



PENSION BENEFIT GUARANTY CORPORATION

Semiannual Report to the Congress

Management's Response to the OIG Semiannual Report:

October 1, 2013 – March 31, 2014

Office of the Director
Washington, D.C.

PENSION BENEFIT GUARANTY CORPORATION

MANAGEMENT'S RESPONSE TO OIG SEMIANNUAL REPORT

Foreword

This document summarizes our efforts to implement OIG recommendations and to maintain and improve our internal controls.

During the reporting period, PBGC received our 21st consecutive clean audit opinion on our financial statements for FY 2013. PBGC is proud to have met this standard. With the oversight of the OIG, the independent auditor, CliftonLarsonAllen LLP, also noted that three previously-reported material weaknesses in internal controls continue to exist. PBGC is continuing its concerted, corporate-wide effort to respond and correct them. This response describes our actions to improve information security, access controls and configuration, and benefits administration and payment operations. Providing retirement security is PBGC's mission. Americans rely on our protection when their companies have failed and their retirements have been shaken. They must have confidence in PBGC. If there is any doubt about the agency's integrity or competence, it undermines that mission. For that reason, we appreciate the work of our OIG. They provide constant and knowledgeable oversight; even when we ultimately decide upon a different approach, we take their recommendations very seriously. PBGC, an excellent agency, is a better one for OIG's efforts, and we strive to make it better still.

Our Commitment to Excellence and Accountability

It is important that we do our job right, with accountability and integrity. Our participants and other stakeholders expect nothing less. Millions are relying on PBGC to fulfill its mission, and we are proud of our record of efficiency, effectiveness, and professionalism.

Having said that, there remains much to do. We owe our participants our best efforts in ensuring the accuracy of plan asset audits and resulting benefit determinations. Advances in technology and understanding of information security pose a constant challenge to adapt and improve. Since our activities involve complex judgments by hundreds of people about hundreds of different situations, our procedures, controls, and financial systems must continually be both applied and reevaluated.

Audits conducted by the OIG and the GAO are an essential component of promoting the accountability of PBGC management to stakeholders. PBGC is committed to supporting and cooperating with the entire audit process, from the announcement of the audit to completion of audit follow-up activities. All employees and contractors are directed to cooperate and support the audit process, and directly report concerns about potential fraud, waste, or abuse without fear of reprisal. PBGC management officials strive for the prompt and proper resolution and

implementation of agreed-upon audit recommendations, and maintain a complete record of actions taken in response to those recommendations.

Since joining the agency, the Director of PBGC has worked to improve the professional relationship between the PBGC and OIG. Management values the OIG's role in promoting accountability and look forward to a continued positive working relationship.

The OIG's Semiannual Report to Congress and PBGC Management's Response (the report you're reading) both play an important role in providing accountability for the accomplishment of PBGC's mission, improving our internal controls, and addressing OIG recommendations.

PBGC's Mission

PBGC's control environment is best understood in relation to PBGC's overall mission:

Preserving Plans & Improving Retirement Security - Although PBGC is best known for paying benefits after plans fail, ERISA charges the agency with supporting the "continuation and maintenance of voluntary private pension plans for the benefit of their participants." PBGC takes this important obligation very seriously and took the following actions within the reporting period:

- when former Hostess Brands employees were faced with the impending loss of retirement benefits, PBGC used its partition authority to prevent the multiemployer plan from failing;
- when more than 19,000 current and future retirees of Furniture Brands International, Inc. faced an uncertain future due to the company's bankruptcy, PBGC stepped in to provide peace of mind through our insurance protection;
- To ease the regulatory burden on plan sponsors, PBGC improved the premium payment rules, enabling large plans to pay once per year instead of twice, and giving small plans additional time to calculate variable-rate premiums.

Paying Benefits On Time - PBGC's primary focus is to make sure that those who depend on us for their retirement security keep getting their benefits and are paid on time. We are proud of the fact that, of the thousands of pension plans for which we have become responsible and the hundreds of thousands of retirees under those plans, not a single payment has ever been interrupted. For FY 2013, we paid over 850,000 participants a total of nearly \$5.5 billion in pension benefits. We also paid out \$89 million to benefit another 50,000 participants in multiemployer pension plans. We continually refine our practices and procedures to provide the best possible service to those whom we insure. Retirees receiving benefits from PBGC rank us at the top of government agencies in terms of their satisfaction with our service – for FY 2013,

we received a 90 rating from The American Customer Satisfaction Index (ACSI), a rating of 80 or above is considered excellent.

Paying the Right Benefit - Each pension plan is different, and PBGC issued 79,000 benefit determination letters during FY 2013. Under the law, PBGC must pay beneficiaries their *accrued vested* plan benefit *up to* the maximum permissible under Federal law. This requires the PBGC to learn and apply both tests to every person when we become responsible for a plan -- often without the help of the previous plan administrators. While we do so, we pay current benefits. (However, if current benefits are more than the legal maximums, we are required to recoup the difference over time.) We also seek out new ways to prevent improper payments and were pleased that the OIG again found PBGC to be in compliance with the Improper Payments Information Act for FY 2013. (For more on our work in preventing improper payments, see page 8, below.)

Acquiring Plan Assets, not just Obligations - Since the PBGC becomes responsible for paying a plan's benefits, it's important that we also get the plan's assets -- its invested funds -- as well as pursuing funds from the plan's sponsor to fulfill its obligations under Federal law. We do this by acquiring the assets and negotiating settlements or litigating with the plan sponsors.

Maintaining Fiscal Integrity - PBGC is self-financed and receives no funds from general tax revenues. We make every effort to collect premiums due and to manage our investments for the benefit of our participants and our insurance programs. For FY 2013, we collected over \$3 billion in premiums from more than 24,000 ongoing plans, had about \$75 billion in investments under management, and posted over \$2.6 billion in investment earnings.

Doing Our Work Accountably - Being a public agency with public responsibilities for plans involving millions of people and hundreds of billions in funds means we have an obligation to do our work to the highest standards of accountability. We are proud of the fact that, for the past 21 years, our accounts have received a clean audit opinion. Our accounts are audited annually by our OIG's external auditors, and our practices and procedures are reviewed by our OIG, as well as by the Government Accountability Office (GAO). This report is focused on these activities.

A "Clean" Annual Financial Statement Audit

During the reporting period the OIG, and its external auditors, CliftonLarsonAllen LLP, completed work on the financial statements for the 2013 fiscal year. As noted above, in November 2013, PBGC received an unmodified ("clean") opinion on its financial statements -- its 21st in a row. This means that the public, policy makers, and other stakeholders can rely on the information reported in our financial statements and in the notes to the financial statements.

Material Weaknesses in Internal Control

Unlike most agencies, PBGC undergoes a separate audit of its internal controls. This additional audit measures our controls on a higher standard and requires more testing than that of the

financial statement audit. It identifies those areas where controls are adequate and where they require improvement. The OIG and CliftonLarsonAllen reported that the previously reported material weaknesses in internal controls continue to exist, as follows:

- Entity-wide Security Program Planning and Management;
- Access Controls and Configuration Management; and
- Benefits Administration and Payment Department (BAPD) Operations.

We are working hard to address these weaknesses and improve the related controls. To that end, we agreed with the original and continuing findings of material weaknesses, and have implemented compensating controls, and continue to follow our comprehensive corrective action plans to fully remedy them. In the following paragraphs, we provide updates on how PBGC is working to remedy the material weaknesses:

The Agency Continues To Make Progress in Addressing Weaknesses

Information Security

The agency has taken several steps to address the material weaknesses relating to information technology. Our information technology strategic plan places information security as the core of all systems. In addition to improving PBGC's access control processes, we have acquired additional resources to address the OIG's audit recommendations identified in the material weaknesses. We have adopted best practices from other federal agencies and formed a team of specialized resources with the specific responsibility of remediating the material weaknesses. The IG and the CIO periodically meet to review progress and gain a better understanding of the differences between the OIG's expectations and PBGC's deliverables.

Benefits Administration Procedures

The Benefits Administration and Payment Department (BAPD) continued to make significant progress on the Strategic Review to transform BAPD operations. For example, BAPD has hired new plan asset valuation specialists, reworked its plan asset evaluation policies and procedures, and trained BAPD auditors, managers, and support contractors on those procedures. BAPD has also updated documentation and record retention processes and incorporated new accountability language into performance plans. To promote quality within BAPD and throughout the agency, PBGC has established a new Quality Management Department. This department will assess work processes and employ business analytics to support continuous process improvements.

PBGC Works to Improve Negotiated Funding Agreements

On March 21, 2014, the OIG issued a report on Negotiated Funding Agreements. PBGC management has agreed with all eight of the OIG findings related to monitoring and enforcement of negotiated funding agreements. Shortly after the initiation of the audit in 2011, PBGC management began making improvements to its process, controls, and automation for this activity. By March of 2013, we had implemented several new processes and controls to improve the monitoring, modification and enforcement of agreements. PBGC expects to submit requests for closure of the eight audit findings by the end of 2014.

Completing Actions & Closing out Audit Recommendations

While the number of open OIG recommendations is currently high, we are working diligently to address them. . We have focused on the very oldest recommendations and completed actions on most of them in the reporting period. In addition, to better understand our universe of OIG recommendations, we analyzed those issued over the past 10 years ending with the start of this reporting period. In this, we learned that, while much remains to be done, management has completed work on more than 70 percent of the audit recommendations issued over the past 10 years. To further assess where we are, we looked at all of the recommendations in resolved audit reports over 12 months old (See Table 1). Here again, despite the need for further efforts, we found that work has been completed on more than 70 percent of the recommendations over 12 months old.

Of the 163 open recommendations at the end of the reporting period, 30% relate to material weaknesses. During the reporting period, despite the normal inflow of 54 new recommendations from recent reports, the OIG agreed to close 64 recommendations, 8 of which related to material weaknesses. Management has taken final actions on an additional 32 recommendations and is awaiting the OIG's review. Twelve (12) of the 32 (38%) of these final actions relate to material weaknesses.

A Vigorous Process for Coordinating Audits and Recommendations

PBGC has a vigorous process in place to promote audit coordination and audit follow-up. During an audit, management seeks to ensure that the auditors are receiving the information needed from management. For example, in the financial statement audit, management tracks very closely the more than 800 different evidentiary materials requested by the auditors to make sure that the audit is successful. When management learns of an audit finding, we provide timely responses to the auditors on each finding. We respond to every draft report, as well, so that there are

seldom surprises in a final report. When final reports are issued, every recommendation is assigned to a responsible department, tracked in a central database, and reported out monthly—with estimated completion dates—to both executive management, including department directors, and the OIG. To help prevent date slippage, any change in an estimated completion date must go through a separate process that ensures executive management is aware of the change. Regular meetings with the OIG are held to ensure good communications on management’s corrective actions. When management completes action on an audit recommendation, the department director submits a package of evidence to CCRD for review. If acceptable, CCRD transmits the package to OIG for concurrence that there is sufficient evidence of the work being completed.

Success in Resolving OIG Recommendations Requiring Management Decisions

Under OMB Circular A-50, Audit Follow-up, audit recommendations are considered to be ‘resolved’ when management and the IG reach an agreed-upon management decision on how management will proceed in addressing the IG’s recommendations. Management and OIG, working together, successfully resolved a previous recommendation needing resolution by the end of the reporting period, resulting in our having no reportable unresolved recommendations. Subsequent to the period, management and OIG also worked together and resolved a newer recommendation issued near the end of the reporting period.

Maintaining Management Controls and Accountability

Everyone at PBGC has responsibility for the effectiveness of the Corporation’s internal controls. The Corporation has structured its Internal Controls Program to support compliance with Federal Manager’s Financial Integrity Act (FMFIA) and OMB Circular A-123 requirements. Within the context of our mission to provide timely, uninterrupted pension benefits, PBGC management is charged with “establishing and maintaining internal control to achieve the objectives of effective and efficient operations, reliable financial reporting, and compliance with applicable laws and regulations.” (OMB Circular A-123, *Management’s Responsibility for Internal Control.*)

PBGC’s Internal Control Committee (ICC) provides oversight and accountability for internal controls over operations, financial reporting, and compliance with laws and regulations. Chaired by the CFO, the ICC membership includes voting members from each major area of the agency, and a non-voting member from PBGC’s OIG. PBGC’s Contracts and Controls Review Department (CCRD), which facilitates ICC activities, also tests financial reporting, entity-wide, and information technology controls throughout the Corporation. Resulting reports are issued to executive management as input to control design and effectiveness decisions. Employees responsible for applicable key controls maintain logs documenting control execution, and

provided quarterly representations regarding the performance of these controls. Work under the Internal Control Program undergirds the Director's FMFIA Assurance Statement that is included in the Annual Report each fiscal year.

Management's Own FY 2013 Test Results

In addition to the testing and reporting on the Corporation's controls by OIG and GAO, PBGC is periodically subjected to other testing by external agencies, including the United States Office of Personnel Management, the Internal Revenue Service, and the Office of Government Ethics. On top of all of this, management proactively tests a plethora of its own controls each year. This testing is handled by a separate department, the Contracts and Controls Review Department, using its own trained auditors as well as well-known firms under contract to perform the tests.

PBGC's Internal Control Program is primarily focused on documenting and testing controls within the following areas: financial reporting, entity-wide, and information technology. During the year, selected controls were evaluated for the adequacy of control design and tested to determine operating effectiveness of the controls. Reports regarding results of testing were provided to PBGC management and ICC members for consideration under FMFIA.

Financial Reporting Controls: The PBGC has identified 12 major business process cycles which have a significant impact on the PBGC's financial reporting processes: Benefit Payments, Benefit Determinations, Budget, Financial Reporting, Human Resources/Payroll, Investments, Losses on Completed and Probable Terminations, Non-Recoverable Future Financial Assistance, Payables, Premiums, Single-Employer Contingent Liability, and Present Value of Future Benefits. As of the end of FY 2013, PBGC had identified 157 key controls over financial reporting for testing within these major business cycles. Employees responsible for performance of these controls maintained logs documenting control execution, and provided quarterly representations regarding the performance of those controls. For the FY 2013 cycle, PBGC management tested 76 financial reporting controls for both design and effectiveness and found more than 90% of them with no issues.

Entity-Wide Controls: These controls are overarching controls which support the overall effectiveness of PBGC's internal control environment. As of the end of FY 2013, PBGC had identified 46 key entity-wide controls for testing within the following six components of its internal control environment: control environment, risk assessment, control activities, information and communication, monitoring, and anti-fraud. During last year's cycle, PBGC management tested 45 of the controls, finding more than 90% of them with no issues.

NIST Controls: In order to protect the confidentiality, integrity, and availability of PBGC information systems and the information processed, stored, and transmitted by those systems, PBGC implements the controls required by National Institute of Standards and Technology Special Publication No. 800-53 Revision No. 3 (NIST 800-53), Recommended Security Controls for Federal Information Systems and Organizations. During FY 2013, PBGC performed testing of 137 controls related to its General Support Systems, the Present Value Future Benefit (PVFB) valuation system, and Risk Management Early Warning (RMEW) system. Overall, the IT testing yielded results of more than 70% with no issues.

PBGC Prevents Improper Payments

For FY 2013, following a rigorous risk assessment, which involved statistically projectable testing of our contractor payments, PBGC once again issued a report on the results: PBGC's payments to contracting firms that provide PBGC goods and services were not susceptible to significant improper payments. This comports with prior testing of payments to participants and multiemployer financial assistance payment, neither of which were susceptible to significant improper payments. In a recent report issued after the end of the period, the OIG stated: "We concluded that for the FY 2013 review of contract payments, PBGC complied with requirements as specified by OMB."

These results are not due to happenstance. PBGC makes a concerted effort to prevent improper payments through its system of controls. PBGC focuses not only on ensuring that our controls support accurate, timely payments, but also on preventing fraud through regular monitoring. We remind all PBGC employees on a quarterly basis of ways in which they can help prevent fraud. At the end of the reporting period, management met with OIG to discuss both preventive and detective ways of combatting fraud. We intend to meet regularly on this important initiative moving forward.

Audit Coordination and Follow-up Procedures

Audit Coordination and Follow-up Procedures

PBGC has established procedures to ensure proper coordination of the OIG and GAO audits and follow-up on related recommendations to comply with the IG Act and OMB Circular A-50, *Audit Follow-up*. These procedures were developed with the input of the OIG and are set forth in PBGC Directive No. GA-15-04, *Audit Coordination and Follow-up*, dated August 26, 2008.

Regular Status Reporting

Transparency and effective communications are key factors to an effective audit follow-up process. The Contracts and Controls Review Department (CCRD) regularly prepares and circulates status reports to management on ongoing audits initiated by the OIG and the GAO. One of the objectives of this report is to ensure that audit recommendations are being addressed in a timely manner. To ensure that agreed-upon recommendations are implemented timely, the CCRD also regularly prepares and circulates lists of open OIG and GAO audit recommendations, reporting the status of corrective actions and estimated completion dates to management. This process serves to highlight recommendations that are not meeting milestones or that are overdue.

Should changes to estimated completion dates become necessary, these changes are first coordinated with executive members in management, then communicated to the OIG. Further, as part of the annual financial statement audit process, Management provides the OIG and its external auditors, with formal presentations regarding progress made towards the material weaknesses during the past year.

Submission of Evidence for Completed OIG Recommendations

A key component of gaining closure on open OIG recommendations is providing evidence that management has completed corrective actions. When presenting such evidence to OIG for a closure determination by the OIG, PBGC requires the submission of a recommendation completion form, which contains a certification by Management that work has been completed.

Tables Required by the Inspector General Act

Management has prepared two tables required by the Inspector General Act, as follows:

- Table 1 provides our comments on resolved OIG audit reports that are more than 12 months old and contain recommendations for which the final action is pending; and
- Table 2 details OIG reports requiring management decisions.

The OIG did not identify any “funds to be put to better use” during the reporting period. Therefore, no table for this item was prepared.

Table 1

**Management Statement on Resolved Audit Reports Over Twelve Months Old
With Final Action Pending as of March 31, 2014**

Date Issued	Report No.	Title of Report	Status of Management Actions
09/23/1999	1999-08	FY 1998 Financial Statement Audit – Management Letter	Of the 24 recommendations included in the report, 23 have been closed. The remaining recommendation has been submitted to the OIG for closure.
10/10/2003	2003-10	Review of PBGC’s Premium Accounting Process	Of the 16 recommendations included in the report, 12 have been closed. The remaining four recommendations have been submitted to the OIG for closure.
01/15/2004	2004-02	Audit of PBGC’s FY 2003 and 2002 Financial Statements	Of the 14 recommendations included in the report, 13 have been closed. The remaining recommendation has been submitted to the OIG for closure.
11/15/2004	2005-02	Audit of PBGC’s FY 2004 and 2003 Financial Statements	Of the 21 recommendations included in the report, 20 have been closed. The remaining recommendation remains in progress.
03/31/2005	2005-10	FY 2004 Financial Statement Audit – Management Letter	Of the 37 recommendations included in the report, 36 have been closed. The remaining recommendation remains in progress.
11/15/2007	2008-02	Report on Internal Controls – PBGC’s FY 2007 and 2006 Financial Statement Audit	Of the 18 recommendations included in the report, seven have been closed. Of the remaining recommendations, two have been submitted to the OIG for closure and nine remain in progress.
11/13/2008	2009-02	Report on Internal Controls Related to PBGC’s FY 2008 and 2007 Financial Statements Audit	Of the six recommendations included in the report, two have been closed. The remaining four recommendations remain in progress.
01/15/2009	2009-04	FY 2008 Financial Statements Audit Management Letter	Of the 16 recommendations included in the report, 15 were closed. The remaining recommendation remains in progress.

Table 1

**Management Statement on Resolved Audit Reports Over Twelve Months Old
With Final Action Pending as of March 31, 2014**

11/12/2009	2010-02	Report on Internal Controls Related to Pension Benefit Guaranty Corporation FY 2009 and 2008 Financial Statement Audit	Of the 20 recommendations included in the report, five were closed. The remaining 15 recommendations remain in progress.
02/23/2010	2010-04	FY 2009 Financial Statements Audit Management Letter	Of the 35 recommendations included in the report, 28 were closed. The remaining seven recommendations remain in progress.
03/20/2010	2010-07	FY 2009 FISMA Independent Evaluation Report	Of the 12 recommendations included in the report, eight have been closed. The remaining four recommendations remain in progress.
08/18/2010	2010-08	Authorization to Operate PBGC Information Systems	Of the four recommendations included in the report, one has been closed. The remaining three recommendations remain in progress.
09/16/2010	2010-09	PBGC Needs to Improve Participant to Better Protect Participant Personally Identifiable Information (PII)	Of the three recommendations included in the report, one has been closed. The remaining two recommendations are in progress.
11/16/2010	2011-01	Evaluation of PBGC's Strategic Preparations for a Potential Workload Influx	Of the five recommendations included in the report, two have been closed. The remaining three recommendations remain in progress.
02/24/2011	2011-06	FY 2010 Financial Statement Audit – Management Letter	Of the 19 recommendations included in the report, 15 have been closed. Of the remaining recommendations, three were submitted to the OIG for closure and one is in progress.

Table 1

**Management Statement on Resolved Audit Reports Over Twelve Months Old
With Final Action Pending as of March 31, 2014**

11/30/2011	2012-05	PBGC's Processing of Terminated United Airlines Pension Plans was Seriously Flawed	Of the 15 recommendations included in the report, seven were closed. The remaining eight recommendations remain in progress.
03/29/2012	2012-06	FY 2011 Financial Statement Audit – Management Letter	Of the 27 recommendations included in the report, 18 were closed. Of the remaining recommendations, six were submitted to the OIG for closure and three remain in progress.
5/11/2012	2012-09	FY 2011 FISMA Audit	Of the six recommendations included in the report, four were closed. Of the remaining recommendations, one was submitted to the OIG for closure and one remains in progress.
11/5/2012	2013-02	Report on Internal Controls	Of the five recommendations contained in the report, three were closed. The remaining two recommendations remain in progress.

Table 2

**Management Statement on OIG Reports Requiring Management Decisions
For the Period Ending March 31, 2014**

	Number of Reports	Questioned Costs
A. For which no management decision, including any matters relating to questioned costs, had been made by the commencement of the reporting period.	0	\$ -
B. For which a management decision, including any matters relating to questioned costs, was made during the reporting period.	0	\$ -
i. dollar value of disallowed costs		\$ -
ii. dollar value of costs not disallowed		\$ -
C. For which no management decision, including any matters relating to questioned costs, had been made by the end of the reporting period.	1	\$ -
D. For which no management decision, including any matters relating to questioned costs, was made within six months of issuance.	0	\$ -