Appendix D

EBSA Response to Draft Report

U.S. Department of Labor

Employee Benefits Security Administration
Washington, D.C. 20210

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MEMORANDUM FOR: ELLIOT P. LEWIS
Assistant Inspector General for Audit

FROM: ALAN D. LEBOWITZ
Deputy Assistant Secretary for Program Operations

SUBJECT: EBSA Response to OIG Performance Audit
Report Number 05-09-003-12-001

Thank you for the opportunity to comment on the recommendations in your performance audit of the Employee Benefits Security Administration's evaluation of enforcement project results.

The Employee Benefits Security Administration (EBSA) is responsible for the administration and enforcement of the civil and criminal provisions of Title I of the Employee Retirement Income Security Act of 1974 (ERISA) as well as related provisions of other Federal laws (e.g., Title 18 USC federal criminal statutes). EBSA oversees approximately 3.2 million private sector pension and health plans, and similar numbers of other welfare benefit plans, such as those providing life or disability insurance. The employee benefit plans under our jurisdiction hold approximately $4.7 trillion in assets and cover approximately 150 million Americans.

An important part of EBSA's mission is to deter and correct violations of ERISA through a strong enforcement program to ensure workers receive promised benefits. Your audit was designed to determine if EBSA is effectively evaluating its civil enforcement project results and directing its resources to enforcement issues that have a significant impact on American workers' health, pension, and other employee benefits.

Before addressing each of your recommendations, we would like to explain the design, management, and operation of EBSA's enforcement program.

EBSA's Enforcement Program

Given the size of the plan universe that EBSA oversees relative to its number of investigators, EBSA has focused its available resources on investigations that we believe will most likely result in the deterrence, detection, and correction of ERISA fiduciary violations. Our enforcement program is driven by this mission, and, by design, retains a flexibility that permits dynamic policy considerations to be strategically incorporated. The enforcement program is fully integrated with EBSA's customer service functions. In FY 2008, 871 investigations were opened based on referrals from EBSA's Benefits Advisors.

Our regional directors are required to establish an annual, specific operating plan that creates a visible EBSA presence throughout their geographic regions, pursuant to national priorities, regional priorities, and individually selected cases. On the national level, we identify broad topic areas where we believe plan participants and beneficiaries are most susceptible to actual loss of benefits. Long-term policy goals are articulated in the Strategic Enforcement Plan (StEP); the three current investigative priorities, designed to protect at-risk populations, are plan service providers, health care plans, and defined contribution pension plans. Once the broad framework has been established, EBSA develops initiatives to support these priorities. There are two types of initiatives: national enforcement projects, which are directly based on the StEP goals; and regional projects, which are localized investigative projects undertaken by individual EBSA regional offices. Our internal program development guidelines state that regions should conduct investigations covering many criteria. Pursuant to these guidelines, regions should:

- Maintain an appropriate number of case openings;
- Achieve an appropriate balance among the types of plans investigated;
- Investigate all types of plans (both large and small plans, both pension and welfare plans);
- Demonstrate an adequate enforcement presence in all states within their geographic jurisdictions;
- Conduct a robust criminal enforcement program; and
- Devote adequate resources to national enforcement projects as well as regional enforcement projects.

EBSA establishes its national enforcement projects in order to focus its enforcement resources on areas that have the greatest impact on the protection of plan assets and participants' benefits, and regional offices are expected to place particular investigative emphasis in these areas. The regional enforcement projects may focus on a narrower part of an existing StEP goal or may explore a new area where benefit plans may be at risk. In addition, regions conduct investigations that are not part of an existing national or regional enforcement project, based on annual internal program development guidelines issued by the Office of Enforcement.

As can be seen from the internal program development guidelines, EBSA strives for a well-balanced enforcement program. This means that all sizes and types of plans should be investigated in pursuit of the goal to detect and correct ERISA violations. The OIG report noted that EBSA conducted only 548 ESOP investigations in the time period reviewed as compared to 3,951 Employee Contribution Project cases, implying that this difference in resource allocation was questionable. However, in 2006, there were only 7,128 ESOPs compared to 465,653 401(k) plans. As these numbers illustrate, placing EBSA's investigations in the context of the plan universe is important in understanding resource allocation.[1]

Merely because each region is not conducting the exact same proportion of types of investigations is not an indication of poor resource management. On the contrary, it is evidence of an enforcement program that is designed to take into consideration the varied conditions

[1] We would like to correct a misperception. On page 5, the OIG report stated that ESOP cases are time consuming. As we indicated during the audit, ESOP and ECP cases took roughly the same amount of time to conduct (15.5 vs. 17.4 staff days).

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among regions. Regional directors are expected to assess current enforcement activities, trends, and areas of noncompliance within the region's jurisdiction and ensure that areas of potential risk are targeted for investigation. Because areas of potential risk vary from region to region, different priorities and management decisions will occur among regions in order to most effectively address these risks.

Under the Government Performance and Results Act (GPRA), EBSA, in consultation with the Department and OMB, established a civil enforcement goal based on the following ratio:

$$\frac{\text{Closed Civil Investigations with Fiduciary Corrections}^{2}}{\text{Total Closed Civil Investigations}}$$

EBSA uses its civil enforcement GPRA measure to help evaluate its civil enforcement program. However, EBSA's evaluation of its enforcement program, including its national enforcement projects, encompasses more than the GPRA measure, and includes an assessment of whether our mission, the detection, correction, and deterrence of ERISA violations, is being met. The enforcement program, including every national enforcement project, is thoroughly evaluated at least twice a year. EBSA uses many factors to determine whether a national enforcement project is successful including, but not limited to:

- The frequency with which violations are detected;
- The ability to obtain meaningful corrections to violations;
- The amount of investigative time being spent to achieve the corrections;
- The appropriateness of using other methods of achieving compliance (for example, the "Orphan Plan" national enforcement project was discontinued once the new Abandoned Plan Program was available);
- Whether criminal violations are being detected;
- Whether policy considerations are implicated, including public interest.

We have concluded that it is not appropriate to use the GPRA goal, or similarly constructed measure, to evaluate regional enforcement projects. Regional enforcement projects are often used as "laboratories" to assess risks within a geographic area or to determine whether there is a need for a national enforcement project. After testing a regional enforcement project, EBSA may determine that the violations are not as widespread as anticipated, that a different enforcement approach should be used, or that the project does not contribute to fulfilling the mission of the agency. Placing a GPRA measure on this type of activity would unduly constrain the regions and prevent them from being innovative, hampering the development of new, but untried, methods of deterring and correcting violations of ERISA.

[2] The OIG's draft report asserts that EBSA does not measure non-monetary results. This is incorrect. The GPRA goal numerator includes both monetary and non-monetary fiduciary corrections. EBSA considers non-monetary fiduciary results valuable contributions to our mission. For example, removing breaching fiduciaries from positions of control is a significant way to deter future violations of ERISA. Preventing millions of dollars in unpaid claims from being incurred by removing a fraudulent MEWA operator may be just as valuable as recovering money to get claims paid.

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EBSA's Civil Enforcement GPRA Goal

EBSA has spent over ten years developing a GPRA goal and has come to fully recognize, through its years of experience in developing performance measures, that there is no quantifiable, pure outcome measure for the law enforcement work undertaken by EBSA's enforcement program. This conclusion has been acknowledged repeatedly by external reviewers and performance management experts in the field. In 2003, the then-EBSA Assistant Secretary met with officials from the Office of Management and Budget (OMB) to discuss the ongoing issue of EBSA's GPRA performance measures. After this meeting of OMB, DOL, and EBSA leadership, the parties agreed that it was extremely difficult to measure outcomes for an enforcement program that address the compliance of pension, health and welfare plans, and a range of service providers with a complex federal statute. Based on consultation with outside experts, we did adopt a series of surrogate measures that, we believe, when taken together with other underlying management data, indicate the level of success of the enforcement program. The current GPRA measure is such a surrogate, and has been used and reported on by the Department for a number of years in their integrated performance.

As we pointed out to the OIG audit team, developing GPRA goals that measure program outcome is difficult for other law enforcement agencies as well as for EBSA. In fact, we are unaware of any similarly-situated law enforcement agency that has been able to develop a valid outcome measure. For example, the DOL OIG has adopted performance measures that are purely output measures. Other regulatory agencies have also had difficulty establishing outcome-related goals.

The Federal Deposit Insurance Commission's (FDIC) supervision program is similar to EBSA's enforcement program. Part of the FDIC's goal is to promote the safety and soundness of FDIC-supervised insured depository institutions. However, unlike EBSA, the FDIC is responsible for a limited number of banks, all of which are somewhat similar.[3] Even with the limited number of regulated entities, FDIC's performance goals used to evaluate this strategic goal are almost all output oriented. Indicators include:

- Percentage of required examinations conducted in accordance with statutory requirements and FDIC policy, and
- Percentage of follow-up examinations of problem institutions conducted within required time frames.

FDIC officials have looked for opportunities to establish outcome-related goals but continue to "struggle" with the validity of such measures because there are factors beyond the control of the FDIC that influence achievement of the outcomes.[4]

[3] The FDIC is the primary federal regulator for 5,197 state-chartered banks, while EBSA is responsible for millions of private sector pension, health, and welfare plans, as well as an unquantifiable number of service providers. FDIC figures from the FDIC 2008 Annual Performance Plan.

[4] Evaluation of the FDIC's Use of Performance Measures, May 2007, Report No. EVAL-07-002, Office of Inspector General, page 3.

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Some of the Securities and Exchange Commission's performance goals for compliance with securities laws appear to be output-oriented, although they are identified as outcome-oriented.[5]

> Measure: The percentage of exams that resulted in deficiency letters requiring the registrant to take corrective action. [Explanation: Deficiency letters promote compliance with federal securities laws and self regulated organization rules.]

This is very similar to EBSA's measure of the percentage of investigations that resulted in corrective action.

> Measure: Percentage of firms receiving deficiency letters that stated they took or would take corrective action in response to all exam findings. (New measure, added February 2008.)

Although worded differently, this is also similar to EBSA's measure of corrective action taken.

The IRS uses an Employee Plans Compliance rate as one GPRA measure, which is defined as the ratio of plans with no significant compliance issues to the total number of IRS approved private retirement plans. The rate is estimated through an ongoing research program which uses audits of a random sample of plans to assess risks and compliance rates by market segment. The IRS divided its return unit customer population into market segments based on plan type and principal business activities. The baseline studies for these groups were still ongoing at the end of FY 2008. Although the IRS's performance measure identifies improved compliance as an outcome goal, using this study only a preliminary baseline had been developed by FY 2006 and baseline studies for only 18 out of 78 groups had been completed by July 2008. This appears to bring into question the effectiveness of a measure that could take so many years to complete.

In EBSA's continuing effort to measure compliance where feasible, EBSA has conducted discrete, baseline studies of compliance with selected aspects of ERISA, including audit plan quality, Part 7 compliance, and the Employee Contribution Project baseline study, as well as certain follow-up studies. Although these baseline studies provide valuable information, we are not convinced that they are an accurate measure of the effectiveness of EBSA's enforcement program. There are many other factors that influence compliance with ERISA. For example, if a future ECP baseline study indicates that compliance rates have not increased, this may not have any relevance to measuring the effectiveness of EBSA's enforcement program. One of the most-offered reasons why employers do not contribute employee contributions on a timely basis is that other company bills needed to be paid first. This is a factor directly related to the economic environment, not necessarily to the effectiveness of EBSA's enforcement program.

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[5] http://www.whitehouse.gov/omb/expectmore/detail/10004456.2005.html#performanceMeasures

OIG's RECOMMENDATIONS

Recommendation 1: EBSA should clearly define the objective of each of its civil enforcement projects.

We agree that the objective of each of our national enforcement projects could be clearer. EBSA will expand its public description of the national enforcement projects to include a specific objective of "finding and correcting violations of ERISA." We believe that putting the public on notice of our investigative emphases contributes to the goal of deterring violations of ERISA.

Recommendation 2: EBSA should establish a performance measure(s) that evaluate(s) each civil enforcement project's outcomes versus the stated objective.

We disagree with this recommendation. As previously discussed, EBSA has spent an enormous amount of time trying to develop a meaningful and useful performance measure to evaluate our civil enforcement program based on outcomes. Because this has proven fruitless to date, EBSA uses a surrogate measure which is widely recognized as an acceptable alternative by experts in the performance management arena. We discovered early on that there is no practical outcome measure available, and this infeasibility has been acknowledged repeatedly by external reviewers. We note that the OIG's draft report does not recommend an alternative outcome-based performance measure for EBSA.

Recommendation 3: EBSA should develop guidance for allocating enforcement resources based on intended enforcement outcomes and actual performance results.

As previously explained, the internal program development guidelines provided to EBSA's regional directors clearly state that EBSA's enforcement program is mission-driven, a mission that is well known to each regional director. All national enforcement projects are implemented with the objective of furthering EBSA's mission to deter and correct violations of ERISA. These projects are developed and continually evaluated by EBSA management.

The OIG report implies that EBSA should focus its resources disproportionately on potential high-dollar results that affect large numbers of participants. EBSA has resisted this formula for resource allocation for many years, as we believe such a measure would interfere with our mission to deter and correct violations of ERISA. Our mission is not limited to correcting only large dollar violations or to protecting only participants and beneficiaries of large plans. Nor do we believe that using pure dollar amounts captures the full impact of our investigations. EBSA has long had a policy to address all participant complaints. Over the years, the process of addressing these complaints has changed, but when EBSA determines that a fiduciary is unwilling to correct a violation, EBSA believes it is important to take appropriate action even if the number of participants or dollars involved is small. Over 80% of 401(k) plans have fewer than 100 participants; half of all 401(k) plans have between 2-24 participants[6]. As our case files reveal, such cases include a review of general records, such as the plan document, financial statements, plan bonds, and other issues. At the close of an ECP case, plan fiduciaries are likely better informed of their obligations under ERISA, including the timelier remittance of

[6] Private Pension Plan Bulletin, December 2008, U.S. DOL, page 42, http://www.dol.gov/ebsa/PDF/2006pensionplanbulletin.PDF

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contributions. We believe this plays a role (albeit not measurable) in deterring future violations and strengthening the security of pension plans. In fact, because we do pursue valid participant complaints, and have a correction ratio of over 80%, we believe we are clearly accomplishing our mission to correct violations of ERISA.

The OIG report stated that EBSA regions differed in their allocations of resources because EBSA headquarters did not provide clear guidance on intended enforcement outcomes. As previously explained, because each region addresses different risks, the regions *should* differ in their allocation of resources. We would not expect a regional office with only a few well-managed ESOPs in its jurisdiction to allocate the same amount of time to the ESOP project as a region in which there are many noncompliant ESOPs. EBSA expects each region to conduct investigations on a full range of plans, service providers, and issues, and to take into account the demographic make-up of its geographic jurisdiction. Furthermore, when a situation such as the collapse of Enron or the uncovering of a massive Ponzi scheme such as that run by Bernard Madoff suddenly arises, regions must have the flexibility to immediately focus on these cases. In our view, each region needs to retain the ability to address the risks within its own jurisdiction.

CONCLUSION

EBSA is proud of its civil enforcement program. We protect one of the most important assets in the country today--employee benefits. Although EBSA is highly leveraged, with a comparatively small investigative staff, we allocate these resources in a manner that has allowed us to close nearly 23,000 investigations during the past six fiscal years with fiduciary violations corrected in almost 75% of these investigations. Each of these years produced over $1 billion in monetary results. Most of these corrections have been achieved through voluntary actions; only about 7% have needed to be referred for litigation. Although the OIG report focuses on the civil enforcement program, EBSA investigations have also resulted in over 680 individuals indicted and more than 400 guilty pleas or convictions. Applications under our Voluntary Fiduciary Correction Program have increased from 240 in FY 2003 to more than 1,600 in FY 2008. The new Abandoned Plan Program is receiving more applications to terminate abandoned plans. If not for these two alternative enforcement programs, more investigative resources would have had to be used to conduct investigations.

This success would not have occurred if EBSA had not been developing civil enforcement projects that support its mission of deterring and correcting violations of ERISA, and thoroughly evaluating the success of the projects on an annual basis. EBSA's enforcement program needs to remain flexible enough to accommodate policy considerations and unforeseen occurrences that require quick investigative action. Adopting a rigid mathematical formula against which the enforcement program would be measured does not provide the kind of flexibility demanded by today's economic realities, a situation in which policy choices and decisions must be made in the face of quickly changing circumstances.