STATEMENT OF
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BEFORE THE SUBCOMMITTEE ON OVERSIGHT
COMMITTEE ON WAYS AND MEANS
U.S. HOUSE OF REPRESENTATIVES

March 4, 1997

Good Morning Madam Chair and Members of the Subcommittee. Thank you for inviting the Office of Inspector General (OIG) to discuss pension plan enforcement activities of the Department of Labor. I am here in my capacity as Deputy Inspector General to present the views of the OIG, which may not necessarily be representative of those of the Department of Labor.

It is the opinion of the OIG, Madam Chair, that ensuring that pension assets are safeguarded is an area that continues to require major departmental and congressional attention. So I thank you for your interest in holding this hearing to further explore this issue. As you may be aware, current pension plan assets now total close to $3.5 trillion. Because of the nature of these assets -- large sums of dollars, entrusted for deposit and long-term investment for a future benefit -- the potential for serious abuses exists. And no-one is really exempt from becoming a victim. Our criminal investigations of pension plan fraud demonstrate that the people being defrauded come from all walks of life. It does not matter whether you are a truck driver or a roofer contributing to an union pension fund or whether you are a Member of Congress.

The Department must be effective in ensuring that pension funds are deposited fully to workers' accounts in a prompt manner and that these funds be safe while held in trust. The problem of pension asset fraud and abuse is of such importance that the Department of Justice has launched an initiative to increase prosecution of pension-related cases.

Jurisdiction

By way of background, oversight responsibility over the various aspects of the Nation's pension system and assets rests with four Federal agencies: the Department of Labor's Pension and Welfare Benefits Administration (PWBA); the Internal Revenue Service (IRS); the Pension Benefit Guaranty Corporation (PBGC); and the Department of Labor, Office of Inspector General (OIG).

PWBA is responsible for administering Title I of the Employee Retirement Income Security Act 1974 (ERISA), which governs the rights and financial security of

employee benefit plan participants and beneficiaries in the Nation's private pension and welfare benefit plan system. PWBA's responsibilities include the promulgation of regulations, providing interpretations of ERISA, and the enforcement of the provisions found in Title I. The IRS is responsible for the enforcement of ERISA's Title II tax-related provisions, while PBGC is responsible for Title IV, which provides Government insurance in the event of failure of certain types of pension plans. Title III of ERISA provides the framework for all of the agencies to coordinate their activities.

Under the Inspector General Act of 1978, as amended, the OIG has oversight responsibilities over PWBA's programs and operations. Over the years, the OIG has conducted audits to identify weaknesses in the system and to make recommendations to improve the oversight of the Nation's pension assets. In addition, the OIG is the investigating unit within DOL for criminal labor racketeering and organized crime matters, and thus, some of the OIG's investigative jurisdiction regarding employee benefit plans overlaps that of PWBA. Within our jurisdiction, we conduct investigations into: (1) labor-related criminal conduct involving unions and/or industries with demonstrated ties to, or influences by, known organized criminal groups, whether they be traditional organized crime groups or newer, non-traditional groups; and (2) significant, prolonged, systematic and related criminal conduct and may be categorized as labor racketeering.

Ensuring Pension Funds are Fully and Appropriately Deposited

A serious problem that has been identified in the pension area is that of ensuring that contributions withheld from employee paychecks are appropriately and promptly deposited by employers. The Department has taken steps to help ensure this by making regulatory changes that reduce the time from which contributions are withheld or paid by the employee and received by the employer and the time the contribution is considered a plan asset. While these regulations reduce the time in which someone could temporarily use the pension funds inappropriately and then deposit the funds without being detected, they will not prevent individuals inclined to do so from converting funds for their own use. That type of activity needs to be addressed through an aggressive criminal enforcement program. In fact, the Government continues to identify instances of employee pension contributions not being deposited properly or funds diverted for the personal use of those administering the assets. The OIG is of the opinion that enforcement and oversight of this area needs to remain a priority of the Department.

Last week, my office issued an audit of the Department's employee contribution project (ECP). This project was initiated by PWBA in May 1995 to address plan administrators' failure to remit employee contributions to 401(k) pension plans and health plans. The purpose of the OIG audit was to determine if the Department, through the ECP, is adequately addressing the area of employee contributions to

ensure that funds in those plans are safeguarded from unscrupulous plan administrators.

Our audit found that PWBA's efforts in this project had a positive impact in protecting plan assets, particularly with respect to increasing enforcement in this area as well as participant awareness of the problem. The latter was evidenced by a significant increase in participant complaints to PWBA. However, we also found that improvements were needed in the targeting of this enforcement initiative as well as in their Case Management Information System. The audit found that PWBA had not focused its investigative resources on plans with the most serious potential for abuse. We attributed this ineffective targeting to the fact that PWBA left the development of enforcement strategies to the discretion of regional directors, but did not conduct a timely evaluation of project results. As a result, enforcement results varied from region to region. Strategies utilized by the regions included reviewing participant complaints, referrals, and leads from plan service providers or administrators; as well as case development through computer targeting or self initiation. It is our opinion that an evaluation of project results would assist management in identifying the most effective targeting strategies, evaluating the success of the project, and determining its future scope and direction. PWBA is now evaluating the results of the ECP project.

We also found that data in PWBA's Case Management System is inaccurate, particularly with respect to information on the sources of cases and occurrences of fiduciary violations. It is our opinion that the accuracy of this data is essential in enforcement planning and, when correlated with case results, crucial in assessing the success of the project.

We also found that PWBA does not collect data or report on funds that have been misapplied and which are unrecoverable by participants or the Federal Government. The OIG believes that, by not providing information on unrecoverable assets, as it does for restored assets, PWBA fails to communicate a complete picture of this issue. This partial disclosure may be misleading PWBA clients as to the seriousness of this issue and deprives the Congress and the Department pertinent information.

Ensuring Pension Assets are Safeguarded While in Trust

The OIG also has some long-standing concerns with respect to ensuring that funds are safeguarded while they are held in trust by plan administrators, service providers, or trustees.

Chief among our recommendations in this area is the need to repeal the limited scope audit provision of the Employee Retirement Income Security Act (ERISA) of 1974, which results in inadequate auditing of pension plan assets. Since 1984, the OIG has reported its concerns that employee pension funds are not being adequately

audited to ensure that they will be available in the future to pay promised benefits. This provision exempts from audit all pension plan funds that have been invested in institutions such as savings and loans, banks or insurance companies already regulated by Federal or State Governments. At the time ERISA was passed two decades ago, it was assumed that all of the funds invested in those regulated industries were being adequately reviewed. Unfortunately, as we have found from the savings & loan crisis, that is not always the case.

According to PWBA, more than $950 billion in pension plan assets (out of approximately $2 trillion subject to audit requirements under ERISA) are not examined because of the limited scope audit provision. Currently, because of this provision, independent public accountants (IPAs) conducting audits of pension plans cannot render an opinion on the plan's financial statements in accordance with professional auditing standards. It is important to note that the disclaimer of any opinion on the financial statements includes even those assets that are not held by financial institutions. The OIG believes that these "no opinion"' audits provide no substantive assurance of asset integrity to benefit participants or the Department. Our concerns in this area were raised in two OIG audits and have subsequently been supported by PWBA, the General Accounting Office, and the American Institute of Certified Public Accountants.

Madam Chair, the OIG believes that requiring full scope audits of employee benefit plans is a reasonable mandate that would not be a burden on businesses. Currently, at least half of the Nation's pension plan assets are the subject of full scope audits. Moreover, these audits are usually routine add-ons to annual financial audits of a corporation, and therefore, their specific cost is not high. To illustrate the difference in value between a limited scope audit opinion and a full scope audit opinion, I have attached a copy of opinions from each to my testimony.

The OIG believes that the failure to adequately audit pension plans opens the door for many forms of fraud and abuse, including understating required contributions or degrees of risk, and overstating plan investments and valuations. Obviously, these factors can potentially lead to pension plan failures.

The OIG has also recommended that independent public accountants (IPAs) and plan administrators be required to report serious ERISA violations directly to the Department. The OIG believes this requirement will enhance oversight of pension plan assets as well as ensure the timely reporting of violations. This change will involve accountants in the kind of active role that they are supposed to play in the safeguarding of pension assets, by providing a first line of defense to plan participants through their timely and direct reporting of potential problems with employee benefit plans.

Because of the vulnerability of pension assets to fraud and mismanagement, Madam Chair, the OIG believes that full scope audits of employee benefit plans and

reporting of serious ERISA violations by IPAs and plan administrators are crucial factors in ensuring that pension assets are safeguarded. However, while legislation to address these concerns has been proposed in past years, a legislative fix has yet to be enacted. It is my understanding that the Administration is currently working on introducing a proposal that would address these two OIG recommendations.

From an investigative perspective, the OIG continues to focus on identifying abuses by service providers, administrators, and others with respect to union pension funds and investment activities. The OIG is currently conducting investigations of more than $200 million in pension assets that are suspected of being abused or defrauded. Our investigations continue to uncover abuses of employee benefit plans in the manner in which pension assets are managed and invested. The size of these plan assets offer inviting targets to unscrupulous service providers and individuals who offer services to the plan administrators such as accountants, attorneys, or investment advisors.

An example of some of the types of abuses we have identified involves an attorney for an employee benefit plan with over $30 million in assets. In this case, the attorney engaged in a scheme to temporarily divert pension assets to invest in an off-shore, lucrative (yet high-risk) investment scheme. Some $10 million in pension assets were lost in the scheme when the offshore investors stole the money. The attorney pled guilty to charges of conspiring to solicit and receive kickbacks related to influencing the investment of the $10 million of pension funds. Other service providers to the fund, an investment advisor and an accountant have been charged as well. The attorney is currently incarcerated.

The OIG, in conjunction with its probe of labor racketeering in the construction industry, has been looking into the use of pension plan assets as loans for construction projects and other related loan activity. These cases are very complex in terms of the way the fraud is concealed. An example of this type of activity involved a case where an individual in California pled guilty to charges that he was involved in a scheme to defraud pension funds through the use of construction loans. The defendant, acting as the general managing partner of a partnership, obtained over $10 million in construction financing through a mortgage company from four union pension funds. As part of the loan agreement, the defendant was advanced funds in order to directly pay subcontractors for any work that they performed on the project. To obtain a release for some of the funds, the defendant was obligated to provide the mortgage company with documentation supporting the use of the funds to pay the subcontractors for construction materials and services. The defendant used the money on other unrelated real estate construction projects, while the project that was to be funded with the money failed. Unfortunately, the pension plans had to absorb the monetary loss.

The OIG is also playing a very active role in the Attorney General's Pension Abuse Initiative. This enforcement project seeks to increase emphasis on the problem of pension asset fraud and abuse. U.S. Attorneys' offices are working with Federal and

State Government agencies to determine the magnitude of this problem in their respective districts. Of the initial cases that have been identified where prosecution is anticipated, at least 20 percent are being investigated by this OIG. The cases, which are scattered across 36 different federal districts, involve embezzlements and kickbacks to union and plan officials ranging from $3,000 to $28 million.

Continuing OIG Oversight

Ensuring that pension assets are safeguarded is of such importance that the OIG has prepared a 5-year audit plan of potential areas we will be exploring with respect to pensions. As part of this endeavor, in this next year, we will be conducting an audit on ERISA reporting and disclosure requirements. ERISA requires a significant amount of reporting and disclosure by employee benefit plans as a means of protection for employee benefit plan participants. Our review will determine how the IRS and PWBA gather the required information, and analyze how the information is used by the Government and participants. Since reporting and disclosure requirements place a burden on plan administrators yet are critical to participant protection, we will attempt to determine if the current requirements are necessary and sufficient to accomplish the intent of ERISA.

The OIG will also evaluate PWBA's enforcement strategy with respect to ERISA's prohibited transaction rules, fiduciary responsibilities, and reporting and disclosure requirements. We will specifically evaluate the use of computer targeting as an enforcement tool and the resources devoted to it and will obtain information from other agencies to determine any other targeting methodologies of benefit to PWBA.

The OIG will also monitor the development of PWBA's two major computer system development projects - their new form 5500 system and a new Case Management System from their start through completion. At a 5-year projected cost of $59 million for the form 5500 system alone, OIG monitoring is necessary to ensure that the systems are an appropriate and efficient tool in PWBA's oversight and enforcement efforts.

Madam Chair, this concludes my prepared statement, I would be pleased to answer any questions that you or the other Subcommittee Members may have.