2005 Top Management Challenges Facing the Department of Labor Identified by the Office of Inspector General

Following are the areas the Office of Inspector General (OIG) considers to be the most serious management and performance challenges facing the Department of Labor. They involve compliance, accountability and delivery of services and benefits.

- Improving the Integrity of the Procurement System
- Reducing Improper Payments
- Safeguarding Unemployment Insurance
- Maintaining the Integrity of Foreign Labor Certification Programs
- Improving Financial and Performance Accountability
- Improving Systems Planning and Development
- Ensuring Security of Employee Benefit Plan Assets
- Improving Management of Real Property Assets
- Pursuing Reauthorization of the Workforce Investment Act

Improving Integrity of the Procurement System

Ensuring controls are in place to properly award and manage procurements is a challenge to the Department. The current organizational structure lacks separation of duties between procurement and program functions, which facilitates noncompliance with procurement requirements and may result in procurement decisions that are not in the best operating or financial interests of DOL. In addition, our audits have demonstrated that file documentation has not been adequate to support the validity and rationale of procurement decisions and actions. The OIG believes that, until procurement and programmatic responsibilities are properly separated and effective controls put in place, DOL continues to be at risk for wasteful and abusive procurement practices.

The OIG recently completed two audits involving procurement at two DOL agencies, which were conducted as a result of hotline complaints. These audits have shown that problems arise when the procurement function is not independent of program functions. This scenario may result in program officials, instead of contracting experts, driving procurement policy and decisions as our audits identified.

An audit of a contract for encryption software disclosed that the award to a sole-source contractor was not adequately justified. Furthermore, the contract included two additional products that were added without the Department's Procurement Review Board's review and approval. These unapproved modifications significantly changed the contract's scope and cost. The Department ultimately did not use $3.8 million worth of purchases of encryption products and could not justify its reasons for abandoning the investment.

In another audit, we found that one specific agency's procurement procedures exhibited a pattern of disregard for acquisition requirements and did not adhere to the principle of full and open competition. By operating in such an environment, management was unable to ensure that contracts were in the best interest of the Government, and that all eligible contractors were given the opportunity to compete for the agency's contracts.

Several audits involving procurement by the Department also have demonstrated that procurement files did not contain adequate documentation to support the validity or rationale of procurement decisions and actions. Also, cognizant officials with oversight responsibility for both the program and procurement functions could not demonstrate that their decisions were sound.

The Service Acquisition Reform Act of 2003 addresses a number of issues aimed at improving procurement management, including the requirement for each Federal agency head to establish a Chief Acquisition Officer (CAO) position, to be filled by a non-career employee whose primary responsibility is acquisition management. The Department is taking steps to address the lack of separation of duties in its procurement

function with a recent draft Secretary's Order establishing the position of CAO. To adequately address the OIG's recommendations regarding separation of duties, day-to-day procurement duties should be under the direction of the new CAO, with acquisition being the CAO's primary responsibility.

Reducing Improper Payments

Reducing improper payments in DOL-administered programs, such as Unemployment Insurance (UI) and the Federal Employee Compensation Act (FECA), remains an ongoing challenge for the Department. Improper payments include those made in the wrong amount, to an ineligible recipient, or improperly used by the recipient. The need for Federal agencies to take action to eliminate overpayments is recognized by the President's Management Agenda (PMA) and the Improper Payments Information Act of 2002. Calendar year (CY) 2004 UI overpayments by the states are projected by the Department at $3.4 billion. The Department estimates FECA overpayments in FY 2004 at $6.4 million.

Unemployment Insurance and the Use of New Hire Data

The UI program, a Federal-state partnership, is DOL's largest income maintenance program with outlays almost doubling in the past 6 years: from $24.9 billion in FY 1999 to $48.9 billion in FY 2004. Benefits for individuals are dependent on state law and administered by State Workforce Agencies, but the program framework is determined by Federal law. In recent years, the OIG has raised concerns about the magnitude and consistency of the overpayment rate in the UI program.

A 2004 OIG audit determined that, although implementing a state new hire directory cross-match was more effective in identifying overpayments than cross-matching against employer wage records, 12 states were not using new hire data at the time. According to ETA, 8 of the 12 states still have not connected to their respective state's new hire database; however, 4 states are expected to implement in the near future. We continue to recommend that the Department provide technical assistance and resources to state UI programs currently not using new hire detection to quickly initiate and/or complete plans for implementation.

The OIG had also recommended that DOL encourage state UI agencies to access the National Directory of New Hires. Access to this database provides states with additional data not available in state directories of new hires, such as new hire information from multi-state employers who report to a single state and new hire information from the Federal government. Last year's passage of the SUTA Dumping Prevention Act enabled states to access the National Directory.

The Department is currently working closely with the Department of Health and Human Services, the Social Security Administration, and the states to determine technical and operational aspects of access to the National Directory. DOL is currently performing a 3-state pilot study to determine if the benefits of using the National Directory to reduce overpayments would exceed the cost of implementation. The Department plans to have the study completed and issue a final report to all 50 states in the fall of 2005.

The OIG urges the Department to continue to offer assistance to the states on the use of both the state and National Directories.

Federal Employees' Compensation Act Program Controls

The OIG considers the risk of FECA overpayments a Departmental challenge. The DOL-administered FECA program impacts the employees and budgets of all Federal agencies. FECA provides income and medical cost protection to covered Federal civilian employees injured on the job, employees who have incurred work-related occupational diseases, and beneficiaries of employees whose deaths are attributable to job-related injuries or occupational diseases.

In previous years, the OIG reported that the Department needs to obtain and review medical evidence on a periodic basis in order to justify continued eligibility for FECA compensation payments. This was due to the fact that the Office of Workers' Compensation Programs did not establish effective controls to ensure that current medical evidence was requested and received in a timely manner, increasing the risk of improper payments. In March 2005, DOL completed the roll-out of its new benefit payment system, iFECS

(Integrated Federal Employee Compensation System). This system automatically tracks the due dates of medical evaluations. Management expects to have an enhanced iFECS system fully operational by March 2006.

Safeguarding Unemployment Insurance

Improving the integrity of the UI program to provide income maintenance to qualified individuals again remains a challenge for the Department. In FY 2004, the UI program paid $35 billion in temporary income support. Recurring issues faced by the UI program are the adequacy of Unemployment Trust Fund (UTF) resources and identity theft and organized crime activity in the UI program.

Unemployment Trust Fund Resources
Overcharging for UTF administration by the Internal Revenue Service (IRS) poses a major challenge for the Department. Earlier OIG audits demonstrated the UTF was being improperly charged for hundreds of millions of dollars over several years in administrative expenses. The OIG previously recommended that the ETA work with the IRS to adopt an alternative method to allocate costs and seek reimbursement for overcharges. The IRS subsequently reduced the amount of UTF FY 2002 administrative charges.

In FY 2003, the Treasury Inspector General for Tax Administration (TIGTA) reported that the IRS needed to establish an effective process for determining UTF administrative expenses. Based on TIGTA's recommendation, the IRS implemented a new cost methodology in October 2004. Even with this change, the administrative charges for UTF exceeded $75 million for the first 3 quarters of FY 2005, and at the current rate, the OIG estimates charges will exceed $100 million for FY 2005. ETA has expressed concern about the complexity of the IRS's new methodology and the magnitude of the administrative charges. The OIG recently requested that TIGTA audit the new methodology's adequacy for charging UTF administrative expenses. We understand that TIGTA is planning an audit in FY 2006.

Identity Theft and Organized Crime Activity in Unemployment Insurance Program
OIG investigations have found increasingly complex, costly and pervasive UI fraud schemes resulting in program losses in the millions of dollars. Many of these schemes include both identity theft and the involvement of multinational non-traditional organized crime groups. For example, a significant OIG investigation revealed the crime group had controlled more than 4,000 check-mailing addresses and used more than 15,000 identities in several states. The defendants were ordered to pay $59 million for their role in the scheme. In a recent case, several members of a California family were sentenced for various crimes. In this case, one defendant was ordered to pay more than $7.5 million in restitution for her role in the UI identity theft scheme.

Maintaining the Integrity of Foreign Labor Certification Programs

Reducing the susceptibility of DOL Foreign Labor Certification (FLC) programs to abuse remains a challenge for the Department. These programs permit U.S. employers to hire foreign workers when their admission does not adversely impact the job opportunities, wages, and working conditions of citizens and legal residents. In FY 2004, DOL received approximately 466,000 foreign worker applications for the FLC programs from employers. Abuse of the FLC programs may cause unlawful admission of foreign nationals and incur economic hardship for American workers.

Problems with the Labor Certification Process
The responsibility for approving employers' labor certification applications falls under the jurisdiction of ETA, which is the initial step in the process by which foreign nationals obtain work visas. Unfortunately, a recurring concern of the OIG is the integrity of the foreign labor certification process.

New regulations, which were effective March 2005, provide for the electronic submission of new permanent applications to Federal Processing Centers located in Atlanta and Chicago. The OIG cautions that an

electronic approval, rather than human review of applications by State Workforce Agencies, could potentially increase fraud.

In 2004, the OIG also expressed concerns over both the high volume of backlogged applications and the associated risk of approving questionable applications. Unprocessed applications submitted before March 28, 2005, to ETA regional offices or State Workforce Agencies have been transferred to the ETA Backlog Elimination Centers located in Philadelphia and Dallas. As of August 2005, the Backlog Elimination Centers had 312,438 applications pending. ETA expects to eliminate the backlog by CY 2007. The OIG continues to recommend the Department ensure the processing of backlogged applications does not result in the certification of unqualified applications.

Labor Certification Fraud
Labor certification fraud remains a major OIG concern. Recent OIG investigations have revealed corrupt employers, labor brokers, and lawyers who file fraudulent applications. The prevalence of these cases consistently demonstrates the susceptibility of the program to fraud. For example, one such broker recently submitted more than 900 labor certifications on behalf of Chinese nationals seeking entry into the United States. In this instance, the labor broker had charged foreign workers up to $90,000 per labor certification.

Improving Financial and Performance Accountability

In order to manage DOL programs for results and fully integrate budget and performance, the Department needs timely financial data, a managerial cost accounting system that matches cost information with program outcomes, quality performance data, and useful information from single audits, which cover 90% of its expenditures.

Managerial Cost Accounting
A cooperative effort between the Department's Office of the Chief Financial Officer (OCFO) and the program agencies resulted in the successful development of cost models for most of DOL's major agencies and programs during the latter part of FY 2004. These cost models provide capabilities to integrate program activities, outputs, costs, and non-financial data to provide the basis for reporting useful managerial cost accounting information. Additionally, OCFO, the Office of the Assistant Secretary for Administration and Management (OASAM), and the program agencies are continuing to improve the cost models and related capabilities for integration of cost and performance information.

The Department received high marks on the PMA the past few years for its financial management. To fully realize the benefits of cost accounting, the Department now needs to turn attention to refining its cost models and their related capabilities for integration of financial and programmatic data, and successfully institutionalizing the use of cost accounting information to improve program operations and routinely report program results.

Quality Performance Data
Three recent OIG reviews of the validity of DOL program data identified the need for improvement in the way DOL ensures completeness and reliability of program results data. Also, much of the program results data required by DOL to measure attainment of its strategic plan goals are generated by states and other sources below the Federal level. This presents challenges for ensuring data quality and evaluating program effectiveness. Past OIG audit work has disclosed high error rates in grantee-reported performance data and raised concerns about the use of that data for decision making. ETA has developed a data validation program to improve the reliability of program data. The OIG plans to audit ETA's data validation system in FY 2006.

Single Audit
The Department relies on audits conducted under the Single Audit Act to provide oversight of more than 90% of its expenditures. The OIG is concerned about the adequacy of information DOL receives from these audits, which are conducted by public accountants or state auditors and procured with DOL grant funds. OIG quality control reviews since 2002 have revealed serious deficiencies in single audits, including inadequate sampling, which would make the audits unreliable. The OIG is currently participating in the

National Single Audit Sampling Project. This project is designed to: determine the quality of Single Audits by providing a statistically reliable estimate of the extent that Single Audits conform to applicable requirements and standards; and make recommendations to address any noted audit quality issues.

Management Controls
In FY 2005, Office of Management and Budget (OMB) Circular A-123 was amended to provide updated internal control standards applicable to all Federal agencies. The amendment also included new specific requirements for conducting agency management's assessment of the effectiveness of internal controls over financial reporting. Appendix A of A-123 requires that documentation be maintained, not only of the controls in place, but also of the assessment process and methodology that management used to support its assertion as to the effectiveness of the internal control over financial reporting. In addition, Federal agencies will be required to perform monitoring activities that include direct testing of the controls as part of the assessment process. With implementation set at the end of FY 2006, all Federal agencies, including DOL, will be challenged to establish procedures and mechanisms to assess, test, document, and certify that their internal controls are in place and operating effectively.

Improving Systems Planning and Development

Developing efficient and effective systems to perform daily activities remains a significant challenge for the Department. OIG audits have identified that DOL Information Technology (IT) system development life-cycle activities need strengthening in the areas of planning, project management, and decision making. Current system development plans should be structured to include timely reviews of initiatives progress in relation to planned project activities, and significant milestones, especially at key decision points. Project plans should be strengthened to include budget and cost tracking, project timelines, and resources monitoring. Taking these steps would improve DOL's management of IT systems.

The Department's Chief Information Officer needs to take a stronger role to ensure that the agencies adequately plan for system development activities and are providing adequate project management. The Department's agencies should assess their progress in having sufficient numbers of IT and business line personnel obtain certification in the field of project management. These resources will help to assure the future success of DOL IT initiatives and can be leveraged throughout DOL, as warranted, given the importance, size, and complexity of an initiative.

Department of Labor Core Financial System Replacement
The New Core Financial Management System (NCFMS) is an enterprise-wide initiative that will enhance the Department's ability to integrate financial and performance information. By replacing DOL's legacy mainframe based core accounting system (DOLAR$) with a commercial-off-the-shelf financial management information system, program managers and decision makers throughout the Department will receive more timely, accurate, and useful information to improve results delivered by the programs they administer. DOL will be challenged to develop a system that meets PMA and OMB Requirements. In addition, the NCFMS project will affect all organizations in the Department that currently utilize DOLAR$, or have systems that interface into DOLAR$.

Emerging Technologies
DOL is reviewing new technologies to better manage and provide services to the public. In doing so, it is likely to experience new security threats and other events as these new technologies' vulnerabilities are exploited. The Department is currently embracing the new technologies of wireless local-area networks and personal electronic devices, and has started using wireless technology to better serve the needs of the organization. To meet the new challenges that these technologies bring, the Department should have acquisition and implementation plans consistent with protecting informational assets and confidential and sensitive information, while providing the highest level of quality of service and access to needed information. These new technologies will require updated policies and procedures to maintain a high level of operational effectiveness. Close monitoring will be key to ensuring that the promised benefits of these technologies are achieved.

Homeland Security Presidential Directive (HSPD) -12
The Department, as well as all other Federal agencies, must implement a standard system for identifying Federal employees and contractors. This system must implement a secure and reliable method of identification, which has the capability to coordinate access with other Federal agencies and sites. The HSPD-12 has an aggressive implementation date of September 2006. Under this system, agencies will need to provide employees identification cards that will be used to validate and monitor Federal employees and contractors. The General Services Administration is responsible for reviewing and approving third party-solutions available for agencies to procure. However, the HSPD-12 allows agencies to develop or procure non-approved services, which will challenge DOL to implement the new Personal Identity Verification cards (*i.e.,* Smart Cards) that are: secure and reliable forms of identification; issued based on sound and recognized criteria; rapidly authenticated; and strongly resistant to identity fraud, tampering, counterfeiting, and terrorist exploitation. In addition to the challenge of providing this new technology, DOL will also be challenged in managing the implementation, distribution, and maintenance of the Smart Cards.

Implementation of Public Key Infrastructure (PKI)
Despite working the last several years on implementing a PKI solution to secure and authenticate electronic documents within the Department, DOL has yet to identify a PKI solution. During the same period, DOL has twice procured encryption products that need PKI to achieve maximum benefit from these products. Because the use of keys to encrypt, decrypt, and authenticate documents is a complex process, agencies and public organizations may experience difficulties implementing an integrated and effective PKI program. DOL has been challenged to implement a Department-wide PKI system and manage the underlying infrastructure, and is currently exploring other avenues to find the best fit for the Department's needs and environment.

Ensuring Security of Employee Benefit Plan Assets

A major challenge confronting the Department is protecting the benefits of American workers, which includes pensions and health care. The Employment Benefits Security Administration (EBSA) oversees the administration and enforcement of the fiduciary, reporting, and disclosure provisions of Title I of the Employee Retirement Income Security Act (ERISA). Under ERISA, the Secretary of Labor is responsible for the rights and financial security of participants in approximately 730,000 private pension plans and 6 million health and welfare plans covered by ERISA. These pension plans hold over $4.5 trillion in assets and cover more than 150 million American workers. Recent failures in corporate financial management and reporting, as well as in the auditing and oversight of these activities, show the need to enhance worker pension and healthcare security by expanding safeguards and improving benefit plan regulatory enforcement.

Safeguards to Protect Pension Assets
Improving the process through which employee benefit plans are audited is a serious challenge faced by DOL. As a result of an earlier OIG audit, and on its own initiative, the Department made several improvements to its processes for identifying and correcting deficient employee benefit plan audits. EBSA now reviews the audit quality processes of those firms performing the greatest number of employee benefit plan audits. In addition, it will continue to review individual audits of smaller firms on a sample basis, allowing for more coverage. For those deficiencies identified, the Department has agreed to obtain more corrective action. As for the smaller firms where EBSA will review individual plan audits, the Department implemented procedures ensuring review of the most current work available.

For the audits that the OIG found to be deficient, EBSA has begun a process of reviewing more current audit work of these firms. If the Department finds current work to be deficient, EBSA has agreed to obtain greater documentation of corrective actions from the firms involved.

Pension Plan Fraud
Ensuring the security of employee benefit plan assets, which are attractive targets to organized-crime groups, remains a challenge for the Department. Recent OIG labor racketeering investigations and the increased activity of EBSA's criminal enforcement program consistently identify the vulnerability of pension assets. The OIG has continued to monitor the integrity of Taft-Hartley plans, which are jointly administered by labor

union and management representatives and have been previously identified as at risk. A typical labor-management case often evolves from the collaboration of management representatives and corrupt union officials. One such case recently led to the 53-count indictment of 32 members and associates of a well-known organized-crime family. Defendants included both a president and a trustee of a local union.

Cash Balance Pension Plans
A 2002 OIG audit found that some cash balance pension plan participants, who had collected the lump sum payments before normal retirement age, were being underpaid benefits. The OIG again raises the issue regarding the methodology used to calculate the benefits. The OIG continues to recommend that EBSA increase the Department's oversight of cash balance pension plans. However, the first step in this direction requires the guidance of the IRS regarding the calculation of participant-accrued benefits on this matter. Disparate interpretations of how accrued benefits are calculated will result in some plan participants continuing to be paid incorrectly. The OIG urges the Department to press the IRS for the necessary guidance to ensure cash balance pension plan recipients receive the benefits they are owed.

Corrupt Multiple Employer Welfare Arrangements (MEWAs)
MEWAs are typically marketed to small businesses as a means of obtaining inexpensive health coverage for their employees. Fraudulent MEWAs, which default on their benefit obligations, are often misrepresented by plan promoters as being maintained under a bona-fide collective bargaining agreement. The OIG continues to recommend EBSA investigate unscrupulous health insurers who are burdening Americans with an increasing number of unpaid medical claims. Therefore, the OIG recommends that the Department continue its efforts to decrease the number of fraudulent MEWAs, in particular by seeking legislative changes to increase its authority to obtain reliable plan information and assess penalties.

Improving Management of Real Property Assets

Improving the accountability for and management of real property is an ongoing challenge for the Department. A Government Accountability Office (GAO) report released in June 2005 noted that the Department has taken actions in response to last year's Executive Order 13327 which addresses the Federal Asset Management initiative to the PMA. A senior real property officer has been designated to, among other things, monitor the real property assets of the Department. However, the GAO report raises the government-wide issue of the lack of reliable and useful property data that are needed for strategic decision making.

Job Corps Real Property
In our FY 2004 report on the Department's internal controls over financial reporting, the OIG noted that ETA did not sufficiently utilize DOL's property reporting and tracking system and did not establish sufficient controls to ensure that Job Corps real property was safeguarded and accurately reported in DOL's tracking system and general ledger systems. In FY 2004, Job Corps real property was valued at $770 million. ETA is in the process of taking action to ensure the Job Corps real property is accurately reported and restructuring its existing processes to strengthen the property management system.

State Workforce Agency Real Property
In addition, an OIG audit of management controls over Federal equity in State Workforce Agency (SWA) real property found that ETA had not established adequate management controls over accounting for the Department's equity interest in SWAs' real properties. Specifically, ETA's inventory of SWA property was neither accurate nor complete, and ETA did not ensure the states properly handled the proceeds from disposing of SWA properties with DOL equity. We recommended the ETA make control and management of real property a higher priority. ETA has begun to review its existing processes and restructure them to strengthen the property management system. For example, ETA will no longer approve new grantee amortization plans, and will review and renegotiate existing plans on a case-by-case basis.

Pursuing Reauthorization of the Workforce Investment Act (WIA)

WIA authorization expired in 2003, and Congressional reauthorization is still pending. Both the revision and improvement of WIA programs by the Department via the reauthorization process will continue to be a challenge. OIG audits identified areas in which WIA could be improved through changes to increase training provider participation, improve dislocated worker program services and outcomes, better document youth program outcomes, and better assess states' current WIA funding availability. DOL has agreed to our current recommendations, but it is waiting for reauthorization to implement them.

Changes From Last Year

In identifying the most critical Management Challenges faced by the Department each year, the OIG recognizes matters meriting the continued attention of the Department may be omitted from the list. Changes from the Top Management Challenges Facing the Department of Labor from FY 2004 are the addition of Improving the Integrity of the Procurement System and the inclusion of last year's challenge of Information Technology Security Controls within the Challenge of Improving Systems Planning and Development.

E-payroll conversion, one of last year's concerns, was addressed when the Department transferred its payroll system to the National Finance Center in April 2005. The delay in the conversion due to issues raised by the OIG significantly contributed to the Department having only minor issues when the conversion was completed.

One of last year's issues regarding the solvency of Unemployment Trust Fund resources within the challenge of Safeguarding Unemployment Insurance has also been eliminated. When the OIG initially raised this issue, the Trust Fund balance was in steady decline and benefit payments were on the rise. The concern was that the balance could reach a point where Federal money would not be able to cover state shortfalls. But this is no longer the case, because, during the recent recession, the Trust Fund remained solvent and covered state shortfalls as needed.

In the areas of grant accountability, ETA has undertaken a grants management initiative, the results of which the OIG is currently reviewing. While it is not included in this year's Management Challenges, accountability over DOL-awarded grants will continue to merit diligent attention.