Required Supplementary Stewardship Information: Social Insurance

Statement of Social Insurance

Actuarial Surplus or (Deficiency) [a]

75-year Projection as of January 1, 2005

(Present values in millions of dollars)

	1/1/2005	1/1/2004	1/1/2003	1/1/2002	1/1/2001
Estimated future income (excluding interest)[b] received from or on behalf of:					
Current participants not yet having attained retirement age	$56,842	$55,778	$58,315	$60,452	$60,437
Current participants who have attained retirement age	56,859	54,882	54,491	51,137	51,202
Those expected to become participants	31,313	30,327	32,419	30,843	30,690
Subtotal – contributions and tax income for the 75-year period	145,014	140,986	145,225	142,432	142,329
Estimated future expenditures[c]:					
Current participants not yet having attained retirement age	72,927	71,803	72,976	75,781	74,453
Current participants who have attained retirement age	84,054	81,128	80,374	73,840	73,455
Those expected to become participants	15,783	13,912	13,789	12,776	12,905
Subtotal – benefit payments for the 75-year period	172,764	166,843	167,139	162,397	160,813
Estimated future excess[d] of income over expenditures	(27,750)	(25,857)	(21,914)	(19,965)	(18,484)

Footnotes to the Statement of Social Insurance:

[a] Represents combined values for the RR Account, SSEB Account, and NRRIT.

[b] Future income (excluding interest) includes tier 1 taxes, tier 2 taxes, income taxes on benefits, financial interchange income, advances from general revenues, and repayments of advances from general revenues. The calculations assume that all future transfers required by current law under the financial interchange will be made.

[c] Future expenditures include benefit and administrative costs.

[d] A closed group estimate using the projected tax rates under employment assumption II may be obtained by excluding amounts for "Those expected to become participants" listed above.

Additional Notes:

The fund balances as of 1/1/2005, 1/1/2004, 1/1/2003, 1/1/2002, and 1/1/2001 were $28,570 million, $26,616 million, $22,679 million, $20,861 million, and $19,251 million, respectively.

Detail may not add to totals due to rounding. Employee and beneficiary status are determined as of 1/1/2004, whereas present values are as of 1/1/2005. Prior to 2003, present value categories for "Current participants not yet having attained retirement age" included those employees eligible for retirement who had not yet retired.

Program Financing

Payroll taxes paid by railroad employers and their employees are the primary source of funding for the railroad retirement-survivor benefit programs. Railroad retirement taxes, which have historically been higher than social security taxes, are calculated, like benefit payments, on a two-tier basis. Railroad retirement tier 1 payroll taxes are coordinated with social security taxes so that employees and employers pay tier 1 taxes at the same rate as social security taxes. In addition, both employees and employers pay tier 2 taxes that are used to finance railroad retirement benefit payments over and above social security levels. Beginning with calendar year 2004, the tier 2 tax rate is based on the ratio of certain asset balances to the sum of benefit payments and administrative expenses.

Revenues in excess of benefit payments are invested to provide additional trust fund income. The NRRIT oversees most investments, including all investments in non-governmental assets. The Board of Trustees of the NRRIT is comprised of three members selected by rail labor to represent the interests of labor; three members likewise selected by rail management to represent management interests; and one independent member selected by a majority of the other six members.

Additional trust fund income is derived from the financial interchange (FI) with the social security trust funds, revenues from Federal income taxes on railroad retirement benefits, and appropriations from general treasury revenues provided after 1974 as part of a phase-out of certain vested dual benefits.

The financial interchange between the railroad retirement and social security systems is intended to put the SSA Federal Old-Age, Survivors, and Disability Insurance (FOASI/DI) trust funds and the CMS Federal Hospital Insurance (FHI) trust fund in the same position they would have been had railroad employment been covered under the Social Security and Federal Insurance Contributions Acts. It follows that all computations under the FI are performed according to social security law. The amount of benefits payable under the RRA has no effect on the results.

Placing the social security trust funds in the same position they would have been had railroad employment been covered under social security since its inception involves computing the amount of social security payroll and income taxes relating to railroad employment and computing the amount of additional benefits which social security would have paid to railroad retirement beneficiaries during the same fiscal year. In the computation of the latter amount, credit is given for any social security benefits actually paid to railroad retirement beneficiaries. When benefit reimbursements exceed payroll and income taxes, the difference, with an allowance for interest and administrative expenses, is transferred from the social security trust funds to the SSEB Account. If taxes exceed benefit reimbursements (this has not happened since 1951), a transfer would be made in favor of the social security trust funds.

On a present value basis, funds provided through the FI are expected to equal $63,098 million, or 43.5 percent of the estimated future income of $145,014 million.

Benefits

Full age annuities are payable at age 60 to workers with 30 years of service. For those with less than 30 years of service, reduced annuities are payable at age 62 and unreduced annuities are payable at full retirement age, which is gradually rising from 65 to 67, depending on year of birth. Disability annuities can be paid on the basis of total or occupational disability. Annuities are also payable to spouses and divorced spouses of retired workers and to widow(er)s, surviving divorced spouses, remarried widow(er)s, children, and parents of deceased railroad workers. Qualified railroad retirement beneficiaries are covered by Medicare in the same way as social security beneficiaries.

Jurisdiction over the payment of retirement and survivor benefits is shared by the RRB and SSA. The RRB has jurisdiction over the payment of retirement benefits if the employee had at least 10 years of railroad service, or 5 years if performed after 1995; for survivor benefits, there is an additional requirement that the employee’s last regular employment before retirement or death was in the railroad industry. If a railroad employee or his or her survivors do not qualify for railroad retirement benefits, the RRB transfers the employee’s railroad retirement credits to SSA, where they are treated as social security credits.

Program Finances and Sustainability

The RRB must submit to the President and the Congress a report on the actuarial status of the Railroad Retirement system. Projections are made of the various components of income and outgo under three employment assumptions.

The Statement of Social Insurance presents an actuarial analysis of the financial position of the RR System as of January 1, 2005. The figures in the table are based on the 2005 Section 502 actuarial valuation extended through calendar year 2079. The present values in the table are based on estimates of contributions and expenditures through the year 2079. The estimates include contributions and expenditures related to future participants as well as to former and present railroad employees. The present values are computed on the basis of economic and demographic assumptions and employment assumption II, the intermediate employment assumption, as used in the 2005 Section 502 actuarial valuation. Under employment assumption II, starting with an average 2004 employment of 227,000, (1) railroad passenger employment is assumed to remain level at 43,000, and (2) the employment base, excluding passenger employment, is assumed to decline at a constant annual rate of 3.0 percent for 25 years, at a reducing rate over the next 25 years, and remain level thereafter.

Required Supplementary Stewardship Information*:* Actuarial estimates of the long-range financial condition of the Railroad Retirement program are presented here. Throughout this section, the following terms will generally be used as indicated:

- Income: sources of income are payroll taxes, income taxes, interest income, and financial interchange transfers.

- Income excluding interest[a]**:** income, as defined above, excluding the interest income from assets of the trust fund.

- Expenditures**:** benefit payments and administrative expenses.

- Cashflow**:** either (1) income excluding interest or (2) expenditures, depending on the context, expressed in nominal dollars.

- Net Cashflow**:** income excluding interest less expenditures, expressed in nominal dollars.

The statement presented on page 68 and the required supplementary information below are based on actuarial and economic assumptions used in the 2005 Section 502 actuarial valuation extended through calendar year 2079, the RRA, and the Railroad Retirement Tax Act. This information includes:

(1) actuarial present values of future estimated expenditures for and estimated income from, or on behalf of, current and future program participants;

(2) estimated annual income excluding interest and expenditures in nominal dollars and as a percentage of taxable payroll;

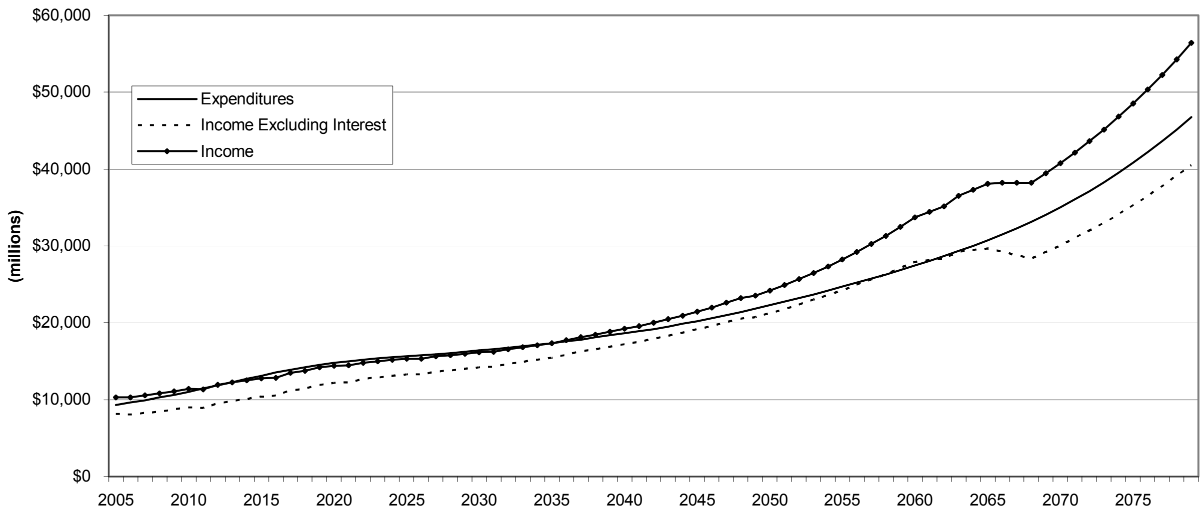
(3) the ratio of estimated annuitants to estimated full-time employees, showing the relationship between the program's benefit recipients and taxpayers; and

(4) an analysis of the sensitivity of the projections to changes in selected assumptions, which is included in recognition of the inherent uncertainty of those assumptions.

Estimates are generally based on a 75-year projection period. Estimates extending far into the future are inherently uncertain, with uncertainty greater for the more distant years.

[a] References to interest income in this section may be considered as referring to total investment income including dividends and capital gains.

Chart 1: Estimated Income and Expenditures

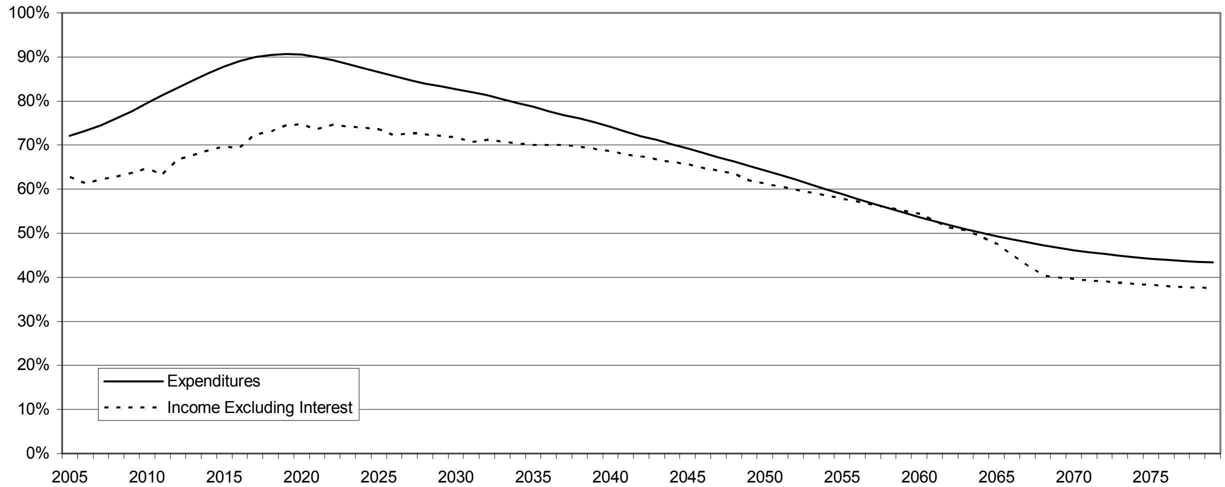


Cashflow Projections – Chart 1 shows actuarial estimates of railroad retirement annual income, income excluding interest, and expenditures for 2005-2079 in nominal dollars. The estimates are for the open-group population, which includes all persons projected to participate in the Railroad Retirement program as railroad workers or beneficiaries during the period. Thus, the estimates include payments from, and on behalf of, those who will be employed by the railroads during the period as well as those already employed at the beginning of the period. They also include expenditures made to, and on behalf of, such workers during that period.

As Chart 1 shows, annual expenditures begin to exceed annual income in 2011, income is briefly greater than expenditures in 2012, and then the trend of expenditures greater than income continues again in 2013. This continues for more than two decades, but by 2036 income is once again greater than expenditures. This remains true throughout the remainder of the projection period. Without investment income, however, annual expenditures are almost always greater than annual income, except for the period 2058-2061. Reasons for this pattern include participant demographics, the assumed drop in railroad employment, and the automatic tier 2 tax rate adjustment mechanism. The combined balance of the NRRIT, RR Account, and SSEB Account never becomes negative largely because (i) a sufficient balance exists at the beginning of the projection period and (ii) tier 2 tax rates respond automatically to changing account balances.

Percentage of Taxable Payroll – Chart 2 shows estimated annual income excluding interest and expenditures for the railroad retirement program expressed as percentages of taxable payroll. Benefits and administrative expenses as a percentage of payroll increase through 2020 primarily due to the anticipated retirement of a large percentage of the current workforce combined with the projected decline in railroad employment. Except for the income from tier 1 payroll taxes, the sources of income vary as a percentage of payroll.

Chart 2: Estimated Railroad Retirement Income Excluding Interest and Expenditures as a Percent of Taxable Tier 2 Payroll



Sensitivity Analysis – The projections of the future financial status of the railroad retirement program depend on many economic and demographic assumptions including rail employment, inflation, wage increase, investment return, age retirement, disability retirement, withdrawal, active service mortality, beneficiary mortality, total termination, probability of spouse, remarriage, family composition, disability freeze, service patterns, and salary scales. Because perfect long-range projections are impossible, this section is included to illustrate the sensitivity of the long-range projections to changes in certain key assumptions that have the greatest impact on the results. All present values are calculated as of January 1, 2005, and are based on estimates of income and expenditures during the projection period 2005-2079.

Employment: Average employment in the railroad industry has generally been in decline for some years. This decline is expected to continue. Since employment is a key consideration, projections of income and expenditures using three different employment assumptions have been made. The Statement of Social Insurance uses employment assumption II, the intermediate assumption, but this section compares results under the three assumptions. For all three cases, the average employment for the year 2004 is equal to 227,000. Employment assumptions I and II, based on a model developed by the Association of American Railroads, assume that (1) passenger employment will remain at the level of 43,000, and (2) the employment base, excluding passenger employment, will decline at a constant annual rate (1.5 percent for assumption I and 3.0 percent for assumption II) for 25 years, at a reducing rate over the next 25 years, and remain level thereafter. Employment assumption III differs from employment assumptions I and II by assuming that (1) passenger employment will decline by 500 per year until a level of 35,000 is reached and then remain level, and (2) the employment base, excluding passenger employment, will decline at a constant annual rate of 4.5 percent for 25 years, at a reducing rate over the next 25 years, and remain level thereafter. Employment assumptions I, II, and III are intended to provide an optimistic, moderate, and pessimistic assumption, respectively.

Under the first two employment assumptions, no cashflow problems occur throughout the entire period. Under the third employment assumption, cashflow problems occur in 2034. Table 1 shows the excess of assets and the present value of income over the present value of expenditures for the three employment assumptions.

Table 1
Excess of Assets and Present Value of Income over Present Value of Expenditures for Three Employment Assumptions, 2005-2079
(in millions)

Employment Assumption	I	II	III
Present Value	$1,118	$820	$268
Average Tier 2 tax rate[a]	15.0%	16.8%	19.0%

[a]Average combined employer/employee tier 2 tax rate is calculated by dividing the present value of tier 2 taxes by the present value of tier 2 payroll. Beginning in 2004, tier 2 tax rates vary based on a ratio of assets to the sum of benefits and administrative expenses. Tier 1 tax rates remain the same as for social security and are not affected by employment assumptions.

Chart 3a shows the combined balance of the accounts under each of the three employment assumptions. Note that from 2034 through 2075, the combined account balance is negative under employment assumption III.

Chart 3a: Combined Balance of the RR Account, NRRIT and SSEB Account under Three Employment Assumptions

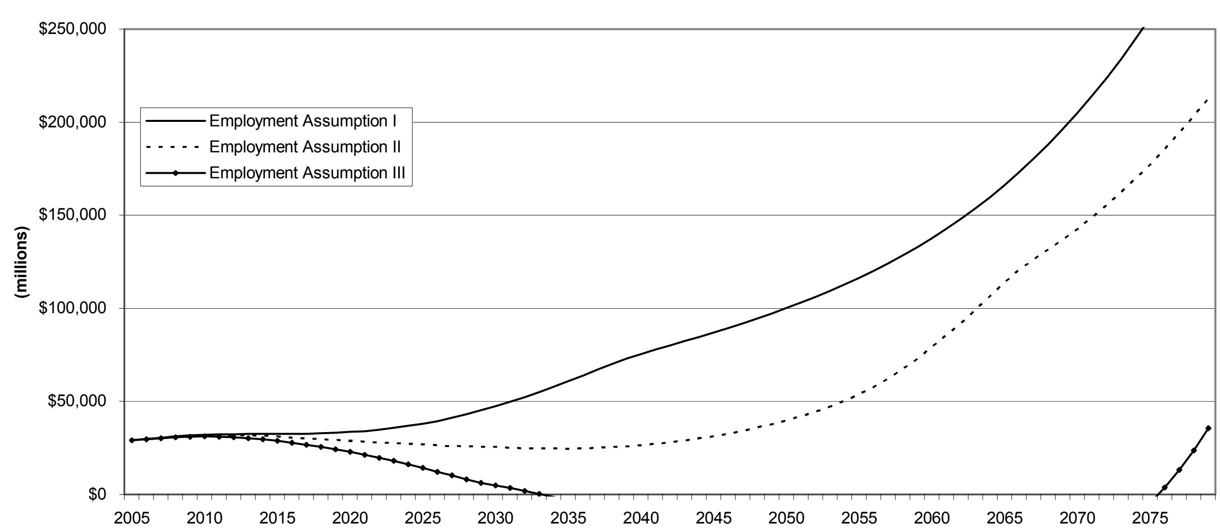
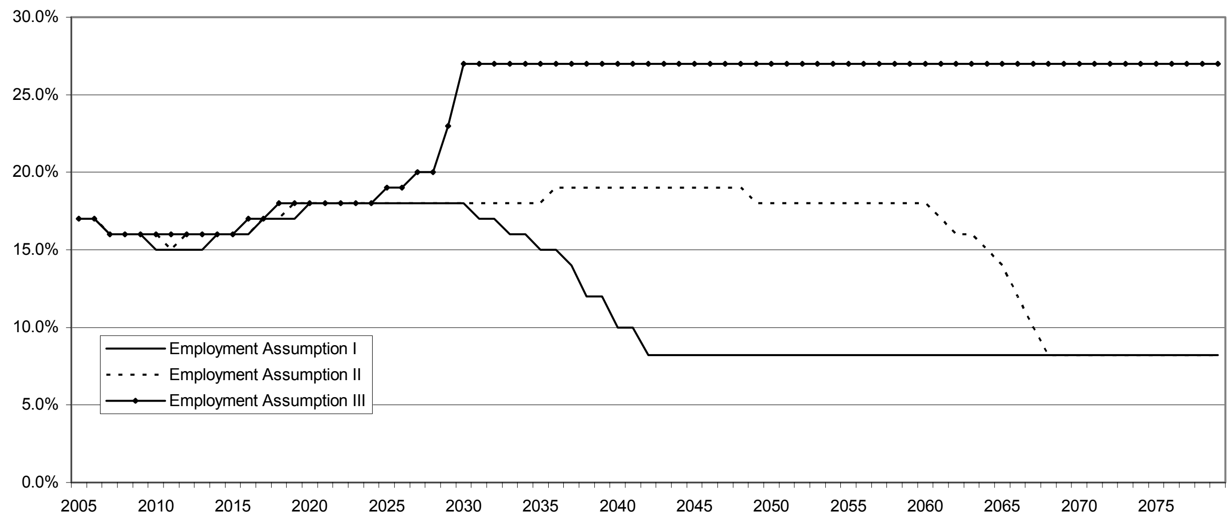


Chart 3b shows the tier 2 tax rate under these employment assumptions. The tax rate reaches the minimum in 2042 under employment assumption I but not until 2068 under employment assumption II. Under employment assumption III, the tax rate reaches the maximum in 2030 and remains at that level throughout the remainder of the projection period because the combined account balances are negative for most of the remaining period.

Chart 3b: Tier 2 Tax Rate under Three Employment Assumptions



Under the provisions of the RRSIA, the tier 2 tax rate for each year is determined by the average account benefits ratio, which is the average for the ten most recent fiscal years of the ratio of fair market value of assets in the RR Account and NRRIT (and for years before 2002, the SSEB Account) to the total benefits and administrative expenses paid from the RR Account and the NRRIT. Therefore, the tier 2 tax rate will be affected by employment assumption. The tier 2 tax rate adjustment mechanism promotes but does not guarantee solvency. The tier 1 tax rate does not vary by employment assumption.

Interest rates: Since investments may include non-governmental assets such as equity and debt securities as well as governmental securities, it is worthwhile to examine the effects of future rates of investment return. In addition to the interest rate of 8 percent used for our projections, we show the effect on the combined accounts of an interest rate of 4 percent and an interest rate of 12 percent. Table 2 shows the excess of assets and the present value of income over the present value of expenditures for the three interest rate assumptions. If the tier 2 tax rate were fixed, the actuarial surplus would increase with increasing investment return. However, the tier 2 tax rate adjusts to changing account balances, resulting in the highest average tax rate under the 4 percent scenario and the lowest average tax rate under the 12 percent scenario. Under the 8 percent scenario, the tax rate adjustment mechanism keeps the system in close actuarial balance. Under the 12 percent scenario, the tax rate is limited to a minimum value, resulting in a higher surplus. Under the 4 percent scenario, the tax rate reaches a maximum value and then remains at that value longer than is needed, resulting in the highest actuarial surplus.

Table 2
Excess of Assets and Present Value of Income over Present Value of Expenditures for Three Interest Rate Assumptions, 2005-2079
(in millions)

Interest Rate Assumption	4%	8%	12%
Present Value	$7,510	$820	$3,995
Average Tier 2 tax rate	21.4%	16.8%	12.9%

Chart 4a shows the combined account balance under the three interest rate assumptions for the projection period. At a 4 percent interest rate, the account balance becomes negative in 2029, reaching its lowest value in 2034. The account balance remains negative until 2040, at which time it becomes positive again and continues to increase. With an 8 percent interest rate, the account balance increases through 2010, decreases from 2012 to 2035, and increases thereafter. A 12 percent interest rate results in a combined balance that increases throughout the projection period. Although the 4 percent scenario shows the lowest account balance at the end of the projection period, the concurrent use of a 4 percent discount rate results in the highest surplus on January 1, 2005.

Chart 4a: Combined Balance of the RR Account, NRRIT and SSEB Account under Three Interest Assumptions

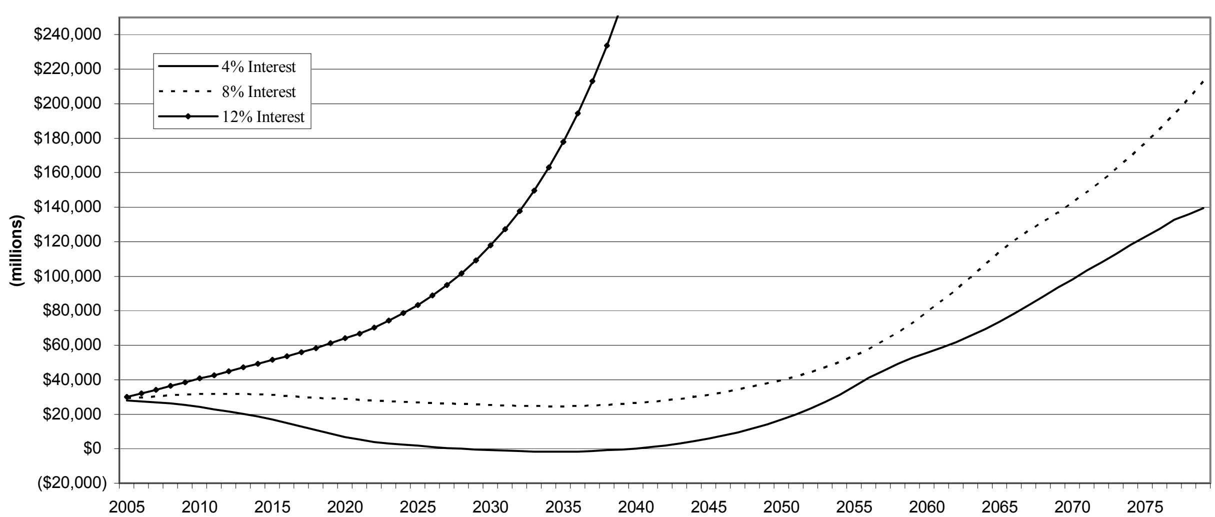
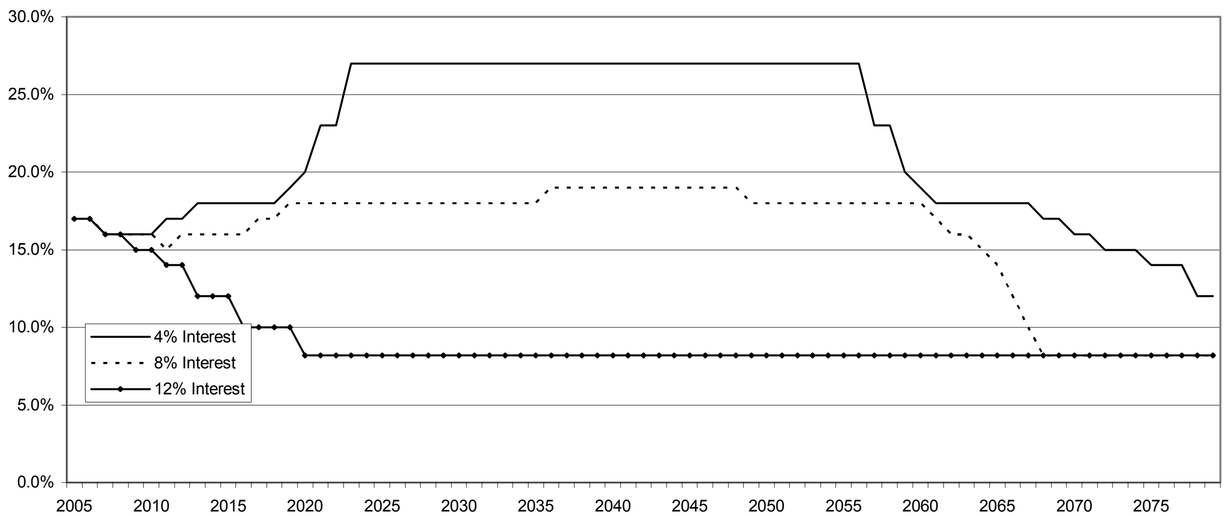


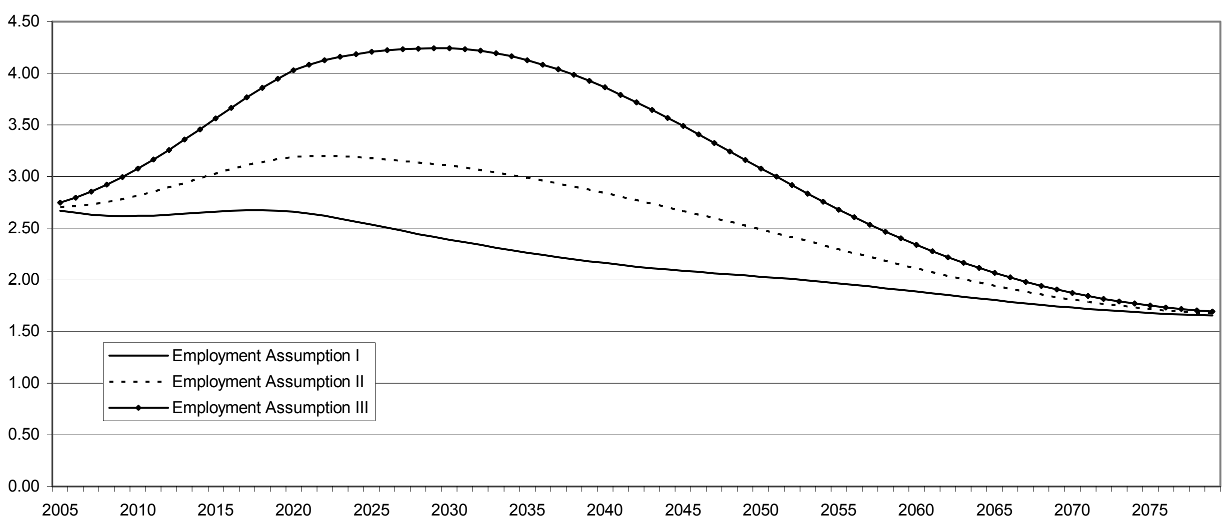
Chart 4b shows the tier 2 tax rate under the same three interest assumptions. With a 4 percent interest rate, the maximum tier 2 tax rate applies throughout much of the projection period, from 2023 until 2056. With the 8 percent interest rate, the maximum tax rate will never be paid, and the minimum tax rate is paid starting in 2068. With a 12 percent interest rate, the maximum tax rate is never applicable, and the minimum tax rate is paid beginning in 2020. As mentioned above, the tier 2 tax rate is determined based on the ratios of asset values to benefits and administrative expenses, so it will be affected by investment return, but tier 1 tax rates will not.

Chart 4b: Tier 2 Tax Rate under Three Interest Assumptions



Ratio of Beneficiaries to Workers: Chart 5 shows the estimated number of annuitants per full-time employee under all three employment assumptions. The average number of annuitants per employee for employment assumption I is highest in 2017. For assumptions II and III, the ratio is highest in 2022 and 2029, respectively. For all three employment assumptions, the average number of annuitants per employee declines to around 1.7 by the end of the projection period. The convergence in number of annuitants per employee at the end of the projection period results primarily from level employment projected in the latter years under all three employment assumptions.

Chart 5: Average Number of Annuitants per Full-Time Employee



Railroad Retirement Assumptions

The estimates used in this presentation are based on the assumption that the program will continue as presently constructed. They are also based on various economic, employment, and other actuarial assumptions. The employment assumptions were described above. The ultimate economic assumptions are an 8 percent interest rate, a 3 percent annual increase in the cost of living, and a 4 percent annual wage increase. Actuarial assumptions are those published in the “Twenty-Second Actuarial Valuation of the Assets and Liabilities Under the Railroad Retirement Acts as of December 31, 2001 with Technical Supplement,” as updated in the 2005 Section 502 Report. The Section 502 Report is an annual report on the actuarial status of the railroad retirement system required by law.

REQUIRED SUPPLEMENTARY INFORMATION
RAILROAD RETIREMENT BOARD
INTRAGOVERNMENTAL ACTIVITY AND BALANCES
FISCAL YEAR 2005

ASSETS:

Trading Partner	Fund balance with Treasury	Investments	Accounts Receivable	Total
Treasury (20)	$74,888,380	$1,265,204,565	$0	$1,340,092,945
Treasury (99)	0	0	0	0
SSA (28)	0	0	3,641,481,458	3,641,481,458
DOL (16)	0	0	94,820,436	94,820,436
Total	$74,888,380	$1,265,204,565	$3,736,301,894	$5,076,394,839

LIABILITIES:

Trading Partner	Accounts Payable	Debt	Other	Total
Treasury (20)	$73,000	$3,041,835,141	$0	$3,041,908,141
Treasury (99)	0	0	119,638	119,638
CMS (75)	453,700,000	0	0	453,700,000
DOL (16)	0	0	336,911	336,911
SSA (28)	0	0	0	0
OPM (24)	0	0	456,244	456,244
GSA (47)	77,000	0	0	77,000
Total	$453,850,000	$3,041,835,141	$912,793	$3,496,597,934

BUDGETARY FINANCING SOURCES - UNEXPENDED APPROPRIATIONS

Trading Partner	Appropriations Received	Total
Treasury (99)	$550,150,000	$550,150,000

BUDGETARY FINANCING SOURCES - CUMULATIVE RESULTS OF OPERATIONS (NOTE 1):

Trading Partner	Appropriations Used	Non-Exchange Revenue (Note 2) Payroll Taxes	Interest	Gain(Loss) on Disposition of Assets	Total
Treasury (20)	$0	$0	$49,599,660	$0	$49,599,660
Treasury (99)	548,394,259	4,535,375,128	0	0	5,083,769,387
Total	$548,394,259	$4,535,375,128	$49,599,660	$0	$5,133,369,047

OTHER FINANCING SOURCES (NOTE 3):

Trading Partner	Transfers In/Out Without Reimbursement (Note 4)	Imputed Financing Costs	Total
DOL (16)	$97,161,821	$0	$97,161,821
OPM (24)	0	8,618,630	8,618,630
SSA (28)	3,846,254,000	0	3,846,254,000
CMS (75)	(477,392,000)	0	(477,392,000)
Total	$3,466,023,821	$8,618,630	$3,474,642,451

PROGRAM COSTS:

Trading Partner	Interest	Salaries and Expenses	Imputed Cost	Reimbursements	Total
Treasury (20)	$163,758,380	$1,414,599	$0	$0	$165,172,979
Treasury (99)	0	3,881,684	0	0	3,881,684
DOC(13)	0	390	0	0	390
DOI(14)	0	831	0	0	831
DOJ (15)	0	0	0	0	0
DOL (16)	0	181,830	0	0	181,830
VA(36)	0	13,311	0	0	13,311
CMS (75)	0	27,295	0	(7,245,977)	(7,218,682)
OPM (24)	0	12,068,984	8,618,630	0	20,687,614
SSA (28)	0	4,404	0	0	4,404
USPS (18)	0	318,166	0	0	318,166
LOC(03)	0	(434)	0	0	(434)
GPO (04)	0	206,287	0	0	206,287
DOD(00)	0	4,269	0	0	4,269
HS (70)	0	380,511	0	0	380,511
SBA (73)	0	0	0	0	0
GSA (47)	0	4,813,397	0	0	4,813,397
NARA (88)	0	363,297	0	0	363,297
Total	$163,758,380	$23,678,821	$8,618,630	($7,245,977)	$188,809,854

EARNED REVENUES NOT ATTRIBUTED TO PROGRAM:

Trading Partner	Other Revenue	Total
DOL (16)	$0	$0
NMB (95)	34,780	34,780
Total	$34,780	$34,780

Note 1: Amount does not include the transfers in from the NRRIT for $809,000,000.
Note 2: Amounts do not include other non-exchange revenue items: -$11,000,000 for additional contingent liability recorded, carriers' refunds of -$12,587, other revenue of $63,684 and interest of $43,327.
Note 3: Amount does not include Non-Federal adjustment of $100,000,000 for military service.
Note 4: Amount does not include Non-Federal adjustments of -$100,000,000 for military service and -$12,575.

RAILROAD RETIREMENT BOARD
DISAGGREGATE OF BUDGETARY RESOURCES
FOR THE FISCAL YEAR ENDED SEPTEMBER 30, 2005

Budgetary Resources:	**COMBINED RAILROAD RETIREMENT PROGRAM**	**COMBINED RAILROAD UNEMPLOYMENT AND SICKNESS INSURANCE PROGRAM**	**LIMITATION ON THE OFFICE OF INSPECTOR GENERAL**	**COMBINED TOTALS**	**INTER-FUND ELIMINATIONS**	**CONSOLIDATED TOTALS**
Appropriations Received	$10,362,914,118	$110,167,720	$0	$10,473,081,838	($442,000,000)	$10,031,081,838
Net Transfers	9,227,225	(16,345,038)	7,060,249	(57,564)	0	(57,564)
Other	(0)	0	0	(0)	0	(0)
Unobligated Balance, Beginning of Period	15,213,876	0	208,620	15,422,496	0	15,422,496
Net Transfers, actual	0	0	0	0	0	0
Spending Authority From Offsetting Collections						
Earned	8,577,149	29,699,067	0	38,276,216	(506,224)	37,769,992
Anticipated for Rest of Year, Without Advances	(0)	0	0	(0)	0	(0)
Recoveries of Prior Year Obligations	1,285,175	0	118,261	1,403,436	0	1,403,436
Temporarily Not Available Pursuant to Public Law	(466,512,998)	(22,125,164)	0	(488,638,162)	0	(488,638,162)
Permanently Not Available	(2,762,264)	0	0	(2,762,264)	0	(2,762,264)
Total Budgetary Resources	**$9,927,942,281**	**$101,396,585**	**$7,387,130**	**$10,036,725,996**	**($442,506,224)**	**$9,594,219,772**
Status of Budgetary Resources:						
Obligations Incurred	$9,912,940,560	$101,396,585	$7,181,265	$10,021,518,410	($442,506,224)	$9,579,012,186
Unobligated Balance	1,128,765	(0)	29,873	1,158,638	0	1,158,638
Unobligated Balance Not Available	13,872,956	(0)	175,992	14,048,948	0	14,048,948
Total Status of Budgetary Resources	**$9,927,942,281**	**$101,396,585**	**$7,387,130**	**$10,036,725,996**	**($442,506,224)**	**$9,594,219,772**
Relationship of Obligations to Outlays:						
Obligated Balance, Net, Beginning of Period:	**$821,724,899**	**$4,214,058**	**$340,464**	**$826,279,421**	**$0**	**$826,279,421**
Obligated Balance, Net, End of Period:						
Accounts Receivable	(96,809)	0	0	(96,809)	0	(96,809)
Undelivered Orders	(7,316,392)	0	(404,818)	(7,721,210)	0	(7,721,210)
Accounts Payable	(838,042,170)	(3,449,556)	(327,317)	(841,819,043)	0	(841,819,043)
Outlays:						
Disbursements	$9,887,925,600	$102,161,087	$6,671,333	$9,996,758,020	($442,506,224)	$9,554,251,796
Collections	(8,577,836)	(29,699,067)	0	(38,276,903)	506,224	(37,770,679)
Subtotal	9,879,347,764	72,462,020	6,671,333	9,958,481,117	(442,000,000)	9,516,481,117
Less: Offsetting Receipts	**3,810,862,000**	**0**	**0**	**3,810,862,000**	**0**	**3,810,862,000**
Net Outlays	**$6,068,485,764**	**$72,462,020**	**$6,671,333**	**$6,147,619,117**	**($442,000,000)**	**$5,705,619,117**

To the Board Members:

The following report presents the results of the Office of Inspector General's (OIG) audits of the financial statements of the Railroad Retirement Board (RRB) as of and for the fiscal years ending September 30, 2005 and 2004.

OPINION ON THE FINANCIAL STATEMENTS

The RRB's financial statements, including the accompanying notes, present fairly, in all material respects, in conformity with U.S. generally accepted accounting principles, the financial position of the RRB, its consolidated net cost of operations and changes in net position, combined budgetary resources, and reconciliation of net cost to budgetary resources as of and for the fiscal years ending September 30, 2005 and 2004.

Emphasis of Matters

The Railroad Retirement and Survivors' Improvement Act of 2001 established the National Railroad Retirement Investment Trust (NRRIT) and provided for the transfer of funds in excess of benefit payment requirements to the NRRIT for investment. Neither the assets held by the NRRIT, nor any related income, are reported in the RRB's consolidated financial statements although they are included in the estimates and projections presented in the statement of social insurance, and related disclosures, for the Railroad Retirement Act program and discussed elsewhere in the Performance and Accountability Report. Funds returned to the RRB for the payment of benefits are reported as transfers-in on the agency's statement of changes in net position.

Transfers-in from the Social Security Administration's Old-Age and Survivors Insurance and Disability Insurance trust funds and transfers-out to the Federal Health Insurance trust fund represented $3.4 billion (net), or approximately 40%, of the nearly $8.5 billion in total financing sources reported on the statement of changes in net position, excluding transfers-in/transfers-out to the NRRIT.

REPORT ON INTERNAL CONTROL

Our evaluation of internal controls disclosed three material weaknesses and two reportable conditions.[1] The details of our findings follow. However, the objective of our audit was not to provide an opinion on internal control. Accordingly, we do not express such an opinion.

Although not considered to be material weaknesses or reportable conditions, we have reported other matters involving internal control and its operation to RRB management in a separate letter dated October 27, 2005.

Material Weaknesses

Information Security

During FY 2005, the OIG evaluated information security pursuant to the provisions of the Federal Information Security Management Act.[2] Our review disclosed continued weaknesses in many areas of the RRB's information security program. Significant deficiencies in program management and access controls make the agency's information security program a source of material weakness in internal control.

The RRB has undertaken the job of strengthening information security and has implemented many corrective actions recommended by the OIG and other technical specialists. However, the agency has not completed the corrective action needed to eliminate the previously reported deficiencies in training and access controls that were the basis for the OIG's original finding of material weakness. In FY 2005, we reported that the RRB is experiencing difficulty in achieving an effective, FISMA compliant security program and reported two new significant deficiencies resulting from delays in meeting FISMA requirements for risk assessments and periodic testing and evaluation.

Performance Measures

During FY 2005, the OIG performed detailed tests of two performance indicators. Audit tests disclosed that the RRB had materially overstated its performance with respect to timeliness because claims had been incorrectly classified and system

---

[1] A material weakness is a reportable condition that precludes the entity's internal controls from providing reasonable assurance that material misstatements in the financial statements, required supplementary information, or performance measures would be prevented or detected on a timely basis. Reportable conditions are matters coming to our attention that, in our judgment, should be communicated because they represent significant deficiencies in the design or operation of internal control that could adversely affect the RRB's ability to meet the objectives described in this report.

[2] "Fiscal Year 2005 Evaluation of Information Security at the Railroad Retirement Board," OIG Report #05-11, September 28, 2005

generated data did not include all processing time.[3] As a result, the agency has withdrawn prior-year performance information for those two indicators and qualified its presentation of current-year performance.

Although agency managers have implemented an attestation process to strengthen accountability for performance data, that process does not require that data be reviewed and validated. Inaccuracies in other performance indicators may have occurred and not been detected or disclosed to users of the information.

Actuarial Projection Process

The RRB needs to strengthen controls over the actuarial projection process that supports the projections and estimates presented in the statement of social insurance and related disclosures which are published with the agency's financial statements as required supplementary stewardship information.

During FY 2005, the OIG performed a detailed evaluation of controls over the actuarial projection process that disclosed inadequacies in internal control over the projections and related reports.[4] Although responsible management and staff have described extensive controls over the preparation of projections, estimates and reports, they have not formalized their policies and procedures, do not capture evidence of the operation of controls and do not perform periodic evaluations of compliance with internal requirements.

Reportable Conditions

Prompt Payment Act

During FY 2005, the OIG performed a detailed evaluation of controls over compliance with the Prompt Payment Act and concluded that existing systems and procedures had not been effective in ensuring that interest is paid to vendors in accordance with the requirements.[5] The RRB does not identify all invoices on which interest should be paid and does not pay the correct amount of interest when a late payment is recognized. In addition, controls are not adequate to ensure that required restrictions on early payment have been properly implemented.

---

[3] "Review of Customer Service Performance Measures For Timeliness of Initial Railroad Retirement Annuity Payments," OIG Report #05-05, May 17, 2005

[4] "Review of Internal Control Over the Actuarial Projection Process," OIG Report #05-04, May 5, 2005

[5] Review of Compliance with the Prompt Payment Act," OIG Report #05-06, June 15, 2005

Accounting for Leases

The RRB does not have adequate controls to ensure that leases are properly classified, justified and reported. Existing procedures do not include formal evaluation and documentation of pre-contract review to identify capital leases and ensure their proper recording and reporting. As a result, capital leases may not be treated in compliance with established requirements for budgetary and proprietary accounting.

COMPLIANCE WITH LAWS AND REGULATIONS

Our tests of compliance with selected provisions of laws and regulations disclosed two instances of non-compliance that are reportable under U.S. generally accepted government auditing standards or Office of Management and Budget (OMB) guidance as described below.

The RRB has not implemented provisions of the Railroad Retirement and Survivors Improvement Act of 2001 that require railroad retirement benefits be disbursed by a qualified non-governmental financial institution, rather than the U.S. Department of the Treasury. The agency was prohibited from using funds appropriated under the Consolidated Appropriations Act of 2005 to implement this provision; agency management is currently seeking legislative relief from this requirement.

The RRB has not fully complied with the Prompt Payment Act. The systems and procedures that the agency uses to implement the Act have not been effective in ensuring that interest is paid to vendors in accordance with the requirements. The RRB does not identify all invoices on which interest should be paid and does not pay the correct amount of interest when a late payment is recognized. In addition, controls are not adequate to ensure that required restrictions on early payment have been properly implemented.

The results of our tests of compliance disclosed no other instances of noncompliance with laws and regulations that are required to be reported under government auditing standards or OMB guidance. However, the objective of our audit was not to provide an opinion on overall compliance with laws and regulations. Accordingly, we do not express such an opinion.

Consistency of Other Information

The RRB's Management's Discussion and Analysis, required supplementary information, required supplementary stewardship information, and other accompanying information contain a wide range of data, some of which are not directly related to the financial statements. We did not audit and do not express an opinion on this information. However, we compared this information for consistency with the financial statements and discussed the methods of measurement and presentation with RRB officials. Based on this limited work, we found no material inconsistencies with the financial statements or nonconformance with OMB guidance except for two matters discussed earlier in our report: (1) the weakness in internal control over performance measurement that limits the reliability of the agency's reporting under the GPRA and (2) the inclusion of program assets held by the NRRIT in the actuarial projections and estimates that comprise the required supplementary stewardship data.

OBJECTIVES, SCOPE, AND METHODOLOGY

RRB management is responsible for (1) preparing the annual financial statements in conformity with U.S. generally accepted accounting principles, (2) establishing, maintaining, and assessing internal control to provide reasonable assurance that the broad control objectives of the Federal Managers' Financial Integrity Act (FMFIA) are met, and (3) complying with applicable laws and regulations.

We are responsible for obtaining reasonable assurance about whether (1) the financial statements are presented fairly, in all material respects, in conformity with U.S. generally accepted accounting principles and (2) management maintained effective internal control that provides reasonable, but not absolute, assurance that the following objectives were met.

- Financial reporting: transactions are properly recorded, processed and summarized to permit the preparation of financial statements in conformity with U.S. generally accepted accounting principles and assets are safeguarded against loss from unauthorized acquisition, use or disposition.

- Compliance with laws and regulations: transactions are executed in accordance with laws governing the use of budget authority and with other laws and regulations that could have a direct and material effect on the financial statements and any other laws, regulations, and governmentwide policies identified by OMB audit guidance.

We are also responsible for (1) testing compliance with selected provisions of laws and regulations that have a direct and material effect on the financial statements and laws for which OMB audit guidance requires testing, and (2) performing limited procedures with respect to certain other information appearing in these annual financial statements. In order to fulfill these responsibilities, we:

- examined, on a test basis, evidence supporting the amounts and disclosures in the financial statements;

- assessed the accounting principles used and significant estimates made by management;
- evaluated the overall presentation of the financial statements;
- obtained an understanding of internal controls related to financial reporting and compliance with laws and regulations;
- obtained an understanding of the recording, processing, and summarizing of performance measures as reported in Management's Discussion and Analysis;
- tested relevant internal controls over financial reporting and compliance, and evaluated the design and operating effectiveness of internal controls;
- considered the process for evaluating internal controls and financial management systems under the FMFIA;
- tested compliance with selected provisions of the following laws and regulations:
    - Anti-Deficiency Act, as amended;
    - Prompt Payment Act;
    - Pay and Allowance System for Civilian Employees;
    - Provisions Governing Claims of the United States Government, including provisions of the Debt Collection Improvement Act;
    - laws providing for the appropriation of funds for the administration of the programs mandated by the Railroad Retirement and the Railroad Unemployment Insurance Acts, including the payment of benefits; and
    - Railroad Retirement and Railroad Unemployment Insurance Acts.

We did not evaluate all internal controls relevant to operating objectives as broadly defined by FMFIA, such as controls relevant to preparing statistical reports and ensuring efficient operations. We limited our internal control testing to controls over financial reporting and compliance. Because of inherent limitations in internal control, misstatements due to error or fraud, losses, or noncompliance may nevertheless occur and not be detected. We also caution that projecting our evaluation to future periods is subject to the risk that controls may become inadequate because of changes in conditions or that the degree of compliance with controls may deteriorate.

We did not test compliance with all laws and regulations applicable to the RRB. We limited our tests of compliance to those laws and regulations that had a direct and material effect on the RRB's financial statements or that were required to be tested by OMB audit guidance that we deemed applicable to the financial statements for the fiscal years ended September 30, 2005, and 2004. We caution that noncompliance may occur and not be detected by these tests and that such testing may not be sufficient for other purposes.

We performed our work in accordance with U.S. generally accepted government auditing standards and OMB audit guidance.

RRB Management's Comments

The Chief Financial Officer and the Board Members have reviewed the draft report. In their reply, they thank OIG management and staff for working closely and cooperatively with agency personnel to ensure that the agency would be able to meet the November 15th reporting deadline.

Management did not comment directly on the three material weaknesses reported by the OIG noting that their comments on these issues were included in their published response to the OIG's management challenges. In response to the reportable conditions cited in the report, management states that they are taking corrective action to ensure compliance with the Prompt Payment Act and will be reviewing leases to ensure that they have been properly recorded and reported.

The full text of management's response follows as an attachment to this report.

Martin Dickman

Martin J. Dickman
Inspector General

October 27, 2005

UNITED STATES GOVERNMENT

FORM G-115f (1-92)

RAILROAD RETIREMENT BOARD

MEMORANDUM

NOV 0 8 2005

TO : Henrietta B. Shaw
Assistant Inspector General for Audit

FROM : Kenneth P. Boehne
Chief Financial Officer

SUBJECT: FY 2005 Financial Statement Audit, Auditor's Report;
Re: Your memorandum dated November 2, 2005

This memorandum is in response to your request for comments on your draft report regarding your audit of the agency's FY 2005 Financial Statements.

My office, and those of the Board Members, have reviewed your draft audit report and have the following comments. You reported material weaknesses in the Railroad Retirement Board's (RRB) information security program, performance measurement program and the actuarial projection process. Our comments on these three areas of concern are included in this Performance and Accountability Report as part of our response to your report on the serious management challenges you believe face the RRB. Regarding other matters presented in your draft audit report, we are taking corrective action to ensure compliance with the Prompt Payment Act, and will be reviewing leases to ensure that they have been properly recorded and reported on. We again thank you and your staff for working closely and cooperatively with us these past few months to ensure that the RRB was able to meet this year's reporting deadline of November 15.

cc: The Board
Executive Committee

OTHER ACCOMPANYING INFORMATION

PAGE INTENTIONALLY LEFT BLANK

SERIOUS MANAGEMENT CHALLENGES IDENTIFIED BY THE RAILROAD RETIREMENT BOARD'S OFFICE OF INSPECTOR GENERAL

The Office of Inspector General (OIG) is monitoring agency performance in addressing the most serious challenges facing the agency.

- Internal Control
- Statement of Social Insurance
- Financial Reporting Entity
- Performance Measures
- Improper Payments
- Information Technology Security

Internal Control

Effective in FY 2006, the Office of Management and Budget's (OMB) revised Circular A-123, "Management's Responsibility for Internal Control" emphasizes management's responsibility for assessing and documenting internal control over financial reporting. The Circular also emphasizes the need for integrated and coordinated internal control assessments that synchronize all internal control-related activities including those related to information technology and the reduction of improper payments.

The OIG has long questioned the effectiveness of the Railroad Retirement Board's (RRB) *overall control environment.* The control environment is the organizational structure and culture created by management and employees to sustain organizational support for effective internal control. We believe that the agency's basic structure, a three-member Board, rather than a single chief executive, cannot provide the kind of proactive top-down leadership that the Railroad Retirement Act (RRA) and Railroad Unemployment Insurance Act (RUIA) programs require to meet the challenges of the coming years.

We have repeatedly questioned the efficiency of an organizational structure, which, no matter how it has been organized and re-organized over the years, fosters an emphasis on the issues and objectives of its various operating units at the expense of larger organizational goals.

The agency has implemented a management control review process to support its responsibilities under the Federal Manager's Financial Improvement Act (FMFIA); however, OIG evaluations performed during FY 2005 found that the process had been unsuccessful in identifying weaknesses and that efforts to integrate information security responsibilities into the process were not fully successful.

In general, managers at the program-level respond positively to OIG recommendations for strengthened controls; however, the three-member Board does not agree with OIG observations about the overall control environment.

Statement of Social Insurance

The RRB's FY 2006 basic financial statements must include, for the first time, a statement of social insurance. Unique to the four Federal reporting entities with responsibility for social insurance programs, statements of social insurance have never been included in the auditor's opinion although the statement has been required supplementary information since FY 2000.

The OIG's FY 2005 assessment of controls over the actuarial projection process that serves as the basis for the statement of social insurance indicates that much remains to be done to ensure an auditable statement of social insurance. Our review disclosed that the agency had not implemented a comprehensive system of internal control for actuarial services, and that its management control review program was not effective in disclosing the system's deficiencies.

Uncorrected weaknesses in internal control could adversely impact the auditor's opinion on the FY 2006 statement of social insurance. Responsible management has agreed to review its control program and make changes if needed with a target completion date of July 2006.

Financial Reporting Entity

The amendments to the Railroad Retirement Survivors' Improvement Act of 2001 resulted in the transfer of the majority of the program's assets to the National Railroad Retirement Investment Trust (NRRIT). These amendments to the Railroad Retirement Act charged the NRRIT with responsibility for investing program assets. The NRRIT has never been included in the RRB's consolidated reporting entity because agency management believed that its status as a non-governmental entity precluded such treatment.

During FY 2004 the OIG urged agency management to resolve financial reporting issues resulting from the creation of the NRRIT as a non-governmental entity. The OIG observed that recently adopted Federal financial reporting requirements related to social insurance and earmarked funds would create unacceptable inconsistencies in the RRB's financial reports if the NRRIT continues to be excluded from the agency's consolidated reporting entity.

In FY 2005, OMB directed the RRB to take action to include the NRRIT in its audited financial reports; discussions among agency, NRRIT and OIG management are ongoing.

Performance Measures

The RRB needs to be proactive in ensuring the credibility of its performance measures as these indicators take on increased significance with OMB's implementation of performance budgeting effective for FY 2005. Performance measurement was mandated by the Government Performance and Results Act (GPRA) of 1993 and the required reports are currently published in the agency's performance and accountability report.

An FY 2005 OIG audit identified weaknesses in the RRB's measurement of selected indicators of application processing timeliness. Program managers generally concurred with OIG recommendations for corrective action and have consulted with OIG staff about the impact of the audit findings on GPRA reporting for the current year.

Improper Payments

As an agency responsible for two social insurance programs, the RRB is continually challenged to reduce improper payments in its programs. Improper payments are payments that should not have been made or were made for incorrect amounts. The risk of improper payments tends to be high in programs such as those administered by the RRB because of the volume of transactions, complex benefit payment criteria and the number of external factors that may impact continuing entitlement.

The Improper Payments Information Act (IPIA) of 2002 has had little real impact at the Railroad Retirement Board (RRB) other than to mandate annual reporting. In FY 2005, the RRB's general counsel advised program managers that RRB is not subject to requirements for statistical estimates or remediation plans that the IPIA imposes on risk susceptible programs. Estimates of improper payments in the agency's benefit programs do not exceed thresholds established by OMB to identify programs subject to those requirements.

Agency efforts to reduce improper payments in its programs include a variety of program integrity initiatives such as data matching to identify beneficiary deaths and unreported post-retirement earnings in addition to quality assurance reviews of adjudicative accuracy. The OIG supports agency efforts in this area with reviews of various aspects of benefit payment operations such as receivable identification, program integrity efforts and quality assurance programs as well as investigations of beneficiary fraud. In FY 2005 the OIG reported on weaknesses in the agency's handling of the post-retirement earnings in disability and survivor annuitants.

Information Technology Security

Information security remains an area of material weakness for the RRB.

The agency is experiencing difficulty in achieving an effective, FISMA compliant security program. Previously cited significant deficiencies in access controls and training persist. In addition, the OIG's FY 2005 evaluation of information security disclosed two new significant deficiencies due to delays in meeting FISMA requirements for risk assessments and periodic testing and evaluation.

We have also identified reportable conditions that require management action to ensure a fully effective, FISMA compliant security program. We observed such weaknesses in the agency's implementation of requirements for risk based policies and procedures, a remedial action process, continuity of operations, and inventory of systems. We have also observed that the RRB's response to OMB and NIST requirements for certification and accreditation of information systems has been adversely impacted by the existence of deficiencies in the FISMA mandated security program.

In general, responsible agency management have agreed with OIG recommendations for corrective action but are experiencing difficulties in developing timeframes for implementation.

Martin J Dickman

Martin J. Dickman
Inspector General

October 6, 2005

Management's Comments

The Inspector General has presented six serious management challenges that he believes face the RRB. Comments of RRB management on each issue are set out below.

Internal Control

The OIG has repeatedly raised the issue of the agency's organizational structure as a serious management challenge. Specifically, it believes that a three-member Board "cannot provide the kind of proactive top-down leadership that the Railroad Retirement Act (RRA) and Railroad Unemployment Insurance Act (RUIA) programs require to meet the challenges of the coming years." The agency's basic structure, a three-member Board, is a statutorily mandated structure that has served its customers efficiently and effectively for about 70 years. The management structure is somewhat unique, in that one member of the Board represents rail management, and another represents rail labor, with the Chairman, as the third member, representing the general public. For a variety of reasons, the Congress statutorily mandated this arrangement, which mirrors the tradition that negotiations between rail labor and management determine the provisions of the RRA and RUIA benefit programs.

Day-to-day operations of the agency are overseen by a six-member Executive Committee comprised of senior executives who head the agency's major subordinate components. The performance plans of the members of the Executive Committee are tied directly to the goals of the agency as set forth in the Strategic Plan and Annual Performance Budget. The members work together closely to ensure that the agency goals are achieved. The Executive Committee reports directly to the three-member Board, and both groups share a commitment to providing the type of proactive, top-down leadership the OIG claims does not exist. That the structure works is evidenced by the strong performance reported by the agency over the last few years in the RRB's Performance and Accountability Report.

Statement of Social Insurance

Although our Chief Actuary agrees that the documentation of internal controls over the actuarial projection process has not been designed to facilitate an audit, he believes that the current system of internal controls is effective and efficient. The actuaries employed by the Railroad Retirement Board have obtained professional credentials from the Society of Actuaries and the American Academy of Actuaries and adhere to applicable professional guidelines issued by these organizations. Internal procedures, which we view as internal controls, are in place. For instance, when producing actuarial valuations, two qualified staff members, working independently, compare their results at every stage of the valuation process. Any differences are resolved before the next stage of the valuation continues. In addition, the review of the triennial actuarial valuations and actuarial experience studies conducted by the Actuarial Advisory Committee in accordance with Section 15(f) of the Railroad Retirement Act found that the actuarial assumptions are reasonable and that the valuation results present a fair picture of the financial condition of the railroad retirement system. Finally, in an independent review commissioned by the Office of Inspector General and issued in November 1997, Watson Wyatt Worldwide stated that the valuation was thorough and objective, the methodology was sound, and the assumptions were reasonable.

Financial Reporting Entity

The Railroad Retirement and Survivors' Improvement Act of 2001 provided for establishment of the National Railroad Retirement Investment Trust and required the Railroad Retirement Board to transfer assets in the Railroad Retirement Account and Social Security Equivalent Benefit Account, not needed to pay current benefits or administrative expenses, to the National Railroad Retirement Investment Trust for investment. The Trust is statutorily authorized to invest the assets transferred to them by the Railroad Retirement Board in the interest of the Railroad Retirement System and to transfer funds to the disbursement agent when such funds are needed to pay benefits. The statute states that the Trust is not a Federal entity and that it is not subject to title 31 of the United States Code. The statute also requires the Trust to engage an independent public accountant to audit the financial statements of the Trust and imposes a requirement that the Trust submit, no later than 180 days after the close of the Trust's fiscal year, an annual management report, including financial information, to the Congress, and concurrently provide copies to the President, the Railroad Retirement Board, and the Director of Management and Budget.

In the past, the RRB has not been required to report the assets of the NRRIT in its financial statements. The Board has, nevertheless, provided information on Trust assets in the narrative portion of the agency's Performance and Accountability Report.

The Railroad Retirement Board Inspector General has expressed the opinion that the new requirement that the Board's annual financial statements include a Statement of Social Insurance (SOSI) as part of the agency's basic financial statements requires that the Trust's financial information be consolidated with the Board's financial information in the Railroad Retirement Board's financial statements. The RRB OIG has taken the position that audited financial information from the Trust must be consolidated in the Railroad Retirement Board's financial statements in time to allow the OIG to audit the Board's consolidated financial statements. The Railroad Retirement Board requested guidance from the Federal Accounting Standards Advisory Board on this matter in 2004, but the issue has not yet been resolved. Moreover, the Trust has advised the Board that because of the complexity and size of the investment portfolio it manages, audited financial information cannot be provided to the Board in time to be included with the Board's financial information prior to submission of the financial statements for OIG review and audit, so it appears, in any case, that consolidation could not be accomplished within the required timeframes.

A meeting was held in October 2005 between the Railroad Retirement Board, the RRB Office of Inspector General, and the National Railroad Retirement Investment Trust and its custodian and auditor to discuss this matter and the Trust's year-end closing and audit process. The Railroad Retirement Board will soon be reporting the results of the meeting to the Office of Management and Budget.

Performance Measures

The Inspector General states that the RRB needs to be proactive in ensuring the credibility of its performance measures. A fiscal year 2005 OIG audit identified technical problems in the RRB's measurement of selected indicators of application processing timeliness. As the OIG indicated, we have agreed with OIG recommendations for corrective action and have made and continue to make system enhancements to ensure accurate measurement. We also plan to review all timeliness performance measures for possible inconsistencies in standards, measures and tracking and make any necessary adjustments or corrections.

Improper Payments

The stated purpose of the Improper Payments Information Act (IPIA) of 2002 is "To provide for estimates and reports of improper payments by Federal agencies." The RRB has complied with that purpose. In addition, we have made a concerted effort to ensure that our improper payment report meets both the spirit and the letter of the law and guidance in this area. This year, the RRB's General Counsel reviewed our interpretation of the guidance as well as the actual estimates developed for the reports. His input is reflected in our final report. We have also included estimates from several recent OIG audit reports and are developing plans for handling the workloads cited.

More importantly, we have made significant progress in resolving discrepancies in our service and compensation records which are the basis for calculating our benefit payments under the Railroad Retirement Act. In addition, development work continues on a program designed to adjust annuities for changes in service and compensation data that occur subsequent to the initial annuity award. Progress in these areas allowed us to reduce the estimated amount of improper payments that result from such discrepancies.

Therefore, we believe that the IPIA has had real impact at the RRB by ensuring continued high priority for those initiatives which are designed to reduce improper payments.

Information Technology Security

In fiscal year 2005, 41 employees with significant computer security responsibilities participated in web-based security training and the program will be expanded in 2006 to include all individuals with information technology security responsibility. Also, the agency has made important progress in improving the system access controls. To date, we have successfully resolved 21 audit recommendations and are working diligently to complete the remaining 4 recommendations. Moreover, the RRB has implemented a sophisticated Intrusion Detection System to monitor the RRB network for unauthorized access. To help support that program, we added an information assurance analyst to the staff of the Risk Management Group.

Recently, the OIG identified two new deficiencies in the areas of risk assessment and testing and evaluation, along with several reportable conditions. RRB is serious about information security and will take suitable measures to resolve identified weaknesses in the RRB information security program with priority being given to those designated as significant deficiencies and reportable conditions. Also, the agency plans to progressively implement a method that will provide the documentation necessary to properly certify and accredit its systems as provided for by guidance from the National Institute of Standards and Technology.

<u>Improper Payments Information Act (IPIA) Reporting Details</u>

I. Describe your agency's risk assessment(s), performed subsequent to compiling your full program inventory. List the risk-susceptible programs (i.e., programs that have a significant risk of improper payments based on OMB guidance thresholds) identified through your risk assessments. Be sure to include the programs previously identified in the former Section 57 of OMB Circular A-11.

The RRB's Office of Programs reviewed each of the two benefit payment programs our agency administers and calculated the amount of improper payments made in fiscal year 2004. These programs are listed in the former Section 57 of OMB Circular A-11: Retirement and Survivor Benefits (referred to as RRA) and Railroad Unemployment Insurance Benefits (referred to as RUIA).

II. Describe the statistical sampling process conducted to estimate the improper payment rate for each program identified.

The agency has established and documented a multi-faceted methodology for identifying improper payments in our RRA and RUIA benefit payment programs. It is based on determining the known overpayments, which have since been set up for recovery, estimating the underpayments which have since been paid out, and estimating those improper payments which result from adjudicative error, but have not been identified or corrected. It also uses information from our annual quality assurance reviews. These employ statistical sampling to study initial retirement awards, post adjudication actions, and unemployment and sickness insurance claims. We also include in our estimates the results of audits. Each year we work to refine our methodology to get more precise in estimating improper payments.

We believe this approach, although not based entirely on statistical sampling, is sufficient for determining our improper payment rates and for making the determination that the improper payments in our programs do not exceed the OMB thresholds.

The RRB's Office of General Counsel reviewed the approach and the fiscal year 2004 data used to develop this year's submission. Its review resulted in some minor reductions in several categories of estimated improper payments, but concluded that, overall, the approach used had merit. Furthermore, in May 2005, the RRB's General Counsel issued a legal opinion confirming that, since the levels of improper payments did not exceed the thresholds, the agency was not required to conduct the statistical sampling described in OMB guidance M-03-13.

III. Explain the corrective actions your agency plans to implement to reduce the estimated rate of improper payments. Include in this discussion what is seen as the cause(s) of errors and the corresponding steps necessary to prevent future occurrences. If efforts are already underway, and/or have been ongoing for some length of time, it is appropriate to include that information in this section.

Improper payments in the RRA and RUIA programs typically fall into two categories: *adjudicative error* (i.e., benefit payment decisions that are inconsistent with the law or regulations) and *out-of-date information* that impacts benefit entitlement.

To detect improper payments due to *adjudicative error*, we conduct our quality assurance programs which identify activities that are susceptible to error and implement process improvements to prevent further errors.

To detect improper payments due to *out-of-date information*, we conduct comprehensive program integrity efforts which aim to validate continued entitlement to our benefits.

To maintain our overall high levels of accuracy, we continue to improve our adjudication and payment systems and procedures to minimize errors. We are also pursuing some initiatives which will minimize specific types of improper payments in the RRA program:

- We made substantial progress on a multi-year effort to resolve earmarks on our earnings database which indicated inconsistencies in the reports sent by railroad employers. This resulted in the correction of a significant number of earnings records and a reduction in the estimated dollar amount of our improper payments.
- We are developing a system that will expand on our current process of evaluating adjustments, received from railroad employers, to our records on railroad employee service and compensation, and adjust annuities if needed. This initiative will identify specific RRA improper underpayments and allow us to pay additional benefits due.
- We are taking steps to reevaluate certain categories of disability payments to ensure the accuracy of our calculations. This often results in paying out additional benefits.
- We are implementing improvements in the processing of survivor benefits that will reduce the incidence of examiner errors.
- We are working on a special project to resolve unverified social security numbers (SSN) of railroad employees. This will ensure that the correct earnings are recorded to the correct SSN which serves as a basis of our calculation of benefits.
- We are developing ways to identify earnings of our auxiliary beneficiaries (spouses, children, and widow(er)s) when inconsistencies related to their SSN's on record do not allow us to match to the SSA earnings database.
- We are developing a system that will allow the RRB to process earnings adjustment cases more timely and efficiently. This will decrease the number of cases which are either underpaid or overpaid due to work with earnings over the exempt amount after retirement.

Furthermore, the agency maintains an effective internal control review process for all our benefit payment programs. Annual risk assessments are performed by responsible officials and weaknesses are identified and addressed promptly.

Additionally, during fiscal years 1998 through 2004, the OIG presented RRB management with 87 recommendations for process improvement and corrective action pertaining to improper payments. Agency management has implemented or plans to implement 81 of the 87 recommendations. We will continue to work with the OIG to address the issue of improper payments in our benefit programs.

IV. The table below is required for each reporting agency:

Improper Payment (IP) Reduction Outlook FY 2003 – FY 2008
($ in millions)

Program	FY 03 $ Outlays	FY 03 IP %	FY 03 IP $	FY 04 $ Outlays	FY 04 IP %	FY 04 IP $	FY 05 $ Outlays (estimated)	FY 05 IP %	FY 05 IP $
RRA	8,900.0	1.90	172.8	9,008.0	1.64	147.9	9,185.4	1.64	150.6
RUIA	132.2	2.50	3.3	123.3	2.11	2.6	110.8	2.11	2.3

Program	FY 06 $ Outlays (estimated)	FY 06 IP %	FY 06 IP $	FY 07 $ Outlays (estimated)	FY 07 IP %	FY 07 IP $	FY 08 $ Outlays (estimated)	FY 08 IP %	FY 08 IP $
RRA	9,476.4	1.64	155.4	9,809.8	1.64	160.9	10,080.8	1.64	165.3
RUIA	119.5	2.11	2.5	129.3	2.11	2.7	135.3	2.11	2.9

At the time we prepared this report, the latest available data was for fiscal year 2004. The fiscal year 2005 outlay estimate is based on the June 2005 mid-session budget review. RRA outlays include monies from the Social Security Equivalent Benefit, Railroad Retirement, and Dual Benefits Payments Accounts. RUIA outlays include monies allocated to both unemployment and sickness insurance benefits.

We do not have sufficient details to determine the impact of our system improvements on our improper payments rate in future years. Therefore, we have straight-lined our fiscal year 2004 improper payment rate to project improper payment dollar amounts for future years.

The estimated amounts of RRA improper payments changed from fiscal year 2003 and fiscal year 2004 as a result of the actions described in our response to question III above. The most significant change was due to the impact our correction of two backlogs of employee service and compensation records had on our estimates. After those corrections were completed, we re-estimated the amounts of underpayments due to our customers. Previous estimates were based on a small sample of those record corrections and were ultimately found to be vastly overstated. In addition, this year, two reviews conducted by the OIG caused us to recognize additional improper payments for certain categories of disability and spouse annuitants involving earnings after entitlement.

V. Discuss your agency's recovery auditing effort, if applicable, including the amount of recoveries expected, the actions taken to recover them, and the business process changes and internal controls instituted and/or strengthened to prevent further occurrences. (This reporting replaces the original legislative requirement for reporting not later than 12/31/04.)

This does not apply to our benefit programs.

VI. Describe the steps the agency has taken and plans to take (including time line) to ensure that agency managers (including the agency head) are held accountable for reducing and recovering improper payments.

Paying benefits accurately and timely, and providing prudent stewardship over our trust funds are our two strategic goals. Agency managers have links to those goals in their performance plans.

VII. A. Describe whether the agency has the information systems and other infrastructure it needs to reduce improper payments to the levels the agency has targeted.

B. If the agency does not have such systems and infrastructure, describe the resources the agency requested in its FY 2006 budget submission to Congress to obtain the necessary information systems and infrastructure.

The agency has an enterprise architecture to address, among other performance goals, the accuracy of benefit payments. Beginning at the end of fiscal year 2005, the agency is embarking on a major multi-year project to transition the agency's mainframe CA-IDMS/DC non-relational database management system to a current technology mainframe relational database management system, DB2/CICS.

Contractor services are to be used to fully convert the agency's IDMS database inventory to DB2. This initiative will contribute to the achievement of one element of our agency's target architecture and to meet the agency's performance goals, including accuracy of benefit payments and stewardship of our trust funds.

The database management system conversion was once a part of an Enterprise Architecture Capital Asset Plan for fiscal years 2005 through 2007. The original plan consisted of an infrastructure modernization initiative, development of a metadata repository, and expansion of our e-Government service delivery. For fiscal year 2006, we requested funding for the second year of an Enterprise Architecture Capital Asset Plan for fiscal years 2005 through 2007. No funds were received for the Enterprise Architecture Capital Asset Plan in either fiscal year 2005 or 2006, which made the agency redirect resources and refocus on accomplishing only one of the major initiatives.

VIII. A description of any statutory or regulatory barriers which may limit the agencies' corrective actions in reducing improper payments.

None have been identified.

IX. Additional comments, if any, on overall agency efforts, specific programs, best practices, or common challenges identified, as a result of IPIA implementation.

For the past several years, the agency's budget request has included a legislative proposal that would allow access to the Office of Child Support Enforcement's (OCSE) quarterly wage data (also known as the National New Hire Directory). According to its 2003 Performance and Accountability Report, SSA has used on-line access to this information to assist in detecting improper payments due to wages, and is exploring the usefulness of a quarterly match with the “new hires” OCSE file. We are no longer pursuing obtaining the National New Hire Directory because we have learned that the estimated cost is well beyond our limited administrative budget, even though it would most likely have been beneficial from a programmatic perspective.

The RRB has made concerted efforts to reduce improper payments over the years. Our payment accuracy rates are at consistently high levels and our return on investment for program integrity activities has been high as well. Both have been set as annual performance goals and reported on each year since the Government Performance and Results Act has been in effect. We monitor our progress on implementing recommendations from the quality assurance process, and we are vigilant about pursuing OIG recommendations which impact the quality and timeliness of payments. We have also worked closely with our OIG in referring potential fraud cases for investigation and prosecution. We hope to be able to maintain our staffing levels so that we can continue this important effort.