January 2003

Major Management Challenges and Program Risks

Office of Personnel Management

GAO

Accountability ★ Integrity ★ Reliability

GAO-03-115

A Glance at the Agency Covered in This Report

The Office of Personnel Management provides human capital leadership, guidance, and expertise to the President, and to federal agencies and their employees. It also ensures compliance with personnel laws and regulations and provides retirement, health benefits, and other insurance services to employees, annuitants, and beneficiaries.

OPM is in the midst of a major transformation effort and has revised its strategic plan to both drive and reflect that effort. The strategic plan outlines the following three goals for the agency:

- ensuring that federal agencies adopt human capital management systems that improve their ability to build successful, high-performing organizations;

- ensuring that federal agencies use effective merit-based human capital strategies to create a rewarding work environment that accomplishes the mission; and

- meeting the needs of federal agencies, employees, and annuitants through the delivery of efficient and effective products and services.

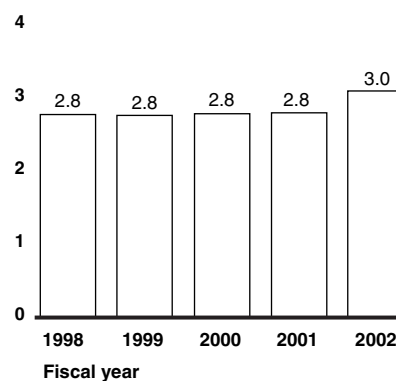### The Office of Personnel Management's Budgetary and Staff Resources

Budgetary Resources [a, b]
Dollars in billions

Fiscal year	Value
1998	112
1999	116
2000	120
2001	126
2002	134
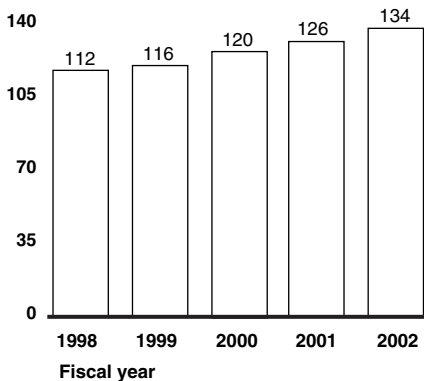
Staff Resources [b]
FTEs in thousands

Fiscal year	Value
1998	2.8
1999	2.8
2000	2.8
2001	2.8
2002	3.0

Source: Budget of the United States Government.

[a] Budgetary resources include new budget authority (BA) and unobligated balances of previous BA.

[b] Budget and staff resources are actuals for FY 1998-2001. FY 2002 are estimates from the FY 2003 budget, which are the latest publicly available figures on a consistent basis as of January 2003. Actuals for FY 2002 will be contained in the President's FY 2004 budget to be released in February 2003.

This Series

This report is part of a special GAO series, first issued in 1999 and updated in 2001, entitled the *Performance and Accountability Series: Major Management Challenges and Program Risks.* The 2003 Performance and Accountability Series contains separate reports covering each cabinet department, most major independent agencies, and the U.S. Postal Service. The series also includes a governmentwide perspective on transforming the way the government does business in order to meet 21st century challenges and address long-term fiscal needs. The companion 2003 *High-Risk Series: An Update* identifies areas at high risk due to either their greater vulnerabilities to waste, fraud, abuse, and mismanagement or major challenges associated with their economy, efficiency, or effectiveness. A list of all of the reports in this series is included at the end of this report.

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Highlights

Highlights of GAO-03-115, a report to Congress included as part of GAO's Performance and Accountability Series

PERFORMANCE AND ACCOUNTABILITY SERIES

Office of Personnel Management

Why GAO Did This Report

This is GAO's first performance and accountability series report on the Office of Personnel Management (OPM), the federal government's human capital agency. OPM faces challenges in four key areas: leadership, oversight, internal management, and administration of the federal retirement and health insurance programs. The data presented in this report are intended to help sustain congressional attention and an agency focus in addressing these challenges and ultimately overcoming them. This report is part of a special series of reports on governmentwide and agency-specific issues.

What Remains to Be Done

Consistent with OPM's ongoing internal transformation efforts, GAO believes that OPM should

- accelerate efforts to seek and implement solutions to problems with the federal pay and hiring systems,

- ensure that agencies establish and maintain merit-based human capital management systems and promote agency self-monitoring programs, and

- ensure that it effectively transitions to its new organizational structure while continuing to address its human capital, financial management, and information security challenges.

www.gao.gov/cgi-bin/getrpt?GAO-03-115.

To view the full report, click on the link above. For more information, contact Chris Mihm at mihmj@gao.gov or (202) 512-6806.

What GAO Found

OPM has implemented important initiatives and has others under way to improve its mission and management performance. Building on these efforts, OPM has additional opportunities to overcome the following management challenges.

- **Leading strategic human capital management governmentwide.** Many agencies continue to experience human capital shortfalls. They want and need greater OPM leadership and assistance to help them strategically manage their human capital and address challenges in recruiting, retaining, and rewarding talented staff—caused, in part, by long-standing problems with the federal pay, classification, and hiring systems.

- **Overseeing agency human capital management systems.** Merit system surveys and studies continue to show a need for strong oversight of agency human capital systems. Surveys show employees continue to believe agencies are not adhering to several of the merit principles.

- **Transforming OPM and managing its internal operations.** As in other areas, OPM has major efforts under way to address this challenge. It is realigning its organizational structure, has prepared a draft succession plan, is implementing a new financial management system, and is addressing several information security weaknesses. But more remains to be done as OPM transitions to its new structure. For example, OPM should implement workforce and succession planning strategies to address the expected staff losses from retirements and to close skill and knowledge gaps, fully implement an agencywide security program and conduct security risk assessments of its information systems, and continue to take steps to address historical weaknesses in activities of its discretionary appropriation funds.

- **Administering the retirement and health insurance programs.** OPM has made major strides in managing these programs, which have received high ratings from customers over the past few years—for example, over 90 percent of federal annuitants are satisfied with OPM's retirement services. But customer satisfaction could fall if OPM is not able to handle the impending retirement wave or implement measures to limit health care premiums.

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Accountability ★ Integrity ★ Reliability

United States General Accounting Office
Washington, D.C. 20548

Comptroller General
of the United States

January 2003

The President of the Senate
The Speaker of the House of Representatives

This report addresses, for the first time, the major performance and accountability challenges facing the Office of Personnel Management (OPM) as it seeks to ensure that the federal government's human capital management systems are merit-based and support agencies in recruiting, hiring, and retaining the high-quality, diverse workforce necessary to meet the current and emerging needs of the American people. It includes a summary of actions that OPM has taken and that are under way to address these challenges. It also outlines further actions that GAO believes are necessary.

This analysis should help the new Congress and the administration carry out their responsibilities and improve government for the benefit of all Americans. For additional information about this report, please contact J. Christopher Mihm, Director, Strategic Issues, at (202) 512-6806 or at mihmj@gao.gov.

David M. Walker
Comptroller General
of the United States

Major Performance and Accountability Challenges

The Office of Personnel Management (OPM), the President's agent and advisor for human capital matters, is charged with overseeing the management of the federal government's most important asset—its people. In January 2001, we added strategic human capital management to our list of federal programs and operations that we have identified as high risk.[1] OPM's charge entails leading agencies and holding them accountable for shaping their human capital management systems in a manner that ensures that (1) the federal government acquires, develops, manages, and retains employees with the knowledge, skills, and abilities needed to deliver services the American people want and deserve and (2) governmentwide values, such as the merit system principles, veterans' preference, and workforce diversity, are consistently upheld. OPM is also charged with providing retirement, health benefits, and other insurance services to employees, annuitants, and beneficiaries.

OPM's leadership in helping agencies shape their human capital management systems has become more crucial as a result of the tragic events of September 11, 2001. These events led to a change in our world and the priorities of our policymakers and produced new challenges to create and staff new governmental structures and restructure some existing ones to fight terrorism and secure our homeland. At the same time, agencies across the federal government need to transform what they do, how they do it, and with whom they partner. These transformations will have enormous implications for the federal government's "people" policies and procedures as well as cultures of government organizations. OPM plays a key role in helping individual agencies and the government as a whole overcome the broad range of human capital challenges, which are at the root of transformation. The four pervasive governmentwide human capital challenges, identified in our 2001 *High-Risk Update*, are (1) strategic human capital planning and organizational alignment, (2) leadership continuity and succession planning, (3) acquiring and developing staffs whose size, skills, and deployment meet agency needs, and (4) creating results-oriented organizational cultures. OPM carries out its leadership role in a decentralized environment where both it and the agencies have shared responsibilities for addressing the human capital and related challenges facing the government.

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[1]U.S. General Accounting Office, *High-Risk Series: An Update*, GAO-01-263 (Washington, D.C.: January 2001).

OPM is in the process of transformation—*from less* of a rulemaker, enforcer, and independent agent *to more* of a consultant, toolmaker, and strategic partner in leading and supporting executive agencies' human capital management systems. As OPM's transformation evolves and it seeks to constructively partner and consult with other executive agencies in shaping their human capital management systems, it must also strive to maintain the degree of institutional independence needed to oversee agencies' human capital efforts objectively.

OPM's transformation has been occurring against the backdrop of at least 15 reorganizations since its inception in 1979 and a nearly 50 percent drop in staff over the last decade, largely due to governmentwide downsizing in the mid-1990s. OPM's total workforce dropped from nearly 6,800 in 1990 to about 3,700 in 2002. OPM's operating budget was also affected during this time frame but not to the same degree. From fiscal years 1990 through 2002, OPM's operating budget fluctuated—ranging from a high of $227 million in fiscal year 2002 to a low of $186 million in 1998.[2] Overall, after adjusting for inflation, OPM's funding declined 10 percent over the 1990 through 2002 period.

The changes that have been occurring in OPM's culture and organization since its creation, as well as the different operating philosophies of each of its directors, have influenced how the agency has carried out its leadership role and mission. OPM's overarching challenge today is to lead agencies in shaping their human capital management systems while also undergoing its own internal transformation. As it addresses this overall challenge, OPM faces several performance and accountability challenges that affect its ability to effectively execute its mission and become a high-performing organization focused more on results and less on process. These include the following:

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[2]These amounts do not reflect OPM's total budget. OPM's total budget, which is shown in the inside cover of this report, primarily consists of the trust funds for civil service retirement and federal health benefits. For the last 5 years, OPM's total budget increased each year from $112 billion in fiscal year 1998 to an estimated $134 billion in fiscal year 2002.

Performance and Accountability Challenges

- Define and exert a stronger leadership role in helping to strategically manage the federal government's human capital

- Oversee human capital management, including ensure agency adherence to the merit system principles

- Successfully transform its organization and workforce to better meet its clients' needs as well as continue to improve management of three key internal areas- human capital, information security, and financial management

- Administer the governmentwide retirement and health insurance programs efficiently and economically to ensure proper delivery of benefits and services and continuation of high customer satisfaction ratings

OPM has taken a number of important steps and has several initiatives under way or planned to address each of its challenges. For example, OPM has exerted greater human capital leadership by issuing agencies its *Human Capital Scorecard*[3] to assist them in improving strategic management of their human capital and administering an annual governmentwide survey on human capital to help assess agencies' progress in achieving performance goals for each of the five dimensions of human capital management contained in its *Human Capital Scorecard*. For example, OPM will be able identify the extent to which workforces in individual agencies as well as the federal government as a whole lack the necessary job-relevant knowledge and skills to accomplish organizational goals. In addition to using the results of the survey to assess and report on federal agency progress overall in achieving the human capital management performance goals contained in its scorecard, OPM intends to compare and benchmark the human capital survey results with private sector organizations. OPM has also exerted greater human capital leadership by developing a set of legislative proposals for providing agency managers the additional flexibilities and tools they need to manage their human capital effectively.[4] OPM is addressing its oversight challenge, in part, by encouraging agencies to develop and maintain internal accountability systems in line with its *HRM Accountability System Standards*.

Internally, OPM has launched an effort to transform its organizational structure and workforce to be more customer-focused and results-oriented. OPM outlined its new organizational structure in September 2002 and is currently implementing it. OPM has also taken several steps to manage its human capital more strategically (such as aligning its human capital goals with program-specific goals), correct financial management weaknesses (such as implementing a new financial management system), and secure its information resources (such as issuing an agencywide security policy). Given its governmentwide leadership responsibilities, it is particularly important that OPM seeks to "lead by example" in its internal management, particularly with its own human capital approaches and initiatives.

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[3]OPM's *Human Capital Scorecard*, issued in December 2001, contains dimensions for strategic alignment, strategic competencies (talent), leadership, performance culture (strategic awareness), and learning (knowledge management).

[4]Some of the proposals were included in the governmentwide human capital provisions in the Homeland Security Act of 2002.

In addition to launching the new federal long-term care insurance program, OPM has made significant strides in administering the federal employees retirement and health benefits programs, which customers have rated highly. For example, OPM has taken steps to modernize its retirement systems and limit the extent of the health care premium increases. Although customers have rated the retirement and health benefits programs highly, these high satisfaction rates could fall if OPM is not prepared to handle the expected retirement wave and implement cost-containment measures that limit health care premium increases.

Building on these efforts, OPM should also exert greater leadership in seeking and implementing solutions to long-standing problems with the federal pay and hiring systems and in working with other interested parties to prepare the way for more comprehensive civil service reform; ensure that agencies establish and maintain merit-based human capital management systems and promote agency self-monitoring programs; and ensure that it effectively transitions to its new organizational structure while continuing to address its internal human capital, financial management, and information security challenges.

Leadership of Human Capital

Strategic human capital management is a pervasive challenge facing agencies across the federal government, and overcoming this challenge will require vigorous and sustained leadership from multiple parties—OPM as well as other key human capital players, such as the President; the Office of Management and Budget (OMB); Congress; and department and agency leaders. Since designating strategic human capital management as a high-risk area in January 2001,[5] our work and the work of others continues to show that agencies need and want greater leadership from OPM in helping them to address their human capital challenges. OPM recognizes the importance of exerting a stronger and more visible leadership role. It, along with several other key human capital players, including GAO, has taken or proposed actions within the last 2 years that are aimed at improving human capital management across government and a real momentum for reform is now evident. Nevertheless, while addressing the challenge of strategic human capital management is a shared responsibility among multiple parties, continuing and augmented leadership from OPM,

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[5]GAO-01-263.

as the President's primary advisor on human capital issues, is critically needed in addressing this challenge.

Our work and that of others has shown that many agencies are continuing to experience human capital shortfalls that erode their ability, as well as threaten the ability of others, to perform their missions economically, efficiently, and effectively. The following examples illustrate the seriousness of the human capital challenges facing agencies.

- The federal government is facing several human capital challenges in its civilian acquisition workforce. This workforce declined by 22 percent over the last decade. As the number of acquisition workers declines, the demand increases for an acquisition workforce with more sophisticated technical, financial, and management skills to handle the procurement of $200 billion in goods and services annually.[6]

- The Federal Aviation Administration (FAA) will likely need to hire thousands of air traffic controllers in the next decade to meet increasing traffic demands and to address the anticipated attrition of experienced controllers, predominately because of retirement. Yet, we reported in June 2002 that FAA had not developed a comprehensive human capital workforce strategy to address its impending controller needs.[7]

- The Securities and Exchange Commission's (SEC) workload has increased in volume and complexity over the past decade due to the tremendous growth in the U.S. securities markets. SEC's growing workload has caused staffing imbalances and put the agency under increasing pressure. In addition, staffing shortages have delayed critical regulatory activities, such as reviewing rule findings and issuing guidance, and affected its oversight and supervisory functions.[8]

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[6]U.S. General Accounting Office, *Acquisition Workforce: Status of Agency Efforts to Address Future Needs*, GAO-03-55 (Washington, D.C.: Dec. 18, 2002).

[7]U.S. General Accounting Office, *Air Traffic Control: FAA Needs to Better Prepare for Impending Wave of Controller Attrition*, GAO-02-591 (Washington, D.C.: June 14, 2002).

[8]U.S. General Accounting Office, *SEC Operations: Increased Workload Creates Challenges*, GAO-02-302 (Washington, D.C.: Mar. 5, 2002).

- The Department of Homeland Security is bringing together 170,000 federal employees from 22 agencies with their own cultures and often differing performance management, personnel, and payroll systems. Merging these disparate entities into a coherent, unified, and high-performing department represents a great challenge for the new leadership as well as for OPM in advising and supporting the leadership.[9]

Although federal departments and agencies have primary responsibility for strategically managing their people and addressing their human capital challenges, OPM has an important role and responsibility in leading agency and governmentwide human capital efforts. OPM defines its human capital leadership role as supporting agencies in achieving their strategic goals and managing their human capital more effectively and strategically by

- creating a personnel system (policies, procedures, and tools) that gives agencies the flexibility they need to recruit, retain, train, and manage employees and to align their workforces in a manner appropriate to their unique needs;

- providing guidance and assistance through its Web site as well as through other means to alert agency managers to their human capital responsibilities and authorities;

- making the hiring process more effective and efficient, including improving the attractiveness of the federal government as an employer to people of diverse backgrounds;

- providing expert advice on performance management, classification, and compensation, including proposing options for market-based, performance-oriented compensation reform to enable agencies to recruit and retain high-quality employees;

- promoting demonstration projects that help agencies develop more effective human capital programs and practices as well as providing

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[9]U.S. General Accounting Office, *Homeland Security: Critical Design and Implementation Issues*, GAO-02-957T (Washington, D.C.: July 17, 2002), and *Highlights of a GAO Forum: Mergers and Transformation: Lessons Learned for a Department of Homeland Security and Other Federal Agencies*, GAO-03-293SP (Washington, D.C: Nov. 14, 2002).

them a wide range of human capital products and services, such as examining and testing job applicants;

- encouraging agencies to use workforce and succession planning to strategically manage the impact of demographic and other workforce changes;

- disseminating information about the federal labor-management relations program to agencies, labor organizations, and the general public and consulting with labor organizations on the national level about governmentwide human capital issues; and

- ensuring that essential governmentwide values—such as merit system principles and accountability, veterans' preference, workforce diversity, and family-friendly policies—are sustained.

While important efforts have recently been taken and more are planned or under way, there are additional opportunities for OPM leadership. For example, as a part of our work on human capital flexibilities for a forthcoming report, half or more of the human resource (HR) directors we surveyed in 2001 and 2002 at 24 agencies and departments told us that OPM had not sufficiently assisted them in identifying new flexibilities. Our ongoing review of the federal hiring process is identifying additional areas where OPM can target its efforts. We reported in July 2001 and in an earlier report that OPM should take a more active role in agency workforce planning efforts in light of the expected retirement wave. [10] Our July 2001 report also pointed out that OPM should focus its performance goals more squarely on the degree to which the federal workforce has the right skill mix. Twenty-six percent of the HR directors responding to OPM's fiscal year 2001 customer satisfaction survey said employees in their agencies lacked the skills needed to meet their agencies' missions.

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[10]U.S. General Accounting Office, *Office of Personnel Management: Status of Achieving Key Outcomes and Addressing Major Management Challenges*, GAO-01-884 (Washington, D.C.: July 9, 2001), and *Senior Executive Service: Retirement Trends Underscore the Importance of Succession Planning*, GAO/GGD-00-113BR (Washington, D.C.: May 12, 2000).

The Merit Systems Protection Board (MSPB) has also called for greater leadership on the part of OPM.   MSPB, which is required by statute to periodically review OPM's activities, reported in December 2001[11] that OPM has made commendable progress in a number of areas, such as decentralizing the civil service and improving HR oversight. However, its leadership needs to be more vigorous in responding to a number of critical program areas, such as applicant examining, staffing, and employee compensation policies and practices. MSPB said that OPM is in an ideal position to demonstrate leadership by championing the development and use of the best assessment tools for evaluating candidates. Regarding staffing, MSPB said that many managers and HR specialists continue to be convinced that they are not getting high-quality candidates because policies, laws, and regulations impose restrictions on how agencies are to select, appoint, and promote employees. As the government's human capital leader and expert, MSPB said that OPM should forcefully use its influence to help bring about changes in civil service laws, policies, and practices that either conflict with or detract from a merit-based employment system.

MSPB's 2001 report also noted opportunities for greater OPM leadership in improving the federal government's classification and compensation systems and in addressing key obstacles within the hiring process. For example, MSPB reported that critics of the classification system, which remains the primary determinant of employees' pay after over 50 years, view it as antiquated and irrelevant to the work and workers of today. MSPB also reported that several HR directors said that OPM has relied on a piecemeal approach to solving problems with the compensation system, while others expressed frustration with OPM's lack of progress in creating a system that helps them recruit and retain high-quality workforces.   In particular, MSPB has called on OPM to address key problems with the hiring process, including revamping the system for compensating workers, reducing the number of hiring authorities, and developing new candidate assessment tools.

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[11]U.S. Merit Systems Protection Board, *The U.S. Office of Personnel Management in Retrospective: Achievements and Challenges After Two Decades* (Washington, D.C.: December 2001).

OPM also has a key role to play in improving the governmentwide systems in place for managing employee performance at all levels and holding employees accountable for results, adequately compensating employees at all levels, and maintaining effective employee and labor relations. As we discuss in our 2003 *High-Risk Series: Strategic Human Capital Management,*[12] modernizing agency performance management systems and linking them to agency strategic plans and desired outcomes should be a top priority. We also noted that (1) long-standing issues and concerns over executive compensation and pay compression need to be carefully examined in the context of how to make any pay increases variable and performance-based rather than across-the-board and fixed and (2) effective employee-management relations can aid in achieving organizational outcomes by fostering an environment in which managers and employees work collaboratively. OPM can also assist agencies as they seek to form high-performing organizations. Agencies need to form high-performing organizations to better determine competitive sourcing strategies.

OPM is taking several steps to exercise broad overall leadership over federal human capital management. OPM has the key role leading the administration's efforts to address strategic human capital management, a critical part of the *President's Management Agenda* for improving federal management and performance, and has dedicated staff to work directly with agency leaders to ensure that they are effectively transforming their strategic human capital management. In December 2001, OPM issued its *Human Capital Scorecard*, which is designed to help agencies achieve the human capital standards for success that are part of the *Executive Branch Management Scorecard*. In November 2002, OPM posted on its Web site the administration's revised *Human Capital Standards for Success* that were based on a collaborative effort by OPM, OMB, and us. The revised standards replaced OPM's *Human Capital Scorecard* and more fully reflect the key themes in our strategic human capital model.[13] OPM says it is using these standards to assess agencies' human capital practices.

To increase agencies' awareness and use of effective human capital flexibilities, OPM published two reports in 2001. One report,

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[12]U.S. General Accounting Office, *High-Risk Series: Strategic Human Capital Management*, GAO-03-120 (Washington, D.C.: January 2003).

[13]U.S. General Accounting Office, *A Model of Strategic Human Capital Management*, GAO-02-373SP (Washington, D.C.: Mar. 15, 2002). The model, which was issued as an exposure draft, is intended to be a tool to help federal agency leaders better manage their people.

Demonstration Projects and Alternative Personnel Systems: HR Flexibilities and Lessons Learned, describes best practices and lessons learned from testing a variety of flexibilities, such as pay banding, categorical ranking, and market-based pay, under demonstration projects and alternative personnel systems. The other report, *Human Resources Flexibilities and Authorities in the Federal Government,* is a handbook that is designed to provide agencies information on how they can use the HR flexibilities to address their human capital challenges. Also in 2001, OPM began sending "strike force" teams of HR experts to agencies that requested specific assistance in using existing HR flexibilities.

OPM has also begun to exercise more leadership to address the long-standing problems with the federal government's cumbersome hiring process and inadequate pay and classification systems. OPM began an initiative in the spring of 2002 to improve the hiring process. The hiring initiative will, in part, entail revising the vacancy announcements to make them more reader friendly; providing federal job seekers a single application point through Recruitment One-Stop, an electronic government (e-Gov) initiative;[14] and taking steps to build the image of public service. OPM is developing a resource guide for managers and HR professionals that will highlight efficient and effective hiring practices that can be implemented under existing authorities available to agencies. The resource guide is scheduled to be released in 2003, according to OPM. In addition, OPM's 2003 performance plan indicates increased attention to improving applicant assessment tools, a key obstacle to effective hiring. One of the strategic objectives in OPM's 2003 plan states that by 2005, governmentwide hiring selections are to be based on assessment tools that are more comprehensive in assessing the full range of competencies needed to perform the jobs of the future.

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[14]Recruitment One-Stop is one of five crosscutting e-Gov projects initiated under the *President's Management Agenda* that OPM is charged with leading. The other four projects are e-Clearance, e-Payroll, e-Training, and the Enterprise Human Resource Integration initiative. These projects cover a spectrum of human capital activities.

Regarding pay and classification, OPM issued a white paper in April 2002[15] describing the need for reform of the white-collar federal pay system to make it more flexible, market-sensitive, and performance-oriented as well as a better tool for improving strategic human capital management. The paper characterized the federal government's pay and classification (also called job evaluation) systems as rigid and antiquated with work level descriptions dating back over half a century that are not meaningful for today's knowledge-driven organizations. In July 2002, we testified before the National Commission on the Public Service that OPM's white paper provides a good foundation for the results-oriented pay reform discussion that now needs to take place and noted that the greater use of broadbanding is an option that deserves to be discussed. In that testimony, we also noted that Congress may wish to explore the benefits of (1) giving OPM additional flexibility that would enable it to grant governmentwide authority for all agencies (i.e., class exemptions) to use broadbanding for certain critical occupations and/or (2) allowing agencies to apply to OPM (i.e., case exemptions) for broadbanding authority for their specific critical occupations. However, agencies should be required to demonstrate to OPM's satisfaction that they have modern, effective, and validated performance management systems before they are allowed to use broadbanding.[16]

OPM also had a central role in the development of key personnel reforms that were part of the administration's reform legislation. Some of these reforms were included in the recently enacted Homeland Security Act of 2002,[17] which created the new Department of Homeland Security. According to OPM, it has been the principal advisor on HR flexibilities for the new department and is working with the department's leadership to develop specific HR recommendations in the six areas of management flexibility provided in the legislation—performance management, pay systems, position classification, hiring, labor-management relations, and disciplinary actions and appeals. In addition to providing the President with additional authority to create new policies for managing the

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[15]U.S. Office of Personnel Management, *A Fresh Start for Federal Pay: The Case for Modernization* (Washington, D.C.: April 2002).

[16]U.S. General Accounting Office, *Managing for Results: Using Strategic Human Capital Management to Drive Transformational Change*, GAO-02-940T (Washington, D.C.: July 15, 2002).

[17]Pub. L. No. 107-296, Nov. 25, 2002.

workforce within the new department, the legislation includes provisions that authorize agencies across the federal government to use additional personnel flexibilities. For example, agencies will now be permitted (1) to offer early outs and buyouts to their employees without the requirement to reduce their overall number of employees and (2) to use a more flexible approach in the rating and ranking of job candidates during the hiring and staffing process. In addition, under the legislation agencies will be required to incorporate strategic workforce planning into their performance plans and reports and appoint "chief human capital officers" to oversee workforce management.

Although OPM has initiated several actions to help address governmentwide strategic human capital management challenges, there are opportunities for OPM to augment its leadership. As we have noted earlier in this report and MSPB has outlined in several studies, OPM can build on the steps it has taken and exert aggressive leadership in seeking and implementing solutions to key human capital challenges. Continuing efforts are particularly needed to address hiring and compensations issues, which have plagued federal human capital management for years.

Oversight of Agency Human Capital Management Systems

Agencies and OPM share responsibility for ensuring that human capital practices are effective and carried out in accordance with the merit system principles[18] and other national goals. Effective implementation of human capital practices in accordance with the merit system principles and other national goals is important to ensuring a skilled and qualified federal workforce as well as maintaining the integrity of and public confidence in the federal civil service.   In recognition of the importance of this issue, one of the dimensions of effective human capital management in the administration's *Human Capital Standards for Success* is "Agency human capital decisions are guided by a data-driven, results-oriented planning and accountability system." While agencies are primarily responsible for managing their human capital, OPM has governmentwide oversight responsibilities. OPM recognizes that oversight is important to improving governmentwide strategic human capital management, especially in the changing human capital environment of increased flexibility in managing human capital both inside and outside the requirements of title 5 of the U.S.

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[18]The nine merit principles, defined in law at 5 U.S.C. 2301(b), are broad principles that define how federal personnel management should be implemented. The principles cover topics such as recruitment, pay, and employee performance.

Code, which defines much of the federal government's personnel system requirements. In recognition of this growing decentralization of the federal personnel system, OPM has taken actions to strengthen its oversight program. Building on these efforts, OPM needs to do more to ensure that agencies are effectively operating their human capital management systems and adhering to the merit system principles. Promoting agency self-monitoring programs is one area needing continued OPM attention.

Effective and strategic oversight of agencies' systems is even more critical today because an increasing number of agencies are using human capital flexibilities, delegating authorities to line managers, and seeking and obtaining exemptions from the requirements of title 5 of the U.S. Code. This is taking place at a time when OPM's and agencies' human capital staffs for overseeing these activities have dwindled substantially. In response to this development, OPM is carrying out its oversight by encouraging and monitoring agency self-assessment efforts, analyzing agency-specific and governmentwide data, conducting governmentwide annual surveys on the merit system principles and human capital to gather employees' perceptions of the systems' fairness and effectiveness, and conducting on-site reviews of agencies' human capital management systems.

The results of several merit principle surveys conducted by OPM and MSPB continue to raise questions about how effectively the agencies and OPM are carrying out their responsibilities for ensuring that human capital practices are carried out in accordance with the merit system principles. Over the years, these surveys have revealed that a varying and sometimes substantial percentage of employees have expressed a belief that their agencies are not adhering to these principles. OPM's Merit System Principles Questionnaire results for 1999 through 2001 showed less than half of the responding employees believed that their agencies protect them against reprisal and provide equal pay for equal work as well as reward excellence. OPM's survey results are broadly consistent with a 1998 MSPB survey where 40 percent of those surveyed said they believed they had inadequate protection against the possibility of a prohibited personnel action being taken against them. MSPB said of these results, "the fact that such a high percentage felt [this way] is a cause for concern and continued vigilance." To its credit, OPM acknowledged in its 2001 performance report that employees' low perceptions of their agencies' adherence to the aforementioned merit principles were unacceptable and that it planned to address the perception issue in future plans and strategies. Its 2003 performance plan says it expects improvement to occur over a period of

years, but it does not address what specific steps OPM and others need to take to improve the percentage of positive responses.

MSPB survey data collected from 1986 through 2001 showed that employees are not convinced that favoritism and unfair advantage have been removed from the government's hiring and promotion processes. For example, 28 percent of employees surveyed in 1986 said they believed they had been denied a job or job reward because of the operation of a "buddy system" without regard to merit. In a study published in December 2001, MSPB reported that 69 percent of surveyed employees believed that "connections to other important people in government" was the single factor most likely to play a role in promotions or selections for vacant positions in their organizations.[19]

To address these ongoing issues in its oversight program, OPM has taken a number of actions. For example, in January 2002, OPM issued *HRM Accountability System Standards* in response to Executive Order 13197. The standards describe the essential elements of internal human resources management (HRM) accountability systems, set criteria for agencies in establishing and maintaining these systems, and provide OPM a framework for reviewing and assessing agencies' systems. OPM reported in its 2001 performance report that the executive order gave the agency clear authority to require agencies to establish and maintain HRM accountability systems. OPM officials told us it is encouraging agencies to develop an internal accountability system in line with these standards and has issued a "toolkit" to assist them in doing so.

Recognizing that it is increasingly important for agencies to have a strong internal capability for ensuring accountability and compliance with the merit principles in the currently decentralized HRM environment, OPM established a strategic objective in its fiscal year 2003 performance plan that all agencies implement accountability systems by fiscal year 2005 that "effectively hold responsible officials accountable for their human resources operations and results." To achieve this objective, OPM set a goal to "develop and improve agency accountability for conducting HRM in accordance with the merit system principles and in alignment with mission." OPM expects to meet this goal by assessing agency accountability systems; improving ways to evaluate the effectiveness of

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[19]U.S. Merit Systems Protection Board, *The Federal Merit Promotion Program: Process vs. Outcome* (Washington, D.C.: December 2001).

HRM accountability systems; and promoting and assisting agencies in developing and improving their accountability systems through sharing of best practices, developing and distributing educational materials, and providing guidance and individual consultation. Meeting this important goal will entail an enormous effort on the part of OPM and the agencies.

OPM also issued a *Human Capital Assessment and Accountability Framework* (Framework) in October 2002 that is based on the revised standards for success contained in the administration's *Executive Branch Management Scorecard*. The Framework provides agencies consolidated guidance on critical success factors and performance indicators that they can refer to as they transform their strategic human capital management programs. It is also intended to support agencies' internal assessment and accountability systems and OPM's evaluation of agency accountability systems and human capital efforts. According to OPM, under its recent restructuring, agency human capital efforts, including accountability systems, are to be evaluated by its Agency Merit System Accountability and Human Resources Programs Office.

Although the actions OPM has taken and planned to improve governmentwide oversight of agencies' human capital systems are promising, the results of the merit principles surveys and MSPB's 2001 report show that there continues to be a need for strong oversight of the merit system from both OPM and the agencies, especially in this era of delegation and decentralization. MSPB reported in December 2001 that OPM needs to show strong leadership in fostering agency self-monitoring programs and find a way for its oversight reviews to address HRM accountability at the line manager and supervisor levels. While OPM's actions to improve governmentwide oversight are promising, the agency needs to do more to accomplish its oversight mission in a decentralized human capital environment in which responsibility for human capital management accountability continues to shift to agencies. Given that OPM's oversight approach includes encouraging and monitoring agency self-assessment programs, it could strengthen this approach by requiring, rather than encouraging, agencies to establish and maintain internal oversight programs and to meet its *HRM Accountability System Standards*. OPM could also develop standards that agencies' oversight staffs would need to meet to be fully qualified to conduct agency oversight reviews. In short, there are opportunities for OPM to build upon the positive efforts it has under way to promote agency self-monitoring programs and ensure that agencies have mechanisms in place for holding their managers and supervisors accountable.

OPM's Organizational Transformation Initiatives

As OPM implements its organizational transformation initiatives, which are shifting its role *from less* of a rule maker and enforcer *to more* of a strategic partner in leading and supporting executive agencies' human capital management systems, it is addressing the need to strategically manage its human capital, including effectively aligning its organizational structure and people resources to achieve its mission and goals, protect its information technology systems against security threats, and manage its financial resources. OPM has undertaken a number of initiatives to address these challenges. However, the experiences of successful major change management initiatives in large private and public sector organizations suggest that it can often take at least 5 to 7 years until such initiatives are fully implemented and the related cultures are transformed in a sustainable manner. Thus, it is entirely to be expected that as OPM moves forward, there are opportunities to strengthen and deepen its current efforts.

Strategic Human Capital Management

As the federal government's human capital agency, OPM must lead by example in managing its people. While OPM faces many of the same human capital challenges as other agencies, it must serve as a role model to other agencies in how to address these challenges. OPM has taken and planned actions to address its human capital challenges, and its actions are in line with the administration's *Human Capital Standards for Success.* OPM's actions also align with the four cornerstones of effective strategic human capital management outlined in our March 2002 model of strategic human capital management:[20] (1) leadership, (2) strategic human capital planning, (3) acquiring, developing, and retaining talent, and (4) creating results-oriented organizational cultures.

Leadership

In addition to demonstrating commitment to strategic human capital management governmentwide, OPM's top leadership has demonstrated this commitment internally by viewing people as important enablers of agency performance. In November 2002, OPM's Director changed the makeup of her senior leadership team by appointing four executives to new associate director positions to help implement the agency's restructuring effort approved in September 2002. The Director noted that the four executives collectively possess special skills in innovative HR reforms, e-Gov, and

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[20]GAO-02-373SP.

labor-management relations as well as knowledge of civil service protections. OPM also (1) sought input on its restructuring from its employees, local union representatives, and key external stakeholders such as departments and agencies, Congress, and academic and other public administration advocates, (2) involved employees in cross-organizational taskforces on other major agencywide projects, and (3) implemented employee-friendly workplace policies, such as telecommuting.

The rate of turnover among OPM's career Senior Executive Service (SES), due largely to retirements, varied widely from 0 percent in fiscal year 1997 to 21 percent in fiscal year 2001, according to OPM's calculations. The size of OPM's career SES workforce during this 5-year period ranged from 36 in fiscal year 1997 to 40 in fiscal year 1999. OPM's projected retirement rate for its SES over the next 10 years will be the largest—8 percent each year—of any group in its workforce, according to its June 2001 workforce analysis. The recent and projected losses in OPM's SES workforce will provide it with a challenge to maintain an effective leadership team.

In light of the impending retirements among its SES workforce, OPM has engaged in succession planning to ensure that it has the leadership talent in place to manage a transformed OPM effectively. OPM's succession planning initiative, begun in 2000, was not fully implemented due to other priorities and the need to consider succession planning in the context of OPM's transformation and restructuring efforts. These efforts naturally have implications for the competencies and career paths OPM will need to be successful. Nonetheless, now that the restructuring effort is being implemented, OPM can revisit and, if necessary, augment its succession planning strategies.

Strategic Human Capital Planning

OPM, like other agencies, was required by OMB to analyze its workforce and develop a plan for restructuring the agency that would meet the President's goals of creating agency organizational structures that are citizen-centered, results-oriented, and market-driven.[21] OPM prepared and submitted its workforce analysis and restructuring plan to OMB and has

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[21]OMB Bulletin No. 01-07, dated May 8, 2001, required agencies to conduct workforce analyses and to develop restructuring plans based on the workforce analyses. OMB directed agencies to submit their workforce analyses by June 29, 2001. The restructuring plans were to be submitted as a part of the agencies' 2003 budget submissions and annual performance plans.

taken and planned actions to address human capital challenges identified as a result of its workforce analysis.

In analyzing its workforce, OPM found that 4.2 percent of its employees (about 123 per year), on average, are projected to retire each year over the next 10 years, and as we discussed earlier, the largest percentage of projected retirements,[22] about 8 percent per year, will come from members of its career SES. OPM's expected retirement rate for its workforce overall is more than the annual retirement rate of 2 percent governmentwide identified in our April 2001 report.[23] OPM's projected career SES retirement rate also exceeds the career SES governmentwide rate of 6 percent, on average, each year identified in our May 2000 report.[24] In addition, OPM's workforce analysis found that of the 123 employees expected to retire each year over the next 10 years, about 25 percent of those retirements will come from employees in OPM's human resources specialist and retirement benefits specialist positions—two positions OPM has identified as being critical to its mission.

Significantly, the workforce analysis also found that skill gaps exist at varying levels in the majority of the jobs occupied by OPM employees as of September 30, 2000. These gaps exist in competencies needed by

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[22]OPM based its retirement projections on the yearly retirement patterns of permanent employees on board as of October 1, 1995, and then applied these patterns to determine retirement probabilities in each of the next 5 years. OPM controlled for variables, such as gender, occupational category, retirement system, and length of retirement eligibility, in determining the retirement probabilities. It then averaged the 1-year probabilities to obtain a composite 1-year probability estimate.

[23]U.S. General Accounting Office, *Federal Employee Retirements: Expected Increase Over the Next 5 Years Illustrates Need for Workforce Planning*, GAO-01-509 (Washington, D.C.: Apr. 27, 2001). In that report, we calculated a retirement rate of 2 percent per year until 2006 for employees at 24 executive branch agencies, which comprise about 98 percent of the federal workforce, excluding Postal Service, Federal Reserve, Tennessee Valley Authority, and intelligence agency employees. Our retirement projections covered the period from 1999 through 2006. For more information on our retirement projections, their assumptions, and methodology, see that report.

[24]U.S. General Accounting Office, *Senior Executive Service: Retirement Trends Underscore the Importance of Succession Planning*, GAO/GGD-00-113BR (Washington, D.C.: May 12, 2000). In that report, we calculated the average estimated annual SES retirement rate for fiscal years 1999 through 2005 on the basis of OPM's estimate of the SES retirement rate for that entire 7-year period. OPM's retirement estimate was based on the actual number of career SES retirements during fiscal years 1996 through 1998 to eliminate the effect of downsizing during the mid-1990s and the increase in retirements during fiscal year 1994 following the substantial 1991 SES pay raise.

employees to perform OPM's work both now and in the future. The skill gap analysis revealed that, overall, OPM's long-term skill needs were greater than its short-term needs, which according to OPM, reflects the impact of the agency's changing work and the high predicted turnover in mission-critical occupations. OPM employees' competency needs were determined through a survey of OPM executives, managers, and supervisors. Gaps were identified in competencies such as attention to detail, customer service, interpersonal skills, writing, oral communication, planning and evaluation, and technical competence.

OPM has developed plans to prepare for the expected retirements in its workforce and address skill imbalances. Its plans and strategies for addressing these and other human capital challenges are described in its *Restructuring Plan* and *Human Capital Scorecard Action Plan* submitted to OMB in September 2001 and January 2002, respectively. For example, in its *Restructuring Plan*, OPM identified strategies such as training to address skill gaps and recruiting and hiring from all sources to replace expected staff losses due to the impending retirements. And in its *Human Capital Scorecard Action Plan*, OPM identified goals and plans that related to (1) recruiting, hiring, developing, and retaining employees with the strategic competencies for its mission-critical occupations and (2) aligning its human capital policies and organizational structure with its mission, vision, and strategies. OPM's plans and strategies for addressing its human capital challenges represent important steps toward strategic human capital planning.

OPM's *Restructuring Plan* identified goals and strategies for addressing human capital challenges in each of its program offices. This action is in line with a recommendation we made in our July 2001 report as a result of reviewing OPM's fiscal year 2002 performance plan and fiscal year 2000 performance report as part of our Government Performance and Results Act work.[25] In that report, we recommended that OPM better link its internal strategic human capital management goals to specific OPM programs and outcomes. Its *Human Capital Scorecard Action Plan* lays out specific action items and target dates for completing each item that align with dimensions of its *Human Capital Scorecard*, released to agencies governmentwide in December 2001.

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[25]GAO-01-884.

Realigning its organizational structure and workforce in a way that will best achieve its mission, goals, and results has been challenging for OPM for several years. Since its creation in 1979, OPM has undergone a number of reorganizations[26]—three of which, including its most recent one that was approved in September 2002, have involved major restructurings of the agency. Some of the reorganizations resulted, in part, from different operating philosophies of its directors. OPM's latest restructuring, which it intends to complete by March 2003, is designed to create a new, flexible structure that will "de-stovepipe" the agency; enable it to be more responsive to its primary customers, federal departments and agencies; and focus on the agency's core mission. For example, OPM has decided to put its various program development offices under the control of one associate director and its product and services functions under another associate director to ensure that it appropriately and efficiently responds to its customers. Effective implementation of OPM's latest organizational and workforce realignment will be crucial to maximizing its performance as the federal government's human capital leader, assuring its own and other agencies' accountability, and ultimately achieving its goals.

OPM has also decided that its Equal Employment Opportunity (EEO) Officer will have direct access to the agency head on EEO case and policy issues but will directly report to, be rated by with input from the agency head, and be supervised by the Associate Director for Management on a day-to-day basis. Although OPM recognizes that regulatory and implementing guidance issued by the Equal Employment Opportunity Commission (EEOC) requires an agency's EEO Director to report to and be directly supervised by the agency head,[27] OPM officials indicated the reporting arrangement between its EEO Officer and agency head is in line with the intent or spirit of EEOC's requirement because it will allow the EEO Officer to report directly to the agency head on EEO case and policy issues when the EEO Officer deems it is necessary, which is critical. The OPM officials also indicated that an advantage of the reporting

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[26]For purposes of this report, a reorganization is defined as a change in the agency's organizational structure and/or reporting relationships, including adding or abolishing an office or function.

[27]EEOC's regulation, 29 C.F.R. 1614.102(b)(4), and guidance (EEOC Management Directive 110, Chapter 1) require an agency's EEO director to report to and be supervised directly by the agency head for the purposes of demonstrating the importance of EEO to employees and ensuring that the EEO director's independence is not undermined, particularly in situations where the person to whom he or she reports is involved in or would be affected by the EEO director's actions in implementing the agency's EEO program.

arrangement between OPM's EEO Officer and agency head is that it does not separate the EEO function from other HR functions that are the responsibility of the Associate Director for Management.

In implementing this arrangement, we believe that it is important for OPM to ensure that its EEO Officer's independence is not undermined as a result of placing him/her under the direct supervision of the Associate Director for Management who is responsible for the overall management of the agency, including overseeing EEO functions, which could affect HR functions. We also believe that it is important for the EEO Officer to have regular one-on-one meetings with the agency head in order for this reporting arrangement to work.

Talent

Similar to other agencies, OPM faces challenges in recruiting and retaining a high-quality, diverse workforce. In its workforce analysis, OPM said that its challenges in attracting and retaining employees are the result of lack of competitive pay with the private sector, cumbersome recruitment and hiring procedures for certain occupations, and a declining attraction of the public service—reasons that are not unique to OPM.

OPM will need to hire and develop employees to replace the loss of knowledge and expertise caused by departing employees and to address gaps in employees' skills identified through its workforce analysis. In addition, OPM will need to address shortfalls in employees' knowledge in two areas—non-title 5 personnel systems and a modernized retirement system environment. OPM recognizes that because an increasing number of agencies are being exempted from title 5 requirements, it will need to ensure that its employees are trained in the various laws, rules, and regulations that govern non-title 5 systems as well as the multiple environments in which they operate to oversee and evaluate them effectively. OPM also recognizes that as the focus of the retirement program shifts from transactions to customer service under its retirement systems modernization initiative[28] currently under way, it will need to ensure that its employees have the knowledge and skills to operate in this new environment. Our interviews with OPM officials and a review of OPM's workforce analysis, *Restructuring Plan,* and related documents

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[28]The retirement systems modernization initiative, which is being implemented in phases, is OPM's long-term strategy for reengineering business processes in order to improve all aspects of the delivery of retirement services. OPM expects the initiative to be fully operational in 2010.

indicate that OPM has strategies in place to meet these challenges. These strategies include expanding its hiring and recruitment sources and providing a variety of training and developmental opportunities to broaden employees' skills. While OPM does not have any numerical hiring goals over the next 5 years, it plans to hire and recruit from the widest sources possible to ensure that the agency has an available group of diverse and skilled candidates in line to assume future leadership responsibilities. OPM also plans to continue to use the Presidential Management Intern program.

To broaden the skills of employees, OPM notes that a particularly effective strategy has been its use of rotational assignments, special projects, and details to "cross-train" employees at various levels of the organization. These opportunities are intended to augment existing staff skills, teach new competencies, and better prepare employees and their work units for vacancies in key positions. OPM has made use of cross-organizational task forces to manage agencywide projects such as the restructuring plan, succession plan, and revision of its strategic plan. OPM says that participants serving on these task forces gain exposure to the full range of OPM's responsibilities and a deeper understanding of the work performed by other offices. In order to pass on the knowledge of departing staff members and expose less experienced staff members to OPM's institutional culture and history, OPM is developing a mentoring program called FOCUS (Facilitating Opportunities & Change that Unleash Success). This program, also a part of the agency's succession plan, is intended to broaden employees' knowledge and mitigate skill gaps within the agency.

While OPM's strategies to address its internal recruitment and retention needs are moving in the right direction, past studies have raised concerns about OPM's training program for new supervisors and its Core Competency Training and Development Model for all employees. In particular, a 1999 oversight review conducted by OPM's Office of Merit System Oversight and Effectiveness (OMSOE),[29] undertaken to assess the state of human capital management at OPM, reported that "newer supervisors" expressed concern about their preparation for supervisory responsibilities and stated that initial training for new supervisors was "uneven and sometimes nonexistent." The findings from OMSOE's report[30] are consistent with the findings from a March 2001 "environmental scan" of OPM's internal human capital management performed by the National Academy of Public Administration (NAPA) at OPM's request.[31] NAPA reported that OPM employees stated in focus groups that there was not a central focus within OPM on training needs assessment and that supervisory training within OPM was an area "needing attention."

In light of the fact that OPM has fewer supervisors now than in the past due to downsizing; is losing some of its more experienced executives, managers, and supervisors to retirement over the next few years; and is increasing its efforts to hire at the entry level, it is important that OPM have a strong training program for new supervisors in place. Supervisory training is also important to help OPM transform from a rules-monitoring organization to a customer-oriented organization that partners with agencies in managing their human capital. OMSOE recommended in its 1999 report that OPM's Office of Human Resources and Equal Employment

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[29]OMSOE, which is now a part of OPM's Agency Merit System Accountability and Human Resources Programs, assesses agencies' effectiveness in personnel management at the governmentwide, agency, and installation levels to gather information for policy development and program refinement, ensure compliance with personnel laws and regulations, enhance agency capability for human resources management accountability, and assist agencies in operating personnel programs that effectively support accomplishment of their primary missions consistent with merit system principles. OMSOE also works with federal agencies to explore potential improvements in personnel systems and better and simpler ways to manage federal personnel.

[30]U.S. Office of Personnel Management, Office of Merit Systems Oversight and Effectiveness, *Report of an Oversight Review: Office of Personnel Management* (Washington, D.C.: June 1999).

[31]National Academy of Public Administration, *An Environmental Scan for the Office of Human Resources and Equal Employment Opportunity, U.S. Office of Personnel Management* (Washington, D.C.: March 2001).

Opportunity develop a training course for new supervisors. According to OPM officials, a core training and development curriculum for new supervisors was introduced in the first quarter of fiscal year 2003 that is designed to provide new supervisors with the tools and competencies they need to perform effectively in their current positions and in future leadership positions.

OMSOE's 1999 oversight review also raised concerns with OPM's Core Competency Training and Development Model for all of its employees. While the review said that the model was a useful tool for new employees, it also reported that (1) experienced employees expressed disinterest in the Core Competency Training and Development Model because they did not believe it would help them advance, (2) managers felt that experienced employees did not want to use the model because they did not want to be viewed as needing training, (3) nonsupervisory employees felt that the training model was not job related, (4) supervisors felt that they could not track the results of the training model back to job performance, and (5) managers and supervisors felt that the model emphasized skills at the basic but not the advanced level. To address these concerns, OMSOE recommended that OPM explore establishing a structured program to provide rotational assignments throughout the agency and suggested that the Core Competency Training and Development Model might be the appropriate avenue for launching the rotational program. To increase employees' perceived usefulness of the core competency model and encourage greater use of it, OMSOE also suggested that OPM consider linking the model to other HR programs, such as career development and workforce planning. An OPM official told us that the agency is updating the Core Competency Training and Development Model.

Creating Results-Oriented Cultures

OPM has taken measures to ensure that the focus of individual expectations and accountability are centered on contributions to achieve organizational results. For example, OPM set a goal in fiscal year 1999 of aligning all of its employees' individual performance plans with the agency's strategic plan. OPM reported in its fiscal year 2000 performance and accountability report that it had achieved alignment for about 90 percent of its employees. OPM told us in July 2002 that all of its employees' performance plans have now been aligned with the agency's former strategic plan, fully accomplishing the goal it set in 1999. However, with the publication of OPM's new strategic plan in November 2002, OPM officials told us that employees' performance plans will be revised where needed to provide the critical link between organizational and individual

performance and that realignment of the plans will be completed in early 2003.

In addition to aligning all of its employees' performance plans with the agency's strategic plan, OPM told us that the selection criteria for its highest award, the Director's Award for Excellence, have been revamped and revised to ensure that the award recognizes those who have made clear contributions to the agency's strategic objectives and furthered the President's goal of creating a government that is citizen-centered, results-oriented, and market-based. Finally, OPM has taken steps to revise all of its executives' performance standards to include clear benchmarks for managing human and financial resources, furthering the President's management objectives, leading positive change, and building effective coalitions.

Information Security

Over the last 2 years, significant weaknesses have been identified in OPM's information systems' security program. OPM's information systems, which support its human capital and financial management operations, are used to manage billions of dollars in the retirement benefits, health benefits, and life insurance trust funds. These systems are also used to process retirement benefits for millions of annuitants and survivors and HR data for millions of active federal employees. And as OPM continues to develop and roll out the five e-Gov projects that the administration assigned it to lead—Recruitment One-Stop, e-Training, e-Clearance, Enterprise Human Resource Integration, and e-Payroll—these systems will also be used to maintain and process HR data. Because OPM's information systems are used to process significant amounts of sensitive but unclassified data supporting both human capital and financial management operations, protecting these systems from computer-based attacks is crucial. Since 1997, we have designated information security as a governmentwide high-risk area because evidence indicated that controls over computerized federal operations were not effective and the related risks were escalating, in part, due to increasing reliance on the Internet. Furthermore, governmentwide audits conducted in 2001 and 2002 continued to show that operations and assets across the federal government were highly vulnerable to computer-based attack.

OPM is working to resolve the weaknesses in its information security program that were identified during audits by an independent accounting firm, OPM's Office of the Inspector General (OIG), and us[32] during fiscal years 2001 and 2002. OPM has implemented new security guidance and has developed a plan to resolve these weaknesses. Also, OPM told us that it has consistently completed actions contained in the plan and is on schedule to meet its remaining milestones. OPM's efforts to address weaknesses in its information security program are part of its ongoing actions to achieve compliance with federal financial management statutes as they relate to information security and with information security requirements contained in the Government Information Security Reform provisions (commonly referred to as "GISRA").[33] As part of its fiscal year 2001 financial statement audit, the independent accounting firm assessed OPM's compliance with the Federal Financial Management Improvement Act of 1996[34] (FFMIA) requirements as they relate to information systems security. The independent accounting firm found that OPM had not provided adequate systems security. It also found that OPM's electronic data processing (EDP) general control environment continues to be a reportable condition from the prior year[35] and five areas of EDP general control need to be strengthened: (1) agencywide security program management, (2) access controls, (3) system software controls, (4) software development and change controls, and (5) service continuity.

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[32]This work was performed as part of our assessment of 24 agencies' compliance with the Government Information Security Reform provisions in the National Defense Authorization Act for Fiscal Year 2001 (Pub. L. No. 106-398, Oct. 30, 2000). Our findings were presented in testimony before the Subcommittee on Government Efficiency, Financial Management and Intergovernmental Relations, Committee on Government Reform, House of Representatives entitled *Information Security: Additional Actions Needed to Fully Implement Reform Legislation*, GAO-02-470T (Washington, D.C.: Mar. 6, 2002). In presenting the results of our work, we reported the results for 24 agencies in the aggregate but did not report the results for each of the 24 agencies individually.

[33]Similar to other agencies, OPM is subject to the requirements of GISRA, which require, in part, that (1) agencies establish agencywide, risk-based information security programs, (2) the inspector general of each agency conduct an independent evaluation of the agency's information security program, and (3) OMB submit an annual report to Congress summarizing the results of agencies' evaluations of their information security programs.

[34]31 U.S.C. section 3512 note.

[35]A reportable condition is a matter coming to an auditor's attention relating to significant deficiencies in the design or operation of the internal controls over financial reporting that, in the auditor's judgment, could adversely affect an agency's ability to record, process, summarize, and report financial data consistent with the assertions by management in financial statements.

According to the independent accounting firm, these conditions could affect OPM's ability to prevent and detect unauthorized changes to financial information, control electronic access to sensitive information, and protect OPM's information resources.

As required by GISRA, OPM's OIG independently evaluated OPM's information security program and reported in September 2002[36] that OPM had made significant progress in improving its information security program since 2001 but could make more improvements. For example, the OIG noted that OPM had integrated its information security requirements and costs estimates into its capital planning and investment control process and took significant steps to meet its governmentwide security training responsibilities. The OIG also noted that OPM's agencywide security policy, originally released in June 2001 and revised in March 2002, and its efforts to certify and accredit its two general support systems—the Enterprise server and local area network/wide area network—are two positive steps that will help OPM to achieve greater compliance with GISRA's requirements. However, the OIG said that although no material weaknesses were found in OPM's information security controls, a number of reportable conditions were identified that OPM needs to address. For example, the OIG said OPM still had not (1) fully implemented its agencywide security program, although it issued implementation guides during the year, (2) integrated its information security program with its critical infrastructure responsibilities, (3) conducted risk assessments for all of its systems, (4) completed security plans for all of its systems, or (5) developed a process to track and monitor specialized training requirements for personnel with significant security responsibilities. These reportable conditions are addressed in OPM's action plan, and according to OPM officials, progress has been made in overcoming them.

The independent accounting firm's and OPM's OIG findings are consistent with ours. In March 2002, we testified on the federal government's efforts in implementing GISRA requirements during fiscal year 2001.[37] We testified that OPM and 23 other large agencies had not conducted risk assessments for all of their systems, and almost half of the agencies had not established

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[36]U.S. Office of Personnel Management, Office of the Inspector General, *Government Information Security Reform Act Fiscal Year 2002 Independent Evaluation, Executive Summary* (Washington, D.C.: Sept. 9, 2002).

[37]U.S. General Accounting Office, *Information Security: Additional Actions Needed to Fully Implement Reform Legislation*, GAO-02-470T (Washington, D.C.: Mar. 6, 2002).

effective performance measures to show how well program officials had assessed the risk to operations and assets under their control. Our review disclosed significant weaknesses in four out of six major areas of OPM's general controls—the policies, procedures, and technical controls that apply to all or a large segment of OPM's information systems and help to ensure their proper operation. In particular, we found weaknesses in OPM's (1) security program management, (2) access controls, (3) change controls, and (4) service continuity.

In its plan of action and milestones (POA&M) report submitted to OMB in November 2001,[38] OPM proposed corrective actions to address a total of 15 weaknesses in its information security program. As of April 30, 2002, OPM reported that it had completed actions for 2 of the 15 identified weaknesses and that corrective actions for the remaining 13 were ongoing. OPM has also taken steps to implement its agencywide security program. For example, it issued an updated information technology security policy in March 2002 that, in part, requires and ensures that security planning is integrated into each of its systems' development life cycle processes and established a formal working group to oversee implementation of the security policy and security program at OPM. OPM also told us that it is applying its information security policy to the five e-Gov projects it is leading and developing a specific e-government Security Management Plan for each e-Gov project. According to OPM, each e-government project's Security Management Plan covers, as appropriate, risk assessment, data encryption, intrusion detection and repudiation, information availability and assurance, audit tracking, user authentication, physical site security, catastrophic disaster recovery, data and power supply redundancy and backup, and computer virus detection and prevention. OPM expects to fully implement its agencywide security program in September 2003 according to its POA&M report submitted to OMB in November 2001.

Although OPM has taken positive steps to improve its information security program, it must continue its efforts to achieve compliance with GISRA and federal financial management statutes as they relate to information security. In addition, it is important that OPM continues its plans to incorporate appropriate information security controls into the design and development of the five e-Gov projects it has been assigned to lead. These

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[38]OPM's POA&M report is a list of corrective actions that OPM will take in response to information security weaknesses identified by its Chief Information Officer, independent auditor, OIG, or us.

controls will help to ensure the integrity, reliability, and availability of data and systems used for the e-Gov projects.

Financial Management

OPM received an unqualified or "clean" opinion on its fiscal year 2000 and 2001 consolidated financial statements, and the independent public accounting firm hired by OPM's OIG to perform these audits reported no material weaknesses[39] in internal controls over financial reporting. However, the independent accounting firm identified several reportable conditions[40] over financial reporting, many of which relate to long-standing problems with OPM's accounting for the activities of its two discretionary accounts—the Salaries and Expenses account and the Revolving Fund. In its audit report, the independent accounting firm also stated that the financial management systems supporting OPM's discretionary accounts as well as its retirement, health benefits, and life insurance programs did not substantially comply with certain requirements of FFMIA[41] that relate to federal financial management system requirements and the *U.S. Government Standard General Ledger* at the transaction level.

Historical weaknesses in accounting for and reporting on the activities of the Revolving Fund and the Salaries and Expenses account have included (1) the inability to substantiate and reconcile reported account balances with OPM's own subsidiary records as well as information maintained by other federal agencies, (2) lack of or failure to adequately implement policies and procedures, and (3) insufficient analyses and review of the financial statements, footnotes, and related adjusting entries. Contributing to some of these weaknesses have been staffing limitations and skill deficiencies as well as weaknesses in computer controls. Evidence of these continuing weaknesses led the independent accounting firm to

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[39]Material weaknesses in internal control are reportable conditions in which the design or operation of the internal control does not reduce to a relatively low level the risk that errors, fraud, or noncompliance in amounts that would be material in relation to the financial statements or other required information being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned duties.

[40]See footnote 35.

[41]Under FFMIA, an agency head must determine whether his or her agency is in substantial compliance with three requirements: (1) federal financial management system requirements, (2) federal accounting standards, and (3) the *U.S. Government Standard General Ledger* at the transaction level.

conclude that as of the end of fiscal year 2001, OPM's financial management systems were not in substantial compliance with FFMIA. These weaknesses call into question OPM's ability to produce timely and accurate financial information for management decision making and financial reporting purposes relative to these two accounts.

The independent accounting firm and OPM's OIG both agree that OPM made progress during fiscal year 2001 in addressing these various weaknesses. A key step to resolving many of its reportable conditions and material system nonconformances is OPM's phased implementation of a new financial management system that supports the Revolving Fund and Salaries and Expenses account and that will eventually interface with the benefit plans' financial systems to enable timely and accurate preparation of consolidated agency financial statements. OPM expects to have completed the last phase of the system implementation by the end of fiscal year 2003, at which time OPM plans to have audits performed on the stand-alone Revolving Fund and Salaries and Expenses account financial statements, in addition to the consolidated agency financial statements, to demonstrate that the discretionary funds' financial statements can successfully pass an audit. OPM has stated that the new system, once fully operational, will improve its overall financial performance by allowing it to routinely report the full cost of programs and projects; integrate program, budget, and financial information; and use this information to measure, monitor, and report on program performance.

Federal Retirement and Health Benefits Program Administration

Through its retirement and health insurance programs, OPM delivers retirement and health insurance benefits to millions of federal employees, annuitants, and their dependents totaling billions of dollars annually. In fiscal year 2001, OPM paid $47 billion in annuities to more than 2 million retired federal employees, annuitants, and their dependents. OPM—which is the largest purchaser of employee health benefits—also paid almost $21 billion in health insurance premiums for more than 8 million enrollees and their dependents in fiscal year 2001. Thus, OPM's accurate, cost-effective, and efficient administration of the retirement and health insurance programs is critical given the substantial dollar outlays. Results of recent independent surveys[42] indicated that OPM's customers have been satisfied with the quality of retirement services and health insurance products and services. The results of OPM's own client satisfaction survey have also indicated that retirees have been highly satisfied with services provided by the agency. However, customer satisfaction could fall in the coming years if OPM is not prepared to handle the expected federal employee retirement wave and implement cost-containment strategies for limiting health care premium increases while continuing to ensure that employees are provided access to quality health care.

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[42]The independent surveys include the American Customer Satisfaction Index, which is used to measure customer satisfaction with OPM's retirement services, and the Consumer Assessment of Health Plans Study, which is used to get customer feedback on performance of health plans in the Federal Employees Health Benefits Program.

In 2001, as in prior years, OPM's retiree customers responding to the American Customer Satisfaction Index survey reported that they were highly satisfied with services they received from OPM. For example, in 2001 OPM received an overall satisfaction rating of 78 (out of a possible 100) for delivery of retirement services, such as timeliness of benefit payments and timeliness of OPM's response to inquiries. OPM's 2001 satisfaction rating represented an increase over its 1999 and 2000 ratings of 75 and 73, respectively, and surpassed the private sector rating of 70.5. In addition, over 90 percent of annuitants responding to OPM's client satisfaction survey said they were satisfied with overall retirement services during 1999 through 2001. Moreover, for fiscal years 1999 through 2001, erroneous retirement payments constituted less than 1 percent of total retirement payments. OPM also reduced its processing times for retirement claims in 2001 and surpassed its target.[43] However, the level of customer satisfaction OPM has achieved and its timeliness in processing claims could dwindle over the next few years if the agency is not able to handle the dramatic increase expected in the number of employees seeking retirement services. By 2006, about one-third (493,000 employees) of the federal workforce will be eligible to retire and about one-half (236,000 employees) of those eligible are expected to retire. OPM's modernized retirement systems—the agency's long-term strategy for delivering more cost-efficient, timely, and accurate retirement services—is planned to be fully operational in 2010. Because modernization of the retirement systems is a complex, long-term undertaking and given the costs and implementation risks associated with it, OPM is considering outsourcing the claims processing and customer service functions.

OPM measures its success in administering the Federal Employees Health Benefits Program (FEHBP), in part, by active and retired employees' perceptions of the quality of the health plans and their accreditation. OPM reported that 82 percent of employees enrolled in FEHBP were in highly rated health plans in 2001, which indicates that they were receiving high-quality health insurance products and services. Other measures of OPM's success in administering the health benefits program are the agency's progress in achieving less fraud and abuse in the program and improving performance and financial oversight of the program—areas that have been

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[43]OPM's target time for processing Civil Service Retirement System claims was 55 calendar days; actual time was 54 calendar days. For Federal Employees Retirement System claims, the target time was 150 calendar days; actual time was 101 calendar days.

identified as top management challenges facing OPM at some point over
the last 2 years.

In January 2002, OPM's OIG removed fraud and abuse in FEHBP from its
list of top challenges facing OPM because it found no material weaknesses
and fewer errors in the program. In fiscal year 2001, erroneous health
benefit payments constituted less than 1 percent of total health benefit
payments. However, the OIG still recognizes that health care fraud is a
nationwide problem and that FEHBP continues to be subjected to this
problem.

Regarding improving performance of the health benefits program,
controlling the costs of premiums is a great concern to the government
because it pays, on average, 72 percent of the total premium, according
OPM's OIG. The OIG noted that OPM is often limited in how it can control
cost increases without also cutting desired health care benefits. We
recently reported that during the period 1991 through 2002, FEHBP
premium increases, overall, have been similar to those for other large
purchasers of employee health benefits, although the increases in the
FEHBP premiums rose slightly faster than other large purchasers from
1997 through 2002. [44] In 2003, health care premiums under FEHBP
increased, on average, 11 percent, continuing a 3-year trend of double-digit
premium increases, although the 2003 premium increase is less than those
for some other large purchasers of employer-sponsored health insurance.
For example, the California Public Employees' Retirement System
(CalPERS)—the second largest public purchaser of employee health
benefits—announced that its health maintenance organizations premiums
increased an average of 26 percent in 2003. To help mitigate FEHBP
premium increases for 2003, OPM told us that it initiated a four-point
strategy that contributed to these premium increases being below national
trends. OPM's strategy, in part, included OPM asking FEHBP health plan
carriers to develop and submit innovative benefit proposals that would not
only maintain the quality of but also contain the cost of health care.

We also reported that OPM relies on enrollee choice, competition among
plans, and its annual negotiations with participating plans to help control
premium increases, whereas other large public and private purchasers
adopt different negotiating strategies. For example, we noted that in the

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[44]U.S. General Accounting Office, *Federal Employees' Health Plans: Premium Growth and
OPM's Role in Negotiating Benefits*, GAO-03-236 (Washington, D.C.: Dec. 31, 2002).

past, OPM has encouraged plans to consider cost-containment strategies, such as increased use of generic drugs and expansion of preferred provider organizations, to lower the cost of premiums. For the 2003 federal health benefits open season, OPM encouraged plans to consider cost-containment strategies such as increasing enrollees' out-of-pocket costs and emphasizing care management for enrollees with chronic conditions. Other major purchasers use other approaches to lower the cost of health benefit premiums. For example, CalPERS and General Motors negotiate based on standard benefit packages, and at the end of negotiations can decide not to include a plan that does not meet their cost or quality standards.

Regarding financial oversight of FEHBP, OPM's OIG reported in January 2002 that OPM has taken steps to provide more effective financial oversight of the program, such as issuing an *Audit Guide* that requires experienced-rated carriers to obtain an annual audit of FEHBP activities and to report on their internal control structures. However, the OIG also reported that OPM still needs to improve its oversight and monitoring of the reconciliation of monies paid as premiums to participating community-rated carriers with the enrollees for whom they were being paid. The OIG noted that because OPM's existing systems were not designed to reconcile differences between enrollment and premium payments, the potential exists for carriers to provide benefits to employees who are not covered by their plans at the time services are rendered. To address this problem, OPM implemented the Centralized Enrollment Clearinghouse System in the summer of 2002. This system is expected to facilitate the carrier and agency reconciliation process.

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