



U.S. RAILROAD RETIREMENT BOARD

OFFICE OF INSPECTOR GENERAL

Enterprise Risk Management Process At The Railroad Retirement Board Was Not Fully Effective

Report No. 18-07

July 9, 2018

OFFICE OF INSPECTOR GENERAL
U.S. RAILROAD RETIREMENT BOARD
Enterprise Risk Management At The
Railroad Retirement Board Was Not Fully Effective



What We Found

Our audit determined that the Railroad Retirement Board's (RRB) Enterprise Risk Management (ERM) process was not fully effective. RRB had not complied with all of the internal control requirements in Office of Management and Budget (OMB) revision of OMB Circular A-123, *Management's Responsibility for Enterprise Risk Management and Internal Control*, and did not implement the ERM process agencywide. Agencies are required to develop and maintain a risk profile that identifies risks arising from mission and mission support operations. We identified weaknesses in the RRB's risk profile. We also found that RRB management had not implemented our recommendations in a timely manner. We identified 191 audit recommendations that management concurred with that have remained open for a calculated average of four and a half years as of September 30, 2017.

What We Recommend

To address the weaknesses identified in this audit, we made 10 recommendations related to improving the ERM process at the RRB that included: implementing an ERM process agencywide, assigning a Chief Risk Officer to manage enterprise risk activities, updating agency guidance for the ERM process, improving supporting documentation for the risk profile, including critical agency operations currently omitted from the risk profile, acknowledging Office of Inspector General identified material weaknesses in the risk profile and revising assessments accordingly, establishing a timeframe for closing audit recommendations, and monitoring open audit recommendations to ensure timely closures. RRB management concurred with nine recommendations and did not concur with one recommendation.

What We Did

OMB Circular A-123 was updated to ensure federal managers are effectively managing risks in achieving their strategic objectives from its activities and operations. This guidance was issued in July 2016 and became effective in fiscal year 2017. Our objective was to assess the effectiveness of the ERM process at the RRB. In order to complete this work, we considered laws and regulations, and compared criteria to RRB policies, procedures, and documentation to determine compliance, and reviewed agency documentation to assess effectiveness. We also interviewed applicable agency staff.

The scope of the audit was the ERM process during fiscal year 2017.

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INTRODUCTION

This report presents the results of the Office of Inspector General’s (OIG) audit of the enterprise risk management (ERM) process at the Railroad Retirement Board (RRB).

The Office of Management and Budget (OMB) revised Circular A-123, *Management’s Responsibility for Enterprise Risk Management and Internal Control* (OMB A-123) in July 2016.¹ ERM implementation requirements became effective in fiscal year 2017. ERM is a discipline that deals with identifying, assessing, and managing risks. It provides an enterprise wide, strategically aligned portfolio view of organizational challenges that provides better insight about how to most effectively prioritize resource allocations to ensure successful mission delivery. Revised OMB A-123 emphasizes the importance of coordinating ERM activities with the strategic planning and review process, and internal controls required by the Federal Managers’ Financial Integrity Act (FMFIA) and Government Accountability Office’s (GAO) *Standards for Internal Control in the Federal Government* (GAO Standards).²

Objective, Scope, and Methodology

The audit objective was to assess the effectiveness of the ERM process at the RRB.

The scope of the audit was the ERM process during fiscal year 2017.

To accomplish the audit objective, we

- identified criteria provided in OMB A-123, FMFIA, and GAO Standards;
- compared criteria to agency policies, procedures, and documentation to determine compliance;
- reviewed agency documentation to assess effectiveness; and
- interviewed applicable agency staff.

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective. We did not test internal controls because we found the agency had not developed internal controls specific to the ERM process.

We conducted our fieldwork at RRB headquarters in Chicago, Illinois from January 2018 through May 2018.

¹ Office of Management and Budget, *Management’s Responsibility for Enterprise Risk Management and Internal Control*, Circular A-123, M-16-17 (Washington, D.C: July 15, 2016).

² Pub. L. No. 97-256, 96 Stat. 814 (1982) and Government Accountability Office (GAO), *Standards for Internal Control in the Federal Government*, GAO-14-704G (Washington D.C.: September 2014).

Background

OMB A-123 specifies that each year agencies develop and maintain a risk profile coordinated with their strategic reviews. Risk profiles identify risks arising from mission and mission support operations. The primary purpose of a risk profile is to provide a thoughtful analysis of the risks an agency faces toward achieving its strategic objectives arising from its activities and operations, and to identify appropriate actions for managing the risk, known as the Current Risk Response. An appropriate response includes implementation of formal internal control activities that conform to GAO Standards.

RRB management and internal control policies and structures are governed by:

- Executive Committee, which functions as the agency's senior management council that assesses and monitors deficiencies in internal control. Under the direction and leadership of the Senior Executive Officer, the Executive Committee oversees daily agency operations and is responsible for oversight and problem solving regarding cross organizational internal control issues.
- Management Control Review Committee (MCRC) also has agencywide internal control responsibilities. The MCRC prepares internal control documents required by the FMFIA for inclusion in the agency's annual Performance and Accountability Report (PAR). MCRC was established to oversee a process to identify and eliminate management control weaknesses and financial nonconformance.
- RRB organizational heads are responsible for installing, maintaining, monitoring, revising, and enforcing management controls within their organizations. The RRB defines assessable units (AU) for agency activities that can impact its mission.

RESULTS OF AUDIT

Our audit determined that the RRB’s ERM process was not fully effective. RRB had not complied with all of the internal control requirements in OMB A-123 and did not implement the ERM process agencywide. Further, we identified risk profile weaknesses and found that audit recommendations were not being addressed timely.

We made ten recommendations aimed at addressing these weaknesses. The full text of management’s responses is included in the appendices.

RRB Enterprise Risk Management Process Was Not Fully Effective

Our audit determined that the RRB’s ERM process was not fully effective. RRB had not complied with all of the internal control requirements in OMB A-123 and did not implement the ERM process agencywide.

RRB Did Not Comply With Office of Management and Budget Internal Control Requirements

RRB had not evaluated whether agencywide internal controls reduced the risk of not achieving the entity’s objectives related to operations, reporting, or compliance to an acceptable level, as required by OMB A-123.

GAO Standards provide the internal control framework and criteria that Federal managers must use in designing, implementing, and operating an effective system of internal control. OMB Circular A-123 states that evaluation of internal controls must be performed for the agency as a whole. OMB A-123 requires evaluation of internal controls following a risk assessment approach:

1. Conduct an evaluation of internal controls for each of the 17 principles (see Appendix II) for each of the entity objectives.³
2. Prepare a summary of internal control deficiencies.
3. Summarize its determination of whether each principle is designed, implemented, and operating effectively.
4. Summarize its determination of whether each component (Control Environment, Risk Assessment, Control Activities, Information and Communication, and Monitoring) is designed, implemented, and operating effectively.
5. Conclude on an overall system of internal control.

³ GAO-14-704G.

RRB management stated that its evaluation of internal controls is driven by the FMFIA and that its approach for reviewing internal controls at the AU level satisfies most of the 17 GAO principles. We found evidence that RRB management complied with some OMB A-123 internal control requirements that included preparation of a risk profile and evaluation of the control environment. While the overall system of internal control addresses the agency's control environment, this is only one of the five required components. There is no evaluation using the OMB A-123 risk based assessment approach at the agencywide level for the other components of risk assessment, control activities, information and communication, and monitoring. Because the required evaluations were not made, any improvements needed for internal controls over operations, reporting, and compliance might not have been identified.

We also found that the Current Risk Response provided in the RRB's initial risk profile did not identify the internal control activities provided in GAO Standards that should be implemented to reduce risk. OMB A-123 states, as part of developing the risk profile, management must determine those risks for which the appropriate response includes implementation of formal internal control activities which conform to standards published by the GAO. These include those risks that meet each of the criteria:

- The agency is working to reduce exposure to risk.
- The objective is related to reporting, compliance or operations.
- The risk is identified in the Agency Risk profile as at least medium impact and medium likelihood.
- Control objectives can be clearly specified.

Recommendations

We recommend that the Management Control Review Committee:

1. establish an internal control evaluation based on the requirements provided in the revised Office of Management and Budget Circular A-123; and
2. implement formal internal control activities in the Current Risk Response portion of their risk profile.

Management's Comments

The Management Control Review Committee concurred with these recommendations.

Enterprise Risk Management Has Not Been Implemented Agencywide

RRB had not implemented the ERM process agencywide. OMB A-123 defines ERM as an agencywide approach to addressing the full spectrum of the organization's external and internal risks by understanding the combined impact of risks as an interrelated portfolio. The

RRB addressed risks by AU, requiring periodic risk assessments during the Management Control Review (MCR). The risk assessment is a Responsible Official's determination of an

AU vulnerability to inherent risks associated with accomplishment of its mission and integrity risks associated with occurrences of waste, loss, unauthorized use, or misappropriation. The effect of this approach is a narrow focus that does not address risks that span across the enterprise.

OMB A-123 defines risk appetite as the broad-based amount of risk an organization is willing to accept in pursuit of its mission. Tolerance level is the acceptable level of variance in performance relative to the achievement of objectives. The concept of risk appetite is key to achieving effective ERM, and is essential to consider in determining risk responses. While the agency developed a risk profile utilizing the necessary components, it did not include a process for considering risk appetite and tolerance level in developing its risk response. Although a formally documented risk appetite statement is not required, agencies must have a solid understanding of their risk appetite and tolerance level in order to create a comprehensive enterprise-level risk profile.

While not required, OMB A-123 states that a Chief Risk Officer, or equivalent function, champions agencywide efforts to manage risk and advise senior leaders on the strategically aligned portfolio view of risks. The RRB does not have a Chief Risk Officer.

RRB management stated that the MCRC does not have a process to track changes in internal control guidance. As our audit progressed, management recognized the need to notify MCRC members of the revised OMB A-123 guidance. This notification was issued in March 2018, almost a year and a half after the guidance became effective. The RRB has not made implementation of ERM a priority. Key management officials such as the Chairman of the MCRC, and the Director of Audit Affairs and Compliance did not attend ERM training until March 2018.

Without an effective ERM process in place that clearly identifies, categorizes, and assesses the effectiveness of controls related to key risks, the FMFIA annual assurance statement may not clearly reflect the RRB's internal control environment, including risks.

RRB's Management Control Guide (MCG) was the primary source of guidance for managers implementing management control policies and accomplishing management control objectives. RRB has not updated their policies and procedures to reflect ERM guidance. While the MCG was revised in February 2017, it does not include any of the guidance from the revised OMB A-123.

GAO Standards state,

“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.”⁴

⁴ GAO 14-704G.

Whenever documented policies and procedures are lacking or outdated, individuals in the organization are unaware of their responsibilities. There is also the risk that knowledge of operations is limited to fewer personnel. Management's assertions cannot be validated without documented or updated policies and procedures.

Recommendations

We recommend that the:

3. Executive Committee implement an agencywide enterprise risk management program;
4. Executive Committee assign an individual as the Chief Risk Officer, or equivalent, who manages enterprise risk activities at the RRB; and
5. Management Control Review Committee update the Management Control Guide to reflect enterprise risk management guidance provided in Office of Management and Budget Circular A-123.

Management's Comments

The Executive Committee concurred with recommendations 3 and 4. The Management Control Review Committee concurred with recommendation 5.

Initial Risk Profile Concerns

While RRB developed an initial risk profile in June 2017 that contained the required components, we found that RRB did not (1) have current documentation to support its assessments, (2) include critical agency operations, and (3) include OIG cited material weaknesses. OMB A-123 requires annual preparation of a risk profile. The risk profile assists in facilitating a determination around the aggregate level and types of risk that the agency and its management are willing to assume to achieve its strategic objectives. The development of an agency risk profile

- encourages open and candid conversations about risks facing an organization at all levels;
- facilitates the ranking of risk priorities (in particular to identify and escalate the most significant risks of which senior management should be aware);
- captures the reasons for decisions made about risk tolerances;
- facilitates recording of the way in which it is decided to address risk;
- allows leadership at all levels to understand the overall risk profile and how their areas of particular responsibility fit into it; and
- facilitates the review and regular monitoring of risks.

Lack of Current Support for Assessments

RRB assessments of risk in its initial risk profile were not supported. RRB activities are divided into 44 AU. For some Current Risk Responses provided in the initial risk profile, the RRB used risk assessments evaluated through the MCR process. MCR’s are scheduled to occur on a three to five year cycle as determined by the MCRC.

For some of the AU, the risk assessments used in the initial risk profiles relied on outdated management control reviews that had not been tested for several years and one that had not been tested in five years.

Assessments of risk were based on information from the fiscal year 2016 FMFIA report. Our review of the risk assessments for the 18 AU for the Office of Programs area in the risk profile showed that 15 of the risk assessments took place between 2012 and 2015 (see Table 1).

Table 1. Office of Programs Risk Assessments

Year of Last Risk Assessment	Number of Assessable Units
2012	1
2013	3
2014	5
2015	6
2016	0
2017	<u>3</u>
Total	18

Source: OIG Analysis of Risk Assessments

We also found that while Actuarial Services and Debt Recovery AU were specifically identified as being regularly evaluated through the RRB’s MCR process as part of the Current Risk Response, the most recent MCRs took place on September 3, 2013 and May 7, 2014, respectively.

We addressed these concerns with RRB management and they stated that annual certifications are also prepared for each AU, which state whether control objectives are being accomplished. RRB management also stated that each responsible official should have documentation to support the statements made in their annual certifications. Annual support is not required by the MCRC. The MCRC requires support when the management control reviews are conducted every three to five years. For AU where there have been recent changes in three to five years, prior control testing may not be reliable for ongoing assessments of the effectiveness of the controls. We noted that 17 of the 20 AU discussed in this finding did not have current internal control tests despite annual certifications.

According to GAO Standards, “[t]ransactions are promptly recorded to maintain their relevance and value to management in controlling operations and making decisions.”

In order for risk responses to be meaningful, management control reviews should be conducted on a timely basis.

Critical Information and OIG Cited Material Weaknesses Not Included

Only 31 of the RRB's 44 AU were included in the Current Risk Response in its initial risk profile. Of the remaining 13 not included, we identified 4 AU that we believe are critical to the agency's strategic goals, namely:

- Issuing Decisions on Appeals – Responsible for performance goal I-A-9, that is, the timeframe between the date an appeal is filed and a decision is rendered.
- Unemployment Benefits – Responsible for performance goals II-A, Pay benefits timely; and II-B, Ensure the accuracy and integrity of benefit payment programs.
- Data-Object Life Cycle – Responsible for numerous key indicators relating to Strategic Goal II, Serve as responsible stewards for our customers' trust funds and agency resources.
- Employer Audits – Work of this AU impacts performance goals I-A, Pay benefits timely; and II-A, trust fund assets are protected, collected, recorded, and reported appropriately.

These AU were not included in the initial risk profile because RRB management did not feel that they provided significant risks. The omission of critical information from the risk profile does not ensure all risks are being identified or the appropriate response is being provided.

OIG reported two material weaknesses in financial reporting in fiscal year 2016. Financial reporting is classified as a material weakness due to ineffective controls for material transactions and because of RRB management's unwillingness to provide OIG auditors with cooperation and communication with National Railroad Retirement Investment Trust auditors. In fiscal year 2016, the OIG also identified a material weakness in the RRB's control environment because the enforce accountability principle is ineffective.

RRB management explained that these material weaknesses were not included in the initial risk profile because they did not concur with them. Because the initial risk profile is required to be provided to OMB, the material weaknesses should be referenced even if RRB management does not agree with them. Omission of such references prevents report recipients from being fully informed of the existing internal control assessments. Although the RRB does not agree with OIG cited material weaknesses, it refers to these weaknesses in its annual FMFIA report and in the fiscal year 2017 Performance and Accountability Report, Management Assurances section. In the annual FMFIA report, RRB provides the reasons for its disagreement. Consistent reporting is needed for RRB documents that pertain to agencywide internal controls.

OMB A-123 states that in completing their risk profiles, agencies may consider reviewing and incorporating results from existing documentation such as GAO and OIG audit findings, OIG’s annual report on top performance and management challenges, and FMFIA documentation. By excluding material weaknesses from its risk profile, the RRB does not provide an accurate indication of risks associated with financial reporting compliance.

Recommendations

We recommend that the Management Control Review Committee:

6. document and maintain current support for Risk Profile determinations;
7. include assessable units in risk profile that are critical to the RRB’s strategic goals; and
8. acknowledge material weaknesses and revise assessments accordingly in the next risk profile.

Management’s Comments and Our Response

The Management Control Review Committee concurred with recommendations 6 and 7, but did not concur with recommendation 8. The MCRC stated that RRB management did not concur with the referenced material weaknesses when they were originally proposed by the OIG and therefore RRB management will not acknowledge them.

The OIG continues to assert the need for RRB management to mention the OIG cited material weaknesses in its risk profile even if RRB management does not concur with them. Making reference to the material weaknesses would provide complete transparency for OMB as the recipient of the risk profile. Omission of reference to these material weaknesses could impact the purposes for which OMB utilizes the risk profile.

Audit Recommendations Are Not Being Corrected Timely

Despite management concurrence with recommendations, many are not implemented in a timely manner. We identified 191 audit recommendations that management concurred with and remain open, all of which are over a year old as of September 30, 2017. We calculated the average length of time these audit recommendations have remained open as four and a half years as of September 30, 2017.

OMB A-123 states,

“Management has a responsibility to complete action, in a timely manner, on audit recommendations on which agreement with the OIG has been reached. Management must make a decision regarding OIG audit recommendations within a six-month period after issuance of the audit report and implement management’s decision within one year to the extent practicable.”

Management has not taken the actions necessary to resolve these open recommendations. Deficiencies that have been identified and not corrected timely are an indicator of the strength of an agency's internal control environment and can lead to potential increase in risks in internal controls and operating effectiveness.

Recommendations

We recommend the Management Control Review Committee:

9. establish a policy in Management Control Guide identifying timeframe for closing open audit recommendations upon which concurrence has been reached; and
10. monitor audit recommendations on a regular basis and take action to ensure they are closed in the required timeframe.

Management's Comments

The Management Control Review Committee concurred with these recommendations.

APPENDIX I: MANAGEMENT COMMENTS



UNITED STATES GOVERNMENT

FORM 6-1157(1)-22

MEMORANDUM

RAILROAD RETIREMENT BOARD

June 29, 2018

TO: Heather J. Dunahoo
Assistant Inspector General for Audit

**TIMOTHY
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ON**

Digitally signed by TIMOTHY
HOGUEISSON
DN: c=US, o=U.S. Government,
ou=Railroad Retirement Board,
cn=TIMOTHY HOGUEISSON,
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Date: 2018.06.29 13:45:24
-0500

FROM: Timothy Hogueisson
Chairman, Management Control Review Committee

SUBJECT: Management Response to Draft Report of Audit *Enterprise Risk Management at the Railroad Retirement Board Was Not Fully Effective*

The Management Control Review Committee (MCRC) CONCURs that the Railroad Retirement Board Enterprise Risk Management (ERM) process was not fully compliant with Office of Management and Budget (OMB) and Government Accountability Office (GAO) requirements.

Recommendation 1. We recommend that the MCRC establish an internal control evaluation based on the requirements provided in the revised OMB Circular A-123.

Management Response 1. CONCUR. Estimated completion date December 30, 2018.

Recommendation 2. We recommend that the MCRC implement formal internal control activities in the Current Risk Response portion of their risk profile.

Management Response 2. CONCUR. Estimated completion date December 30, 2018.

Recommendation 5. We recommend that the MCRC update the Management Control Guide to reflect enterprise risk management guidance provided in Office of Management and Budget Circular A-123.

Management Response 5. CONCUR. Estimated completion date June 30, 2019.

Recommendation 6. We recommend that the MCRC document and maintain current support for Risk Profile determinations.

Management Response 6. CONCUR. Estimated completion date December 30, 2018.

Recommendation 7. We recommend that the MCRC include assessable units in risk profile that are critical to the RRB's strategic goals.

Management Response 7. CONCUR. Estimated completion date December 30, 2018.



UNITED STATES GOVERNMENT

FORM 6-1157(11-32)

MEMORANDUM

RAILROAD RETIREMENT BOARD

Recommendation 8. We recommend that the MCRC acknowledge material weaknesses and revise assessments accordingly in the next risk profile.

Management Response 8. NON-CONCUR. The RRB non-concurred with the material weaknesses when the OIG initially proposed them. It is irrational to presume the RRB will acknowledge the same material weaknesses within the ERM process that we do not agree exist.

Recommendation 9. We recommend that the MCRC establish a policy in Management Control Guide identifying timeframe for closing open audit recommendations upon which concurrence has been reached.

Management Response 9. CONCUR. The MCRC will update the Management Control Review (MCR) Guide to reflect the language contained in OMB guidance and referenced in the report of audit. Estimated completion date September 30, 2018.

Recommendation 10. We recommend that the MCRC monitor audit recommendations on a regular basis and take action to ensure they are closed in the required timeframe.

Management Response 10. CONCUR. Estimated completion date September 30, 2018.

cc: Shawna Weekley, Chief Financial Officer
Jeffery Baer, Director of Audit Affairs & Compliance
Debra Wheat, Supervisory Auditor

APPENDIX II: MANAGEMENT COMMENTS



UNITED STATES GOVERNMENT

FORM R-115f (1-92)

MEMORANDUM

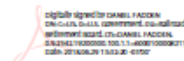
RAILROAD RETIREMENT BOARD

June 29, 2018

TO: Heather J. Dunahoo
Assistant Inspector General for Audit

FROM: Daniel Fadden
Senior Executive Officer/Director of Field Service

DANIEL
FADDEN



SUBJECT: Management Response to Draft Report of Audit *Enterprise Risk Management at the Railroad Retirement Board Was Not Fully Effective*

The Railroad Retirement Board (RRB) **CONCURS** that our Enterprise Risk Management (ERM) process was not fully compliant with Office of Management and Budget and Government Accountability Office requirements.

Recommendation 3. We recommend that the Executive Committee implement an agency-wide enterprise risk management program.

Management Response 3. **CONCUR.** Estimated completion date July 31, 2019.

Recommendation 4. We recommend that the Executive Committee assign an individual as the Chief Risk Officer, or equivalent, who manages enterprise risk activities at the RRB.

Management Response 4. **CONCUR.** Estimated completion date July 31, 2018.

cc: Shawna Weekley, Chief Financial Officer
Jeffery Baer, Director of Audit Affairs & Compliance
Debra Wheat, Supervisory Auditor

APPENDIX III: INTERNAL CONTROL COMPONENTS AND PRINCIPLES AS DEFINED BY THE GOVERNMENT ACCOUNTABILITY OFFICE⁵

Control Environment

1. The oversight body and management should demonstrate a commitment to integrity and ethical values.
2. The oversight body should oversee the entity's internal control system.
3. Management should establish an organization structure, assign responsibility, and delegate authority to achieve the entity's objectives.
4. Management should demonstrate a commitment to recruit, develop, and retain competent individuals.
5. Management should evaluate performance and hold individuals accountable for their internal control responsibilities.

Risk Assessment

6. Management should define objectives clearly to enable the identification of risks and define risk tolerances.
7. Management should identify, analyze, and respond to risks related to achieving the defined objectives.
8. Management should consider the potential for fraud when identifying, analyzing, and responding to risks.
9. Management should identify, analyze, and respond to significant changes that could impact the internal control system.

Control Activities

10. Management should design control activities to achieve objectives and respond to risks.
11. Management should design the entity's information system and related control activities to achieve objectives and respond to risks.
12. Management should implement control activities through policies.

⁵ Government Accountability Office (GAO), *Standards for Internal Control in the Federal Government*, GAO-14-704G (Washington D.C.: September 2014).
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Information and Communication

13. Management should use quality information to achieve the entity's objectives.
14. Management should internally communicate the necessary quality information to achieve the entity's objectives.
15. Management should externally communicate the necessary quality information to achieve the entity's objectives.

Monitoring

16. Management should establish and operate monitoring activities to monitor the internal control system and evaluate the results.
17. Management should remediate identified internal control deficiencies on a timely basis.