Review of the RRB's Cost-of-Living Mass Adjustment Process, Report No. 01-14, August 31, 2001

This report represents the results of the Office of Inspector General's (OIG) review of the Railroad Retirement Board's (RRB) cost-of-living mass adjustment (COLA) process.

BACKGROUND

The RRB's mission is to administer retirement, survivor, unemployment, and sickness insurance benefit programs for railroad workers and their families under the Railroad Retirement Act and the Railroad Unemployment Insurance Act. During fiscal year 2000, the RRB paid $8.3 billion in net retirement and survivor benefits to about 724,000 beneficiaries.

Public Law 92-336 provides for the automatic annual COLA to old age, survivor, and disability insurance benefits beginning in 1975. Prior to that time, special acts of Congress authorized increases on an irregular basis. The RRB uses the cost-of-living formula specified by the Social Security Act. In general, the cost-of-living formula is equal to the percentage increase in the Consumer Price Index (CPI) for Urban Wage Earners and Clerical Workers from the third quarter of one year to the third quarter of the next year. The Bureau of Labor Statistics develops the computation of the CPI.

Under the two-tier railroad retirement formula, the tier I annuity portion approximates a social security benefit and increases by the cost-of-living percentage applied to social security benefits. The tier II portion, which is comparable to retirement benefits paid over and above social security benefits to workers in other industries, increases by 32.5% of the social security percentage. Beginning in 1977, the COLA has been applied to tier II benefits every year except 1985.

The COLA is payable beginning with December of the year for which the increase is due. In December 2000, the RRB's cost-of-living operation adjusted the monthly rates of 671,381 beneficiaries. Applying an increase of 3.5% to tier I benefits and 1.1% for tier II benefits resulted in a net increase of $16,092,239 in railroad annuities.

In September 2000, the Bureau of Labor Statistics discovered an error in the December 1999 CPI. This error resulted in understating the December 1999 cost-of-living increase by 0.1%. This error impacts the payments made by the RRB and the Social Security Administration.

The COLA process basically results in one of three outcomes:

- successfully updating the rate and the appropriate records;
- successfully updating the rate, with a review code that indicates that further work must be done on the beneficiary records; or
- unsuccessfully updating the rate, resulting in a reject that requires additional work to manually adjust the rate.

The Retirement Claims Manual (RCM) is the source of guidance for implementing the provisions of the Railroad Retirement Act. The Policy and Systems Division in the Office of Programs is primarily responsible for the COLA operation. The Bureau of the Actuary receives the CPI data and forwards the information to the Office of Programs and the Bureau of Information Services. The Bureau of Information Services runs the mechanical cost-of-living program and updates the appropriate systems, such as the Payment Rate and Entitlement History (PREH) system. This bureau forwards the identification of the review and rejected cases to the Office of Programs for analysis and correction.

The RRB uses the PREH system to store entitlement and rate history information for all RRB beneficiaries. The results of each annual COLA are also stored in the PREH system.

The RRB's 2000-2005 strategic plan states that the agency "will pay benefits accurately." This audit directly addresses this key area of agency performance.

OBJECTIVE AND SCOPE

The objective of this review is to assess the effectiveness and efficiency of the COLA process. The scope of this review included the December 2000 cost-of-living transactions and the corrective action for the December 1999 cost-of-living error. To accomplish this audit objective, the OIG performed the following tasks in connection with the December 2000 COLA:

- reviewed applicable laws, regulations, policies and procedures;
- obtained an understanding of the COLA process;
- prepared a preliminary analysis of controls;
- reviewed systems and internal documents pertaining to the CPI error;
- extracted from the master benefit file all beneficiaries in current pay status as of April 26, 2001 that had received the December 2000 cost-of-living increase;
- randomly selected and reviewed the rates of 600 cases from the master benefit file extractions;
- used Excel spreadsheets to recompute the tier I and tier II rates for the December 2000 COLA using data in the PREH system;
- tested controls and reviewed procedures; and

- discussed procedures, controls, and error cases with the Office of Programs.

Only exception cases were reviewed with the claim folder. All other rates were reviewed without the folder. As such, OIG relied on the accuracy of specific rate components in the PREH system for the tier I and tier II benefits.

The OIG conducted the audit in accordance with generally accepted government auditing standards appropriate to this review. Auditors performed the fieldwork at RRB headquarters office in Chicago, Illinois from March 2001 through June 2001.

RESULTS OF REVIEW

The OIG found that the Office of Programs can make improvements to enhance the effectiveness and efficiency of the COLA process. The OIG determined that:

- the mechanical cost-of-living program does not always compute the rates for survivor family groups in an accurate manner;
- the PREH system does not always contain accurate information on the cost-of-living reject codes;
- the date of a cost-of-living reject or review correction is not always entered into the PREH system; and
- the tier II cumulative cost-of-living factors as published in the RCM are not always correct.

Detailed findings and recommendations are discussed below.

COLA Computations

The mechanical cost-of-living program does not always accurately compute the rates for family groups receiving survivor benefits. The Social Security Act limits the amount of monthly benefits that may be paid for any month on any employee's wage record. This limited amount is called the family maximum.

The RCM states that when multiple survivor beneficiaries are entitled to benefits, the maximum tier I benefit rate is applicable. Each family member is entitled to a share, or a pre-determined percentage, of the tier I maximum benefit rate. The percentage changes as the composition of the family group changes.

The portion of the cost-of-living program that updates or computes each family member's share of the maximum benefit was written many years ago. When it was written, the system was not programmed to identify how many family members were entitled to a share of the maximum benefit. To simplify the computations, the program updates each family member's share by the tier I cost-of-living increase. The use of this method will not always produce the sum of shares being equal to the maximum benefit rate. Instead, the cost-of-living increase should be applied to the tier I maximum benefit rate. Each family member's percentage share should then be applied to that updated rate.

The OIG estimates that over 3,000 of 5,078 family group cases have been paid inaccurate tier I amounts. The beneficiaries are underpaid $1 per month per family group member. The total financial impact for the cases will vary, as the inaccurate rates could impact more than one family member and the family members could be impacted for multiple cost-of-living periods.

The OIG's review of a judgmental sample of 149 family member beneficiaries shows that 50% were underpaid by $1 each month for an average of three cost-of-living periods. Some beneficiaries were underpaid for six consecutive cost-of-living periods, including the December 2000 COLA. In addition, the judgmental sample showed that the COLAs for several family groups with decreasing members have been paid inaccurately for multiple cost-of-living periods. The results of the sample shows that these errors will continue to occur as long as the cost-of-living program calculates family group shares in this manner.

The tolerance rules in the RCM state that no correction is applicable if the rate change in the monthly annuity rate is $1 or less. As a result, the Office of Programs will not correct the estimated 3,000 cases.

Recommendation

The OIG recommends that the Office of Programs make the necessary modifications to the mechanical cost-of-living program to ensure that the tier I share is computed correctly by applying each family member's share to the maximum that has been updated for the cost-of-living increase (Recommendation #1).

Management's response

The Office of Programs has agreed to review the processing of the COLA program to determine what changes are required to address the OIG-identified weakness.

OIG response

The Office of Programs' corrective action is the first step toward addressing the recommendation. After reviewing the processing of the COLA program, the Office of Programs will also need to implement a plan to modify the program to address the weakness that the OIG identified.

PREH Cost-of-Living Reject Code

Cost-of-living reject codes are not always entered into the PREH system for a particular payment reject code. The mechanical cost-of-living program creates an output file that is used to update the PREH system with the reject codes.

The COLA screen in the PREH system provides information regarding whether the cost-of-living adjustment was processed mechanically or if the system rejected it. This screen contains the codes used to explain the reason for the reject and the codes used to explain the reason for a manual review. It also has a field that records the date that the COLA was processed. Claims examiners have on-line access that allows them to manually update fields on this screen. They make entries to indicate that the necessary action was taken for a reject or a review code. They are also responsible for entering the current date of their action on the screen.

The RCM cites the COLA screen in the PREH system as a resource for processing cases without the claims folder. The information on this screen should be accurate and up-to-date to ensure that the RRB can process these cases effectively and efficiently.

An error in the cost-of-living program was the cause of these omissions from the PREH system. These omissions give an incomplete picture of the cost-of-living results for some cases. Without the reject code information, the Office of Programs cannot identify all cases with previous review and/or reject codes, and cannot determine if all COLA reject cases have been corrected.

Recommendation

The OIG recommends that the Office of Programs make the necessary corrections to ensure that the COLA reject codes are entered into the PREH system (Recommendation #2).

Management's response

The Office of Programs concurs and will make the necessary corrections.

COLA Correction Dates

The mass adjustment update field in the PREH system does not always contain accurate information. From a random selection of 291 December 2000 reject and review cases, the OIG discovered 61 errors.

The procedure for the PREH on-line correction facility in the RCM calls for the claim examiner to enter the date of any manual correction. The PREH correction system enables examiners to correct data in the PREH system when a record will not be updated from an award action or when an award action is not necessary.

The claims examiners do not always change the date when they make manual corrections through the on-line correction facility. Because the examiners do not change the date, the Office of Programs is unable to track the timeliness of the corrections. The OIG estimates that as many as 600 of the December 2000 COLA reject and review cases might also have missing dates. However, management in the Office of Programs stated that it would not be cost-effective to correct the 600 cases.

Recommendation

The OIG recommends that the Office of Programs issue a reminder notice to ensure that the correction dates are entered into the PREH on-line correction facility (Recommendation #3).

Management's response

The Office of Programs has proposed an alternative corrective action. The Office of Programs has requested BIS to change the PREH on-line correction facility to automatically enter the date of correction whenever examiners make a correction. BIS has also agreed to do a mass correction of the dates that examiners failed to update in the past.

OIG Response

The Office of Programs' alternative corrective action is acceptable.

Cumulative COLA Factors

Tier II cumulative cost-of-living factors published in the RCM are incorrect. The OIG learned that errors of this type have also occurred in the past. Once the Bureau of the Actuary notifies Policy and Systems of the new tier II cost-of-living increase, Policy and Systems adds the new increase to the previous increases. These increases are referred to as cumulative tier II cost-of-living factors.

The RCM is the source of historical data, procedures and guidance pertaining to the COLA.

Internal controls were not sufficient to ensure that the cumulative tier II cost-of-living factors were correctly computed for certain time frames. The tier II factors are not reviewed before they are included in the RCM. The Office of Programs believes that no controls are necessary for these computations because neither the mechanical cost-of-living program nor automated systems use these cumulative tier II factors.

Some sections within the Office of Programs that manually recalculate benefits use the cumulative tier II cost-of-living factors listed in the RCM to check the accuracy of the RRB benefit rates. For example, some quality assurance staff use the cumulative factors to manually recalculate benefits. Therefore, additional time could be expended while trying to resolve the confusion that would result from the use of these incorrect factors.

After the incorrect factors were discovered as a result of OIG tests, the Office of Programs made the necessary corrections.

Recommendation

The OIG recommends that the Office of Programs improve the internal controls to ensure that the cumulative tier II factors are computed correctly (Recommendation #4).

Management's response

The Office of Programs has agreed to revise the RCM to simplify the procedure for the cumulative tier II factors and to ensure that the information is correct.

Automation of Legal Partition Cases

Legal partition cases have not been included in the mechanical cost-of-living program. Legal partition cases are those in which a portion of the employee's annuity is paid to a third party under a court order, usually for child support or alimony payments. There are currently 1,500 legal partition cases.

The legal partition amounts are paid to third parties based on a court order. As such, many of them are for a fixed percentage of the RRB annuity rate.

Although the Office of Programs has planned to automate this workload, that automation has not yet taken place. Other high priority work, such as the Consumer Price Index corrections, took time and attention away from automating this workload. Through December 2000, the annual COLA has been run based on the contents of the Master Benefit File, which does not store any information on legal partition cases. For the December 2001 COLA operation, the Office of Programs plans to use an expanded version of the Master Benefit File from the PREH system, which includes this data.

This workload increases by approximately 200 cases each year, and it must be manually adjudicated by claims examiners. Each case requires two manual awards to pay the COLA to the annuitant and to the third party. The manual processing of these cases requires more than 1,000 man-hours.

The Office of Programs has submitted and received approval for a service request for automating this workload. The first phase of the project has already been completed. As a result, the OIG has no recommendations at this time.

Corrective Action for December 1999 CPI Error

RRB beneficiaries were underpaid for their tier I benefits for the COLA beginning in December 1999. The percentage increase should have been 2.5% instead of the 2.4% actually paid. The tier II benefits are not impacted by this error.

The RRB and Social Security Administration have coordinated their efforts to have the retroactive payments and current rate adjustments made in July 2001. The RRB tier I rates will increase by $1 per month for most of the beneficiaries impacted for each month beginning in December 1999. The retroactive accrual payment totaled $8,937,517 in railroad benefits and $1,660,905 in Social Security benefits paid by the RRB. On July 25, 2001, the accrual payments were released to 517,635 railroad and social security beneficiaries.

These corrections will also impact the rates currently in force. Most beneficiaries will receive a $1 per month increase in their current RRB tier I benefits beginning with their August 2001 payment. The total net increase in monthly benefit payments is $484,443.

The correction did not change the monthly rate of 196,040 beneficiaries. Also, 15,951 beneficiaries were not eligible for the correction because they were not entitled to the December 1999 COLA.

In addition, 828 beneficiaries are due retroactive payments but their annuities could not be adjusted mechanically. The Office of Programs plans to manually adjust and release payments to these annuitants within one year, which are the normal working guidelines for cost-of-living rejects.

The OIG reviewed system requests for this job and monitored the progress through internal administrative reports and discussions with the staff responsible for making the corrections. Since the payments had not been issued, the OIG did not perform any tests. Therefore, the OIG has no recommendations at this time.