believe the Inspector General has established that any undetected misstatements in the context of the NRRIT audit are pervasive within the meaning of the AICPA standards. Accordingly, RRB does not believe the situation warrants a disclaimer of opinion on the RRB financial statements.

Regarding the control environment material weakness: The RRB disagrees with a material weakness the OIG asserts based on RRB's control environment. Moreover, the RRB believes that because the OIG has not quantified any impact on financial reporting, the cited material weakness is baseless and therefore, erroneous.

The OIG asserts that the RRB's control environment may have a detrimental effect on the RRB's financial statements and cites OMB guidance as the basis for the assertion. The cited guidance explains five principles of a control environment and, if one principle is ineffective,

management would be unable to conclude that the control environment is effective. The material weakness the IG reported is based on an ineffective control principle, the Enforce Accountability Principle, which states management should hold individuals accountable for their internal control responsibilities.

Per GAO's *Standards for Internal Control in the Federal Government*, management holds personnel accountable through mechanisms such as performance appraisals and disciplinary actions. Additionally, management takes corrective action as necessary to enforce accountability for internal control. These actions can range from informal feedback provided to the direct supervisor to disciplinary action, depending on the significance of the deficiency to the internal control system. The OIG has not evaluated RRB's accountability enforcement mechanisms, so how this provides a basis for a material weakness is disconcerting.

The following paragraphs contain examples the OIG provided as support for the asserted material weakness based on the Enforce Accountability Principle. Note, none of the examples demonstrate the OIG audited aspects of the Enforce Accountability Principle (i.e. mechanisms used to hold personnel accountable, such as performance appraisals and disciplinary actions).

1. Relative to NRRIT net assets ownership: As the IG knows, the RRB is awaiting decision from the Statement of Federal Financial Accounting Standards (SFFAS) No. 47 Steering Committee. Citing this as an example of a control environment deficiency is erroneous. Concern over NRRIT net assets is not related to the cited Enforce Accountability Principle.
2. Relative to response for audit recommendation associated with NRRIT communication: RRB's verbal response was consistent with GAO standards and therefore, does not support a material weakness. Citing this example as support for a material weakness based on Enforce Accountability Principle is erroneous and contrary to GAO auditing standards.

Further, the OIG acknowledged in a memorandum dated July 27, 2016, that the RRB's Chief Financial Officer (CFO) provided a verbal non-concurrence to their audit recommendation. Per GAO Auditing Standards, both verbal and written responses are acceptable. The RRB's verbal response complied with GAO propagated Government Auditing Standards, which allow for oral submission of comments. Therefore, the RRB did, in fact, provide a formal response consistent with GAO standards. Since RRB's verbal response was consistent with GAO's standard, the OIG citing this in support of a control environment material weakness is erroneous.

3. Relative to a change in the social insurance valuation date: As executive agent for the agency concerning financial reporting, the RRB's CFO concurred with NRRIT's request to adjust the social insurance valuation date from calendar year to fiscal year for financial and administrative purposes. The CFO reviewed applicable accounting standards and found no cause to deny the request. In addition, the CFO coordinated the request with OMB's policy office and received concurrence. Furthermore, this change was coordinated with the RRB's Bureau of the Actuary when proposed. Therefore, the RRB requested the valuation date change from calendar year to fiscal year, effective for fiscal year 2016 financial reporting period. This example does not demonstrate evaluation of the RRB's accountability enforcement mechanisms necessary to assert a material weakness based on deficient accountability enforcement.
4. Relative to Medicare cost reimbursements: While the RRB believes the OIG's audit was fundamentally flawed, and therefore requested that the OIG rescind their report, the RRB is committed to enhancing the reimbursement process. During fiscal year 2018, the RRB will

work with CMS to update our *Interagency Agreement* and to streamline RRB's Cost Allocation Plan.

This example does not demonstrate evaluation of the RRB's accountability enforcement mechanisms necessary to assert a material weakness based on deficient accountability enforcement.

5. Relative to improper payments definitions: RRB management rejects OIG's allegation that inaccurate improper payment definitions continue to result in understated reported improper payments. The RRB secured a legal opinion from its Office of General Counsel in FY 2016 and they agree with our classification of RUIA and RRA payments as proper. The RRB also received approval from OMB for our established methodologies to identify improper payments in the RRA and RUIA benefit payment programs. In August 2016, OMB granted the RRB approval to continue conducting the RRA Improper Payment analysis according to our established methodology. Please reference RRB management's more detailed response under "Management Challenge #4 (above)."

This example does not demonstrate evaluation of the RRB's accountability enforcement mechanisms necessary to assert a material weakness based on deficient accountability enforcement.

6. Relative to the OIG's Travel Audit: The OIG, using a statistically valid sample, evaluated all RRB Temporary Duty (TDY) travel for a six year period (2010-2015). Total TDY travel costs during that six year period was approximately \$3.2 million (average annual costs of approximately \$540,000). Neither the average annual amount, nor the six-year total dollar value, assuming a 100 percent error rate, are material to financial reporting. Therefore, by definition, citing this example in support of a material weakness related to financial reporting is erroneous. Additionally, this example does not demonstrate evaluation of the RRB's accountability enforcement mechanisms necessary to assert a material weakness based on deficient accountability enforcement.

#### **Challenge 7 - Lack of RRB Oversight of the National Railroad Retirement Investment Trust**

The National Railroad Retirement Investment Trust (NRRIT) is established by section 15(j) of the Railroad Retirement Act to invest funds from the Railroad Retirement Account that are not needed to pay current benefits. The Inspector General (IG) believes that the Railroad Retirement Board's oversight of NRRIT is inadequate and consequently recommends formal agreement between key parties or amendments to the Act to require independent performance audits, as well as other ERISA-type audits, evaluations, and assessments. The IG further recommends RRB management counsel NRRIT to allow the IG access to the NRRIT auditor. RRB management continues to believe the oversight of NRRIT is sufficient under current law.

The language of section 15(j) and the legislative history leading to its enactment clearly establish the intent of Congress to protect the assets of the Trust and NRRIT itself from political influence. Moreover, in the May 2014 GAO report concerning oversight of NRRIT (GAO-14-312) referenced by the IG, GAO specifically noted that NRRIT was independent of the federal government and exempted from the title 31 of the U.S. Code to protect it from political influence. Further, the GAO report stated that NRRIT is not without oversight beyond mandatory financial audits. In particular, GAO noted the Trust is monitored by the RRB and other federal agencies through regular reports and other communications. GAO also noted that NRRIT on its own

initiative commissioned four performance audits since 2002 which were comparable to and in some cases more comprehensive than those of comparable state pension plans.

Moreover, as also noted by the IG, in fiscal year 2015, the RRB and NRRIT entered into a Memorandum of Understanding (MOU) requiring performance reviews over three-year cycles beginning with calendar year 2015. Contrary to what is stated in the IG's report, per the terms of the MOU, NRRIT does not self-select the objectives and scope of the performance reviews without consultation with the RRB. The key subject areas and timeline, as well as scope of each audit, is only determined after **consultation between NRRIT and the RRB**. In addition, as we noted last year in our response to the IG's 2016 Management and Performance Challenges Report, and contrary to the IG's assertion in the instant report that "there has been no indication that any NRRIT performance reviews have been initiated since the signing of the MOU in 2014," in December 2015, NRRIT engaged the independent firm of KPMG to conduct the first audit under the agreement, on the topic of Corporate Governance Framework. In September 2016, NRRIT provided the RRB with a copy of the report and advised that the audit had identified no significant gaps in the corporate governance framework of NRRIT. NRRIT notes that it agreed with several auditor recommendations to strengthen existing governance policies and procedures. NRRIT appointed a Chief Compliance Officer to be responsible for a more formalized compliance program; expanded the Trust's Code of Conduct to Trustees; expanded the Conflict of Interest Policy; and formalized policies and procedures to define the risk assessment process and corresponding level of review which needs to be performed. In the near future, the RRB shall engage with NRRIT to consult on key subject areas, timeline and scope, among other issues, for the 2018 performance review. Accordingly, in RRB's view, the history of continuing cooperation between NRRIT and RRB on this and other matters renders any amendment recommended by the Inspector General unnecessary.