

## EBSA Response to Draft Report

## U.S. Department of Labor

Assistant Secretary for  
Employee Benefits Security Administration  
Washington, D.C. 20210



MEMORANDUM FOR: ELLIOT P. LEWIS  
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FROM: PHYLLIS C. BORZI  
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*copy of L.O. for Phyllis C. Borzi*

SUBJECT: EBSA Response to OIG REACT Audit  
Report No. 05-09-005-12-001

DATE: September 18, 2009

We appreciate the opportunity to comment on the recommendations made in your performance audit of the Employee Benefits Security Administration's policies and procedures related to the Rapid ERISA Action Team (REACT) project.

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) and related criminal statutes. As you pointed out, EBSA protects the integrity of retirement and welfare benefit plans for over 150 million Americans.

An important part of EBSA's mission is to deter and correct violations of ERISA and other relevant statutes and to ensure workers receive promised benefits. Due to its comparatively small investigative staff, limited resources, and the size of the plan universe that EBSA oversees, EBSA must focus its enforcement efforts in order to direct resources toward areas that will have the greatest impact on the protection of plan assets and participants' benefits. One of the ways in which EBSA's efforts are focused is by the use of national enforcement projects. The REACT project, which focuses on plan sponsors that are in severe financial hardship or that have declared bankruptcy, is one such national enforcement project.

As stated in your report, the REACT project has protected and restored plan assets. In fiscal year 2008, EBSA achieved over \$89.5 million in monetary results through this project. The project has achieved over \$113 million in monetary results in FY 2009 through March 31, 2009.

Your audit was designed to determine if EBSA's REACT project was identifying and responding quickly to protect the rights and benefits of plan participants when a plan sponsor faces severe financial hardship or bankruptcy and the assets of the employee benefit plan are in jeopardy. Before addressing your recommendations, we would like to review the operation of EBSA's REACT project.

#### Overview of REACT

The REACT project began in fiscal year 2001. The goal of REACT is to protect the rights and benefits of plan participants in an expedited manner when the plan sponsor faces severe financial hardship or bankruptcy and the assets of the employee benefit plan are in jeopardy. In a REACT investigation, EBSA takes a variety of steps to meet this goal, including taking immediate action

to ascertain whether all plan contributions have been paid into the trust, advising all affected plans of the bankruptcy filing, and providing assistance in filing proofs of claim.

Like any national project, one of the characteristics of REACT is that it identifies certain types of plans that EBSA has targeted for investigation. In the example of REACT, potential subjects of cases are plans whose sponsors are facing severe financial hardship or that have declared bankruptcy. The U.S. Small Business Administration Office of Advocacy reports that in 2008 there were 595,600 small business closures and 43,546 bankruptcies and that overall about half new small firms survive five years. EBSA must select REACT investigations from a large, heterogeneous pool using available information.

Approximately half of all REACT cases opened in fiscal year 2008 were opened on companies experiencing severe financial hardship. EBSA believes that this distribution is optimal, as ERISA violations in REACT cases can arise both prior and subsequent to bankruptcy. The percentage of cases based on severe financial hardship also reflects the careful case development EBSA must perform to attain the historical results achieved by REACT.

#### **Case openings**

Under REACT, EBSA opens cases based on information from multiple sources, including leads from bankruptcy courts or other government entities, EBSA computer targeting, EBSA's review of media reports, and EBSA benefit advisor referrals. According to the OIG draft report, only the review of media reports should be considered proactive work by EBSA. However, other sources, such as computer targeted cases, referrals from the bankruptcy courts and the predicate complaints made to the Benefit Advisors (BAs) are also the result of proactive efforts by EBSA. For example, cases opened due to EBSA computer targeting are the direct result of EBSA's proactive review of Form 5500s filed by plans. Similarly, referrals from bankruptcy courts or other outside organizations – and complaints made to BAs – are the result of EBSA's successful efforts in developing relationships with outside entities and in educating both the regulated community and participants about ERISA and EBSA.

The OIG draft report specifically identifies BA referrals as a reactive source because they are not the result of "original work" performed by the BAs. This statement ignores the important REACT outreach and education work done by EBSA. As the report cites, almost half of recent REACT cases were based on credible information provided by the public to BAs. Such a response is in fact attributable to proactive work by the agency.

The OIG draft report also assumes that EBSA's case opening sources may not represent identification of the highest risk plans. In EBSA's experience, BA referrals are one of the best sources of actionable information on plans with ERISA violations, particularly complaints from working participants, as they have first-hand knowledge of the plan sponsor's financial condition that is not otherwise available to EBSA in a timely manner. For example, privately-held companies are not required to make any public filings of their financial condition, and information on their financial condition is not consistently reported in the media. Therefore, absent a bankruptcy filing, it is difficult for EBSA to know about the plan sponsor's severe financial hardship other than by receipt of a complaint. Although we agree EBSA's response to

participant complaints is in some respects reactive—and appropriately so—we therefore disagree that complaints do not provide timely or systematic identification of plans in jeopardy.

EBSA has declined to define the term severe financial hardship for several reasons. First, there is the danger that any definition would be under inclusive, and exclude investigations that would otherwise be classified under the REACT project. EBSA regulates plans sponsored by public and privately-held companies of varying size, complexity, and enterprise. Pronouncing a single definition would be simplistic and limiting. Second, the imposition of a static definition would remove discretion from the Regional Directors and hamper their ability to respond to unforeseen situations under the auspices of the REACT project. Finally, different risks are present in different areas of the country, and the imposition of a one-size-fits-all definition will limit a Regional Director's ability to address risks unique to a region. We also reiterate that nationally a large number of companies may be in severe financial distress, but their status may not be apparent outside a limited circle of creditors, advisers, customers, and employees.

Furthermore, we note that the field definitions provided in the draft report, while using different language, are complementary in nature, and represent a general understanding within field offices of the contours of the term severe financial hardship. We do not believe the lack of a formal definition has resulted in any investigations improperly being coded as REACT.

#### **Training and best practices**

As the OIG draft report stated, comprehensive REACT training was provided at the inception of the project. Since then, the National Office has provided guidance through conference calls, the EBSA intranet site, and training at EBSA managers' conferences. In addition, in quarterly training for investigative staff (not only the REACT Coordinators), regional offices have periodically included modules on either REACT or bankruptcy on an as-needed basis (as determined by the Regional Director). Finally, the REACT Coordinators are able to contact the National Office to help resolve technical or procedural questions.

The OIG draft report correctly observes that EBSA does not view best practices as mandates. Best practices are suggestions that, if applicable in a given region, may help the region to achieve its goals more efficiently. According to the United States Government Accountability Office (GAO), best practices are the processes, practices, and systems identified in leading organizations. However, the GAO cautions that before implementing wholesale changes to emulate best practices, it is important for an organization to understand the similarities and differences between its own setting and the context from which the best practice was taken.<sup>1</sup> In EBSA, best practices are identified, consolidated and shared by a best practices committee. However, each Regional Director has a unique and unparalleled understanding of the nature and risks of his or her region. Therefore, Regional Directors should retain the discretion with respect to implementing best practices. We also note that, while discussing best practices in its 2002 Congressional Report on the Pension Welfare Benefits Administration,<sup>2</sup> the GAO did not state that best practices should be mandated.<sup>3</sup>

<sup>1</sup> <http://www.gao.gov/bestpractices/>

<sup>2</sup> EBSA was known as the Pension and Welfare Benefits Administration prior to February 3, 2003

<sup>3</sup> <http://www.gao.gov/new.items/d02232.pdf>

### **REACT Evaluations**

EBSA's Office of Enforcement formally evaluates each region's enforcement performance (including REACT) at the end of each fiscal year. The regional REACT evaluation is based on both qualitative and quantitative factors, derived from case statistics and the National Office REACT Coordinator's knowledge of the program in each region. The National Office REACT Coordinator's knowledge is derived, in part, from individual calls that take place at least once a year.

At midyear, each Regional Director is also given an informal oral evaluation that includes the REACT "progress check" referenced in the OIG draft report. The "progress check" is not only an identification of areas of potential improvement, it also identifies positive aspects of the project's implementation in each region. The overall purpose of the "progress check" is to discuss the region's apparent ability to meet its goals by the end of the fiscal year. Therefore, no regions were falling short of project expectations at midyear 2009.

The OIG draft report also states that EBSA did not have a comprehensive method for measuring the desired activities and outcomes of the REACT project, because the quantitative measures used do not measure the timeliness of EBSA's investigative actions. The performance measures used for the REACT project do not focus on investigative steps such as the timeliness of investigative actions, which are issues of case quality. Instead, they focus on investigative outcomes, such as whether fiduciary violations were found and corrected. Partly in order to monitor the quality of the investigation, including whether all necessary steps were taken in a timely manner, supervisory personnel review case files. In addition, ten percent of all cases closed by EBSA are randomly sampled and comprehensively reviewed for case quality. This robust process allows EBSA to ensure that casework is conducted in accordance with agency objectives. We also note that, as stated in the OIG draft report, an aggregate of the quantitative measures compiled by EBSA allows the agency to monitor how the REACT project is performing. Furthermore, as part of its annual planning process, the agency determines whether the REACT project should remain a national enforcement project.

The OIG draft report correctly states that EBSA's performance measures are based on the measure used under the Government Performance and Results Act of 1993 (GPRA), and do not include the preliminary research conducted by the REACT Coordinators. The preliminary research conducted by the Coordinators is not quantifiable if it does not result in a case opening. For example, if a Coordinator speaks to a bankruptcy trustee and informs the trustee of his responsibilities under ERISA, there is no quantifiable measure for the future ERISA violations that the trustee may not commit due to that interaction.

EBSA has spent over ten years attempting to create a pure outcome measure for the work generally undertaken by its enforcement program and recognizes that such a measure is, at best, extremely difficult. This problem is faced by other law enforcement agencies as well as EBSA and the difficulty of creating such a measure has been acknowledged by external reviewers and performance management experts. Instead, a variety of surrogate measures, such as cases closed

with fiduciary results, are used in conjunction with other data to measure the level of success of the EBSA's enforcement program, including the REACT project. Based on EBSA's experience in developing performance measures, we do not believe it is possible to create a measurement for the Coordinators' preliminary research.

#### **OIG Recommendations**

**Recommendation 1: EBSA should strengthen standard policies and/or procedures for the REACT project to create consistency among all the regional offices. Specifically,**

**a. establish a definition of and a methodology for assessing "severe financial hardship;"**

We continue to believe that establishing a fixed definition of "severe financial hardship" would unduly constrain Regional Directors' discretion to target areas of risk within their respective jurisdictions, to the significant detriment of the project. At the same time, we recognize the need for a degree of uniformity in the manner in which the project is implemented. We agree to establish a list of criteria that regions should consider when determining whether a company is experiencing "severe financial hardship."

**b. implement recurring REACT training and/or create a training manual for REACT Coordinators;**

Regional REACT Coordinators receive recurring and extensive training through a variety of means, including in-depth teleconferences conducted by the National REACT Coordinator, specific guidance issued by the National Office and made available to everyone in the field on EBSA's intranet site, training workshops conducted at national managers' conferences and replicated in various field offices as needed, and ad hoc communication with the National REACT Coordinator on individual technical and procedural issues. We agree to continue providing recurring training and to consolidate this information into a manual for use in training new REACT Coordinators.

**c. require REACT Coordinators to routinely communicate with and obtain information from U.S. Bankruptcy Trustees;**

We will reiterate to the field the importance of ongoing communication with U.S. Bankruptcy Trustees. However, an inflexible requirement to obtain information is impractical because EBSA cannot predict the ability of Trustees to provide desired information.

**d. implement best practices across all regions; and**

Consistent with GAO's approach to best practices, EBSA will continue to identify and share best practices among the regions, incorporating them into the ongoing training provided to the regional REACT Coordinators (identified in 1.b., above). Field office performance will be evaluated, as it has been, based on program accomplishments,

measured against expectations as developed each year in the enforcement program's Program Operating Plan. Field office utilization of best practices is an important part of that evaluation.

**e. require the investigators to document when and how they have advised all affected plans of the bankruptcy filing.**

We agree with this recommendation, and will amend the Enforcement Manual to reflect this requirement.

**Recommendation 2: Establish a performance measure(s) to accurately capture the REACT program's impact – specifically measure the results of the preliminary research the REACT Coordinators perform on bankrupt companies.**

We disagree with this recommendation. EBSA's accepted GPRA measure already reflects to some degree the value of preliminary research in identifying fiduciary breaches. Moreover, as previously stated, there is no way to practically measure the outcome of the preliminary research conducted by REACT Coordinators.

**Recommendation 3: Develop an overall REACT project assessment that incorporates the regional assessments to determine whether the project is accomplishing its goal.**

We believe that the REACT project should continue to be assessed on an annual basis in order to determine whether it is accomplishing its goal. However, we agree that it would be beneficial to develop a formal REACT project assessment. An overall REACT project assessment, which takes into account the regional project assessments, will be conducted starting in fiscal year 2010.

**Conclusion**

Through its civil and criminal enforcement program, EBSA plays an essential role in protecting the integrity of retirement and welfare benefits of over 150 million people. Although EBSA has a comparatively small investigative staff relative to other enforcement agencies and the size of the employee benefits universe, we have successfully leveraged our resources to achieve over \$1 billion in monetary results for each of the past six fiscal years. In the first six months of fiscal year 2009, EBSA has achieved over \$113 million in results through the REACT project alone.

The REACT project has played an important role in meeting EBSA's mission of successfully deterring and correcting violations of ERISA and other relevant statutes, assisting workers in getting the information they need to exercise their benefit rights, and assisting plan officials in understanding the requirements of the relevant statutes in order to meet their legal responsibilities. One of the strengths of the REACT project, like EBSA's enforcement program overall, is that it gives Regional Directors discretion in order to face risks unique to their region, which is essential given the rise in bankruptcy filings and increase in the number of companies facing severe financial hardship.