



SOCIAL SECURITY
Office of the Inspector General

May 7, 2010

The Honorable Charles E. Grassley
Ranking Member
Committee on Finance
United States Senate
Washington, D.C. 20510

Dear Senator Grassley:

In a July 21, 2009 letter, you requested that we conduct an audit of the Social Security Employees' Activities Association, Inc., (EAA) and its related organizational and financial entities. Specifically, you requested that the audit include a thorough, independent review of all EAA-related organizations that would examine current and past lines of business and revenues generated from all sources; a detailed background on EAA management, including terms of services and direct and indirect compensation received; and a review of possible conflicts of financial interest. As Social Security Administration (SSA) employees, Office of the Inspector General staff members are eligible to join the EAA. However, no individuals assigned to this audit team are EAA members. The team also included two auditors provided by the U.S. Postal Service's Office of Inspector General. The enclosed report presents the results of our review.

Thank you for bringing your concerns to my attention. My office is committed to combating fraud, waste, and abuse in SSA's operations and programs. This report includes the results of our audit of EAA and its related organizational and financial entities. To ensure SSA is aware of the information provided to your office, we are forwarding a copy of this report to the Agency.

If you have any questions concerning this matter, please call me or have your staff contact Misha Kelly, Congressional and Intra-Governmental Liaison, at (202) 358-6319.

Sincerely,

A handwritten signature in black ink, appearing to read "Patrick P. O'Carroll, Jr." with a stylized flourish at the end.

Patrick P. O'Carroll, Jr.
Inspector General

Enclosure
cc:
Michael J. Astrue

***CONGRESSIONAL RESPONSE
REPORT***

***The Social Security Employees'
Activities Association, Inc.***

A-06-10-11028



May 2010

Mission

By conducting independent and objective audits, evaluations and investigations, we inspire public confidence in the integrity and security of SSA's programs and operations and protect them against fraud, waste and abuse. We provide timely, useful and reliable information and advice to Administration officials, Congress and the public.

Authority

The Inspector General Act created independent audit and investigative units, called the Office of Inspector General (OIG). The mission of the OIG, as spelled out in the Act, is to:

- Conduct and supervise independent and objective audits and investigations relating to agency programs and operations.
- Promote economy, effectiveness, and efficiency within the agency.
- Prevent and detect fraud, waste, and abuse in agency programs and operations.
- Review and make recommendations regarding existing and proposed legislation and regulations relating to agency programs and operations.
- Keep the agency head and the Congress fully and currently informed of problems in agency programs and operations.

To ensure objectivity, the IG Act empowers the IG with:

- Independence to determine what reviews to perform.
- Access to all information necessary for the reviews.
- Authority to publish findings and recommendations based on the reviews.

Vision

We strive for continual improvement in SSA's programs, operations and management by proactively seeking new ways to prevent and deter fraud, waste and abuse. We commit to integrity and excellence by supporting an environment that provides a valuable public service while encouraging employee development and retention and fostering diversity and innovation.

Background

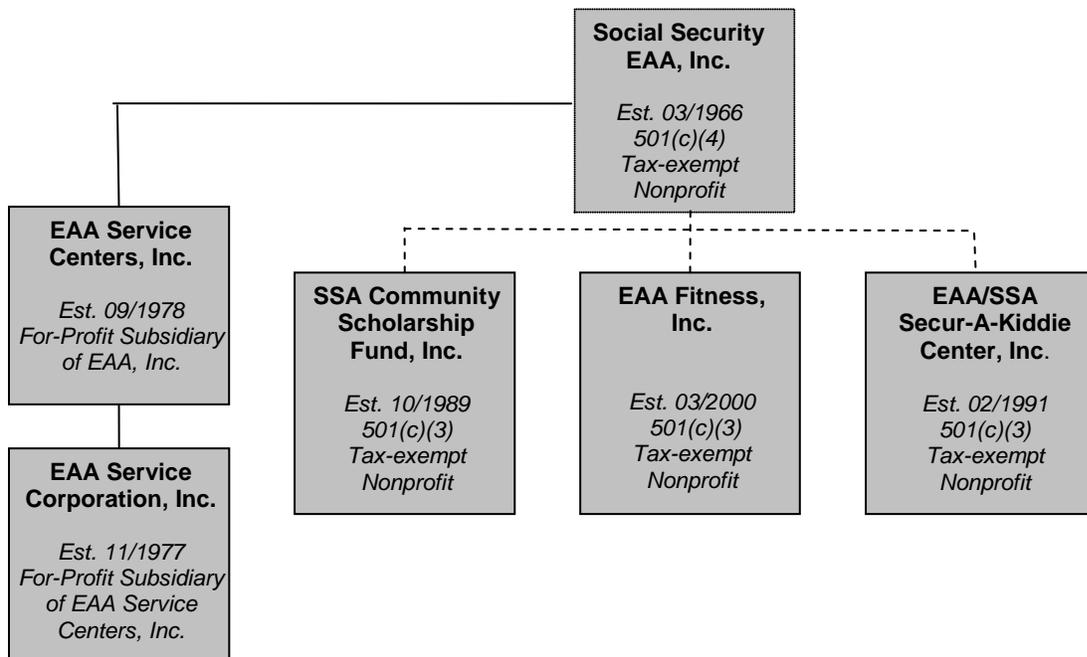
OBJECTIVE

Our objective was to respond to concerns raised by Senator Charles E. Grassley in his request for an audit of the Social Security Employees' Activities Association, Inc. (EAA). Specifically, we reviewed documentation supporting Fiscal Year (FY) 2006 through 2008 financial transactions reported on EAA and related entity financial statements; identified EAA's management structure and reviewed its compensation practices; and determined whether potential conflicts of financial interest existed.

BACKGROUND

EAA is a tax-exempt, nonprofit company established in 1966 under section 501(c)(4) of the Internal Revenue Code (IRC). According to EAA's Articles of Incorporation, on behalf of its members, the EAA provides social, recreational, cultural, welfare, health, and athletic activities. It also provides other facilities, benefits, and services for members as determined by its Board of Directors (Board).

Since its original incorporation in 1966, EAA management has created five additional corporations to carry out various Social Security Administration (SSA) employee-related activities. EAA's organizational structure is summarized in the following diagram.



- **EAA Service Centers, Inc. (Service Centers)** is a for-profit company incorporated in 1978 that provides various services to its customers, including postal and notary services, money orders, vendor shows, theme park tickets, and transit passes. Service Centers is a wholly owned subsidiary of EAA. Service Centers conducted vending operations on SSA's Woodlawn and Metro West campuses, and also conducted vending operations on the Centers for Medicare & Medicaid Services' (CMS) campus in Baltimore, Maryland. In December 2008, SSA's Office of General Counsel (OGC) issued a notice to EAA stating that Federal regulations specifically prohibited vending on Federal property except for commercial activities sponsored by recognized, nonprofit Federal employee associations. The notice stated that EAA's for-profit corporations were not legally permitted to sponsor or engage in vending activities on Federal property and instructed EAA to terminate its vending activities on SSA property effective January 16, 2009. Service Centers currently conducts its SSA vending activities online and in commercial space across the street from the Woodlawn campus. At the time of the audit, Service Centers continued to conduct vending operations on the CMS campus.
- **EAA Service Corporation, Inc. (Service Corp.)** is a for-profit company incorporated in 1977 that sells insurance products to EAA members. Service Corp. is a wholly owned subsidiary of the Service Centers.

EAA includes the activities of three additional nonprofit companies.

- **EAA/SSA Secur-A-Kiddie Center, Inc. (Secur-A-Kiddie Center)** is a nonprofit company established in 1991 and tax-exempt under 501(c)(3) of the IRC. Secur-A-Kiddie Center operated daycare services for SSA employees at SSA's Headquarters in Woodlawn, Maryland, and at SSA's Metro West facility in Baltimore, Maryland, until SSA issued a letter to terminate its agreement in August 2008.
- **EAA Fitness, Inc. (EAA Fitness)** is a nonprofit company established in 2000 and tax-exempt under 501(c)(3) of the IRC.¹ EAA Fitness operated fitness center facilities at SSA Headquarters and at the SSA Metro West facility until SSA terminated its agreement, effective March 2009. EAA Fitness also operated a fitness center on the CMS campus in Baltimore, Maryland, which was in operation at the time of this review.
- **The SSA Community Scholarship Fund, Inc. (Scholarship Fund)** is a nonprofit company established in 1989 and tax-exempt under 501(c)(3) of the IRC. The Scholarship Fund provides scholarships to SSA employees with funds donated by Combined Federal Campaign contributors.

EAA and its related entities are corporations that conduct business operations on SSA and CMS property and receive(d) indirect appropriated funding support in the form of facility use, equipment purchases (playground equipment, fitness equipment, etc.),

¹ On March 1, 2000, EAA Fitness amended its articles of incorporation to reflect a change in status from 501(c)(3) to 501(c)(4).

maintenance, and utilities. However, EAA and its related entities are supported primarily through revenues generated from the sale of goods and services to, or membership dues from, SSA and CMS employees.

EAA For-Profit Entities

In 1977, the Internal Revenue Service (IRS) informed EAA of its intent to revoke the corporation's tax-exempt status. According to copies of correspondence provided by EAA management, the IRS determined that EAA's sale of life insurance and merchandise at a discount to members was not a charitable purpose. As further justification for the revocation of EAA's tax-exempt status, the IRS stated that combining the accounting of the for-profit activities along with the tax-exempt functions performed by EAA could result in the use of tax-exempt income to subsidize non-tax-exempt activities.

During the following year, EAA created two for-profit corporations (Service Corp. and Service Centers) and transferred the merchandise vending and insurance business activities into these corporations. Based on this action, in March 1980, the IRS reversed its decision and reaffirmed EAA's tax-exempt status.

Agreements Between SSA and EAA

In 1977, SSA issued an Administrative Directive that established policies governing the relationship between SSA and employee activity associations, including EAA. The Directive outlined the conditions that employee activity associations must follow to maintain their identification with SSA. The Directive required that employee associations account for all funds used, maintain complete records of receipts and disbursements, and have its records audited annually. EAA's Constitution and By-Laws also state that all EAA books and records shall be available for audit and public inspection by SSA. Further, SSA and EAA separately negotiated Memorandums of Understanding (MOU) outlining specific responsibilities related to the operation of child care and fitness center activities. The MOUs authorized SSA to audit or inspect EAA records.

In 2005, OGC reviewed all MOUs between SSA and non-Federal entities. OGC determined that EAA violated the express terms of its MOUs with SSA by operating the fitness centers with its own employees and by not securing the services of a vendor. EAA initially contracted with a vendor to operate the fitness centers. However, in September 2000, EAA replaced the vendor and began operating the fitness centers with its own employees. OGC concluded this arrangement did not comply with Federal acquisition law. According to OGC, the services should have been made available for full and open competition. Even after OGC made this determination, SSA allowed EAA to continue operating the fitness center with its own employees for another 3 years.

In 2008, SSA terminated the MOUs allowing EAA to operate both fitness and child care facilities on SSA property in Baltimore, Maryland. Federal Occupational Health assumed management of SSA's fitness center operations and the newly formed child care board awarded a Texas-based company a contract to provide child care services.

Prior Audit Engagement

In July 2008, SSA contracted with a public accounting firm to audit EAA and its related organizations for the FYs ended September 30, 2006 and 2007. During the audit, EAA management and staff limited the auditors' access to EAA personnel and financial records. As a result of these restrictions, in December 2008, the SSA Contracting Officer directed the firm to stop work on the audit, effectively ending the contract. At the time, audits on four of the six EAA entities were in the planning phase, and the EAA Fitness audit was in the early phase of substantive testing. The firm's personnel informed us they completed substantive testing on their audit of the Secur-A-Kiddie Center. The auditors needed to meet with EAA management to discuss various issues/concerns identified during the engagement.

During our discussions with the Partner and Senior Manager assigned to the audit, the Senior Manager provided us examples of the unresolved issues and stated that the firm needed to get agreement from EAA management on the audit team's proposed adjustments. However, this meeting did not occur before the engagement was terminated. As a result, the firm did not issue an opinion on the related financial statements. Based on our meetings with the firm's personnel and review of the information they provided, we believe the unresolved issues did not materially affect information presented in the financial statements and would not have prevented the firm from issuing an unqualified opinion on Secur-A-Kiddie Center's FY 2006 and 2007 financial statements.

Results of Review

Balances reported on EAA and its five related entities' financial statements for FYs 2006 through 2008 were generally valid and supported. We identified various reporting or internal control-related issues that required attention, including inter-entity loans totaling \$390,240 that appeared unlikely to be repaid and could potentially jeopardize EAA's tax-exempt status. We also found EAA subjected itself to potential IRS tax liabilities and penalties because it classified a worker as an independent contractor without justification and subsequently failed to report the worker's compensation to the IRS.

An SSA general schedule employee's primary job duties consisted of managing the day-to-day operations of EAA and its related entities over the past couple decades. Specifically, the employee's official duties involved serving as president of EAA-related corporations that received Federal funds. This arrangement appeared to violate Federal conflict-of-interest law and regulations and occur with the approval of SSA management for more than 20 years. Also, between 1988 and 2000, SSA entered into formal agreements that allowed the Federal employee-owned and controlled organization to operate daycare and administer fitness center operations on SSA property. EAA did not comply with significant provisions of its agreements with SSA, and SSA did not enforce these provisions.

SSA has taken several significant actions that affect EAA operations. To prevent continued violation of Federal conflict-of-interest regulations, in Calendar Year 2008, SSA assigned the SSA employee duties unrelated to EAA activities. In addition, SSA hired a public accounting firm to audit EAA and its related entities' financial statements. SSA also terminated the MOU that allowed Secur-A-Kiddie Center to operate daycare centers on SSA Woodlawn and Metro West properties in Baltimore, Maryland, and replaced Secur-A-Kiddie Center as the daycare center provider. SSA's OGC also informed Service Centers it could no longer conduct vendor activities on SSA property, effective January 2009. In addition, SSA terminated the MOU that allowed EAA to manage fitness centers on SSA property and replaced EAA as the fitness center operator in March 2009.

EAA Financial Transactions

We reviewed selected financial statement balances reported on EAA and its five related entities' financial statements for FYs 2006 through 2008. Balances reviewed were generally valid and supported. However, we identified a number of financial reporting discrepancies that required attention, even though they were not material relative to the overall financial statements.

**Service Centers’
Other Assets**

The \$28,000 “Other Assets” amount reported on the Service Centers’ financial statements was overstated by \$18,000. The amount consisted of the recorded value of 16 permanent seat licenses (PSL)² EAA purchased from the Baltimore Ravens from 1998 to 2001. We contacted the Baltimore Ravens Ticket Office and verified that EAA paid \$10,000 for the PSLs. It appeared the balance reported on the financial statements erroneously included the value of 24 additional PSLs EAA purchased on behalf of EAA members, who repaid EAA for the cost of these purchases through installment payments or payroll deductions. As the balances were repaid, EAA transferred title of the PSLs to the EAA members, but it did not reduce the value of the assets reported on its accounting records.

For FYs 2006 through 2008, Service Centers spent \$44,212 to purchase Baltimore Ravens season tickets associated with the PSLs. Service Centers reported these purchases as “Administrative Expenses.” According to EAA management, EAA did not make these tickets available for sale to its membership. Instead, the tickets were given to EAA management, staff, or vendors or were donated to various charitable groups. EAA management maintained no records to account for how these tickets were distributed.

The value of the PSLs has increased significantly since their original purchase. The Baltimore Ravens created a *PSL & Wait List Marketplace Website* where PSL owners can attempt to purchase PSLs from the team by adding their name to a waiting list or list their PSLs for sale to the general public.³ According to the Website, the face value of comparable (same section, similar row) PSLs purchased from the team is \$26,000. Review of comparable PSLs that owners listed for sale as of January 2010 indicated the market value of EAA’s PSLs was approximately \$60,000.

Because of significant recent declines in EAA business activities, Service Centers did not have sufficient resources to continue purchasing the Baltimore Ravens tickets. According to EAA management, to prevent EAA from forfeiting the PSLs, the EAA president personally purchased all 16 Baltimore Ravens 2009-2010 season tickets. The president stated he continued to give the tickets to staff members as a work incentive, but he also planned to sell the individual game tickets to recover his purchase cost. We believe that allowing the EAA president to purchase the season tickets with personal funds to prevent forfeiture of the PSLs raises concerns about EAA’s continued ownership of these assets.

² PSLs give owners the exclusive right to purchase Baltimore Ravens season tickets at M&T Bank Stadium. To retain title to the PSLs, the owner must continue to purchase season tickets each year.

³ Baltimore Ravens PSLs are currently sold out. In the event PSL owners do not continue to purchase season tickets, the PSLs are forfeited to the Baltimore Ravens. The Baltimore Ravens then make the PSLs available for sale at predetermined face values.

Segregation of Duties

EAA could improve the segregation of duties as related to its accounting processes. Key duties and responsibilities should be divided or segregated among different people to reduce the risk of error or fraud. This should include separating the responsibilities for authorizing transactions, processing and recording transactions, reviewing transactions, and handling any related assets. No one individual should control all key aspects of a transaction or event.⁴ However, during our review, we found the EAA treasurer recorded all journal, cash disbursement, and general ledger entries, and performed bank reconciliations for nearly all EAA entities.

President's Expense

EAA and Service Centers reported a total of \$11,930 in "President's Expense" on their FY 2006 through 2008 financial statements.⁵ EAA did not have copies of actual source documents to support these expenditures. Instead, EAA provided an itemized list of the date, amount, payee, and purpose of each payment. The list indicated most transactions involved payments issued to the EAA president or to the issuer of the president's credit card⁶ as reimbursement for expenditures or donations made on EAA's behalf.

FISCAL YEAR 2006			
DATE	AMOUNT	PAYABLE TO	PURPOSE
10/25/05	\$150.00	[REDACTED]	Donation - Union Golf Tournament
03/16/06	\$350.00	Ravens Roast #73	Donation
06/16/06	\$200.00	[REDACTED]	Luncheon for EAA Employees
06/30/09	\$1,000.00	[REDACTED]	Donation to CFC
07/18/06	\$1,000.00	[REDACTED]	Past Presidents Dinner [REDACTED]
08/25/06	\$1,000.00	[REDACTED]	Past Presidents Dinner [REDACTED]
09/22/06	\$1,500.00	Chase Card Services	Pay charge card expenses
TOTAL	\$5,200.00		
FISCAL YEAR 2007			
10/31/06	\$1,000.00	Chase Card Services	Pay charge card expenses
11/22/06	\$500.00	Chase Card Services	Pay charge card expenses
03/05/07	\$1,500.00	[REDACTED]	Past Presidents Dinner [REDACTED]
03/05/07	\$1,500.00	[REDACTED]	Past Presidents Dinner [REDACTED]
07/13/07	\$250.00	[REDACTED]	Luncheon for EAA Employees
TOTAL	\$4,750.00		
FISCAL YEAR 2008			
12/11/08	(\$1,100.00)	EAA Service Center	Reimb for Past Presidents Dinner
12/11/07	\$3,350.00	Chase Credit Card	Payment - Past Presidents Dinner [REDACTED]
TOTAL	\$2,250.00		

The EAA president provided a copy of his November 2007 credit card statement to support a \$3,350 payment EAA issued to "Chase Credit Card" in December 2007. The credit card statement listed two purchases totaling \$3,350 from a restaurant in Annapolis, Maryland. Based on discussions with EAA management, the expenditures related to its "Past Presidents Dinner," an annual event held for EAA's Board, officers, and their spouses in honor of the service of past EAA presidents. We found nothing to

⁴ Government Accountability Office, *Standards for Internal Control in the Federal Government*, GAO/AIMD-00-21.3.1, page 14 (November 1999).

⁵ The itemized list shows \$12,200 in transactions. The list does not reflect a \$270 adjustment that reduced reported expenses to \$11,930.

⁶ The EAA president stated the credit card account was established in his name, but used only for EAA-related purchases.

indicate these transactions were illegal. However, to better document future transactions and avoid the appearance of impropriety, EAA should make purchases directly from vendors instead of reimbursing its officers.

Inter-Entity Loans

EAA and related entity FY 2008 financial statements disclosed the existence of three loans between EAA entities with unpaid balances totaling \$390,240. The loan balances are due on demand without interest. Current events raise serious concerns regarding the likelihood that these loans will be repaid. As of September 30, 2008:

- Service Centers owed EAA \$191,576 and EAA Fitness \$73,541. We question the practice of nonprofit, tax-exempt corporations issuing no-interest loans to a for-profit corporation and believe issuance of the loans could threaten EAA and EAA Fitness' tax-exempt status. A major reason the IRS nearly revoked EAA's tax-exempt status in the 1970s was the potential use of tax-exempt funds to subsidize non-tax-exempt activities. Issuance of these loans similarly created situations where EAA and EAA Fitness' tax-exempt funds subsidized the non-tax-exempt Service Centers' activities. In addition, effective January 2009, SSA no longer allowed Service Centers to conduct vending activities on Agency property. We believe this action impairs Service Centers' operations and its ability to repay the loans.
- Secur-A-Kiddie Center owed Service Centers \$125,123. According to EAA management, when SSA terminated EAA's daycare center operations in August 2008, Secur-A-Kiddie Center did not have sufficient cash on-hand to refund security deposits owed customers or pay the accrued leave balances owed its employees. To satisfy these obligations, EAA issued a loan to Secur-A-Kiddie Center. However, because Secur-A-Kiddie Center is no longer in operation, there is little likelihood this loan will ever be repaid.

EAA Organizational Structure and Compensation

Organizational Structure

EAA's governing body is its Board. The Board is responsible for electing EAA's officers, including the president, vice presidents, and treasurer. The president and vice presidents must be Board members, but the secretary and treasurer need not be Board members.

EAA Management Compensation

As part of this review, Senator Grassley requested we provide information on EAA management's direct and indirect compensation. EAA directors and officers were volunteers and therefore were not compensated for their services—with three exceptions. EAA directly compensated the treasurer and paid him \$50 per hour for services performed during the 3-year audit period. EAA reported the treasurer's payments on its financial statements and tax returns under "Accounting Expense." In addition, both the EAA president and the Service Corp. vice president received indirect compensation for their services. The president was a Federal employee whose salary and benefits were paid by SSA, even though his full-time duties consisted of managing EAA activities. The Service Corp. vice

president was an officer in an insurance agency that provided various insurance products EAA sold its members. While he was not directly compensated by EAA, the Service Corp vice president was compensated for his service through the insurance agency that employed him.

Wages and Salary Expense

EAA issued wage payments to its employees through a payroll servicing contractor. The contractor computed various tax and benefit withholdings and issued payments to EAA employees. The contractor also prepared and submitted quarterly tax reports and required payments to the IRS on EAA's behalf. At the end of the calendar year, the contractor prepared EAA employees' IRS Forms W-2, Wage and Tax Withholding. We determined that approximately \$2.6 million in wages reported on EAA, EAA Fitness, Service Centers, and Service Corp. FYs 2006 through 2008 financial statements was supported and reported to the IRS via Form W-2.

Unlike other compensated staff, EAA classified one worker as an "independent contractor" and did not withhold or pay income, Social Security, or Medicare taxes on a significant amount of compensation paid to the worker. The IRS requires that payments to independent contractors for services in excess of \$600 per year be reported on Form 1099-MISC, Miscellaneous Income (Form 1099).⁷ Independent contractors, in turn, are responsible for payment of any applicable income taxes, as well as both employer and employee shares of Social Security and Medicare taxes.

We requested EAA provide all Forms 1099 issued during the audit period. We reviewed available documents and found nothing to indicate that EAA reported the independent contractor's compensation to the IRS. EAA officials stated that EAA classified this worker as an independent contractor because the individual worked a part-time, irregular schedule. However, we believe EAA did not have sufficient basis for this classification. IRS guidance indicates that anyone who performs a service for you is your employee if you have the right to control what will be done and how it will be done. It does not matter whether the individual works full- or part-time.⁸ Further, EAA compensated this worker on an hourly basis. According to IRS guidance, paying a worker a regular wage amount for an hourly period of time usually indicates the worker is an employee (an independent contractor is usually paid a flat fee for the job).⁹

⁷ IRS 2008 *Instructions for Form 1099-MISC*.

⁸ IRS Publication 15-A, 2009 *Employers Supplemental Tax Guide*, page 4.

⁹ IRS Publication 15-A, *supra* at page 6.

The IRS can hold a corporation liable for employment taxes if the corporation classifies an employee as an independent contractor without a reasonable basis.¹⁰ We question EAA's ability to establish a reasonable basis for this classification. Consequently, this situation potentially exposes not only the worker, but also EAA, to significant tax liability, penalties, and interest. To address this situation, we forwarded pertinent information to the IRS.

Conflict of Interest

An SSA general schedule employee's primary duties consisted of serving as president of the EAA and managing the day-to-day operations of EAA and its related entities. This arrangement appeared to violate Federal conflict-of-interest law and regulations. A conflict of interest exists for Federal employees who participate personally and substantially on a matter as a government employee, when such employees knows that he/she or an organization for whom the employee serves as an officer has a financial interest in such matter.¹¹ Willful violation of the conflict-of-interest law is punishable by fines and up to 5 years in prison.¹² However, SSA allowed an employee's official duties to consist of serving as president of EAA-related corporations that received Federal funds (for example, EAA Fitness equipment purchases, Secur-A-Kiddie Center facility leasing and maintenance, and EAA business office expenses).¹³ Further, Federal employees cannot accept gifts, directly or indirectly, from a prohibited source¹⁴ or given because of the employee's official position;¹⁵ and cannot use their public office for private gain.¹⁶ There were potential violations of these regulations when the SSA

¹⁰ IRS Publication 15-A, *supra* at page 5.

¹¹ 18 U.S.C. § 208(a).

¹² 18 U.S.C. § 216.

¹³ To the extent that the president of EAA negotiated on behalf of EAA other than in the proper discharge of his official duties as a government employee, a potential violation of 18 U.S.C. § 205 conflict-of-interest law may also exist. 18 U.S.C. § 205(a) provides: "Whoever, being an officer or employee of the United States in the executive, legislative, or judicial branch of the Government or in any agency of the United States, other than in the proper discharge of his official duties (1) acts as agent or attorney for prosecuting any claim against the United States, or receives any gratuity, or any share of or interest in any such claim, in consideration of assistance in the prosecution of such claim; or (2) acts as agent or attorney for anyone before any department, agency, court, court-martial, officer, or civil, military, or naval commission in connection with any covered matter in which the United States is a party or has a direct and substantial interest; shall be subject to the penalties set forth in section 216 of this title."

¹⁴ Prohibited source effectively means any persons, corporations, and subsidiaries controlled by such corporations, etc., and officers thereof, who (1) seek official action by the employee's agency; (2) does business or seeks to do business with the employee's agency; (3) conducts activities regulated by the employee's agency; (4) has interests that may be affected by performance or nonperformance of the employee's official duties; or (5) is an organization a majority of whose member are described in (1) through (4) above. 5 C.F.R. § 2635.203(d).

¹⁵ 5 C.F.R. . § 2635.202, *General standards*.

¹⁶ 5 C.F.R. § 2635.702, *Use of public office for private gain*.

employee, in his capacity as EAA president, was given access to Baltimore Ravens season tickets or to meals purchased by EAA, or when the SSA employee used EAA's PSLs to purchase Baltimore Ravens season tickets for his personal use.

It appeared that, as far back as the 1980s, an understanding existed between senior SSA management and the employee that his full-time duties would consist of managing EAA's activities. On March 21, 2001, SSA management formalized this arrangement and approved a position description that made the employee's primary duty to serve as ". . . liaison with SSA employee-sponsored and supported groups and organizations." In this capacity, the employee was to participate in developing objectives and priorities for administering SSA employee-sponsored programs, such as the SSA child-care centers, SSA fitness centers, and EAA; provide advice on Agency-wide initiatives and programs relating to EAA; and establish and maintain working relationships with employee-sponsored groups and organizations.

In December 2008, SSA management addressed this conflict of interest by reassigning the employee to a Public Affairs Specialist position in SSA's Office of Intergovernmental and Community Affairs. In a December 21, 2008 letter, an SSA official formally notified the employee of his reassignment and stated, "I am reassigning you to avoid any possible conflicts of interest between your official duties and the duties you discharge as President of the EAA." The letter stated SSA reassigned the employee to ensure his official duties and responsibilities ". . . in no way bring you into contact with the activities and operations of the Employee Activities Association."

Noncompliance with Agreements Negotiated with SSA

EAA did not comply with certain provisions of agreements negotiated with SSA, and SSA did not enforce these provisions.

- EAA did not have all its entities independently audited annually, as required by a 1977 Administrative Directive governing the relationship between SSA and the EAA and separate MOUs negotiated with SSA. While we observed that EAA produced annual financial statements for all EAA entities, only the Secur-A-Kiddie Center and Scholarship Fund financial statements were audited by an independent accounting firm. EAA management cited the high cost associated with hiring an independent accounting firm to perform financial statement audits as justification for non-compliance. Before hiring a public accounting firm to audit EAA's financial statements in 2008, SSA did not effectively monitor or enforce this requirement.
- EAA did not secure liability insurance coverage for the EAA Fitness operation in amounts required by its MOU with SSA. The MOU required that EAA maintain \$2 million in liability insurance per occurrence and \$4 million in the aggregate. Instead, EAA purchased \$1 million in liability insurance per occurrence, and \$2 million in the aggregate. Available documentation indicated that EAA paid approximately \$7,500 in annual premiums for the liability policy. EAA cited high costs as justification for purchasing less liability insurance than specified in the

MOU. Further, EAA management stated that over the nearly 20 years of operation of the fitness center, no liability claims were filed. Absent enforcement of the MOU provision by SSA, EAA purchased less liability insurance and avoided approximately \$7,500 in annual insurance premiums.

- EAA did not procure the services of a vendor to operate the fitness facilities from 2000 through 2009 as specified in its MOUs with SSA. Although EAA initially complied with this provision in 1988, in Calendar Year 2000, EAA terminated the contract with the fitness center vendor and assumed direct operation of the fitness centers from 2000-2009. Before terminating the MOU and replacing EAA with another vendor in March 2009, SSA did not effectively monitor or enforce this MOU provision.

Further, in 1991, SSA signed an MOU that authorized EAA to provide daycare services for SSA employees who work in Baltimore, Maryland. SSA's award of these services to EAA appeared to violate the intent of the Federal Acquisition Regulation, which generally prohibits a contracting officer from awarding a Government contract to an organization owned or substantially controlled by Federal employees.¹⁷ This regulation is intended to avoid any conflict of interest that might arise between the employees' interests and their Government duties and to avoid the appearance of favoritism or preferential treatment by the Government toward its employees.¹⁸

EAA operated the daycare centers on SSA's campuses for approximately 17 years. In 2008, SSA formed an executive panel to review and make recommendations to improve daycare center operations. To comply with Federal guidelines,¹⁹ the panel recommended establishment of a nonprofit board comprised of employees and other community members. The panel further recommended the nonprofit board award a contract to a child care vendor that could manage, operate, and staff the centers. The nonprofit board was formed and it awarded a contract to a commercial vendor who assumed operation of SSA's Baltimore, Maryland, child care centers from EAA in August 2008.

¹⁷ Federal Acquisition Regulation § 3.601, 48 C.F.R. § 3.601, effective September 24, 1990.

¹⁸ *Id.*

¹⁹ General Services Administration Administrative Order 9252.1, issued in February 1984, allows a Federal agency to allocate space to a voluntary employee association (nonprofit board) for the purpose of providing child care services. With General Services Administration guidance, the Board can select a qualified provider to perform child care services.

Conclusions

Balances reported on EAA and its five related entities' financial statements for FYs 2006 through 2008 were generally valid and supported. However, we identified various reporting or internal control-related issues requiring attention. Also, the financial statements disclosed inter-entity loans totaling \$390,240 that appeared unlikely to be repaid and could jeopardize EAA's tax-exempt status.

EAA may have improperly classified a worker as an independent contractor. EAA paid the worker significant amounts for services performed but did not appear to report the compensation to the IRS. As a result, both the worker and EAA may be liable for payment of significant back income, social security, and Medicare taxes, penalties, and interest.

An SSA general schedule employee's primary duties consisted of serving as president of EAA and managing the day-to-day operations of EAA and its related entities over the past couple decades. This situation appeared to violate Federal conflict-of-interest law and regulations. It appeared senior SSA officials approved this arrangement and allowed it to persist over the past couple decades.

EAA did not comply with certain provisions of agreements negotiated with SSA nor did SSA enforce these provisions. Further, contrary to Federal regulations that prohibit awarding Government contracts to organizations owned or controlled by Federal employees, SSA entered into an agreement that allowed EAA to operate child care facilities on Agency property between 1991 and 2008.

SSA has recently taken several significant actions affecting EAA operations. In December 2008, the EAA president's supervisor formally re-assigned him to duties unrelated to EAA activities. In July 2008, SSA hired a public accounting firm to audit EAA related entities' financial statements. SSA terminated the MOU that allowed Secur-A-Kiddie Center to operate daycare centers on SSA property in Baltimore, Maryland, and replaced Secur-A-Kiddie Center as the daycare center provider in August 2008. Effective January 2009, SSA no longer allowed Service Centers to conduct vendor activities on SSA property. SSA also terminated the MOU allowing EAA to manage fitness centers on SSA property and replaced EAA as the fitness center operator in March 2009.

Appendices

APPENDIX A – Acronyms

APPENDIX B – Scope and Methodology

Acronyms

Board	Board of Directors
CMS	Centers for Medicare & Medicaid Services
EAA	Social Security Employees' Activities Association, Inc.
EAA Fitness	EAA Fitness, Inc.
Form 1099	IRS Form 1099-MISC, Miscellaneous Income
Form W-2	Wage and Tax Withholding
FY	Fiscal Year
IRC	Internal Revenue Code
IRS	Internal Revenue Service
MOU	Memorandum of Understanding
OGC	Office of General Counsel
PSL	Permanent Seat License
Scholarship Fund	The SSA Community Scholarship Fund, Inc.
Secur-A-Kiddie Center	EAA/SSA Secur-A-Kiddie Center, Inc.
Service Centers	EAA Service Centers, Inc.
Service Corp.	EAA Service Corporation, Inc.
SSA	Social Security Administration

Scope and Methodology

We reviewed the responsibilities and benefits derived from Social Security Administration (SSA) funds and resources by the Social Security Employees' Activities Association, Inc., (EAA) and related entities and their management for Fiscal Years (FY) 2006 through 2008. We reviewed EAA's compliance with applicable agreements and Memorandums of Understanding as they pertained to the management and operation of the EAA. To accomplish our objective, we:

- Interviewed employees from SSA and EAA-related entities.
- Reviewed Memorandums of Understanding between SSA and EAA-related entities, and Administrative Directives for compliance with the terms of the written agreements.
- Examined selected income and expense line items from the audited and/or compiled financial statements or tax returns of EAA-related entities for adequate and accurate reporting, validity, and support.
- Identified and reviewed the economic support provided by SSA to EAA-related entities.
- Reviewed work papers and source documentation used in reporting selected income and expense line items for FYs 2006 through 2008.
- Reviewed both direct and indirect compensation received by EAA Board of Directors members, management, and staff.
- Reviewed SSA's awarding, monitoring, and oversight of its agreements with EAA-related entities.

As employees of SSA, Office of the Inspector General staff members are eligible to join the EAA. However, no individuals assigned to this audit team are EAA members. The team also included two auditors provided by the U.S. Postal Service's Office of Inspector General.

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives. We performed our audit from August 2009 through January 2010 at SSA Headquarters and EAA Offices in Baltimore, Maryland.

DISTRIBUTION SCHEDULE

Commissioner of Social Security

Office of Management and Budget, Income Maintenance Branch

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Chairman and Ranking Minority Member, Committee on Appropriations, House of Representatives

Chairman and Ranking Minority, Subcommittee on Labor, Health and Human Services, Education and Related Agencies, Committee on Appropriations, House of Representatives

Chairman and Ranking Minority Member, Committee on Appropriations, U.S. Senate

Chairman and Ranking Minority Member, Subcommittee on Labor, Health and Human Services, Education and Related Agencies, Committee on Appropriations, U.S. Senate

Chairman and Ranking Minority Member, Committee on Finance

Chairman and Ranking Minority Member, Subcommittee on Social Security Pensions and Family Policy

Chairman and Ranking Minority Member, Senate Special Committee on Aging

Social Security Advisory Board

Overview of the Office of the Inspector General

The Office of the Inspector General (OIG) is comprised of an Office of Audit (OA), Office of Investigations (OI), Office of the Counsel to the Inspector General (OCIG), Office of External Relations (OER), and Office of Technology and Resource Management (OTRM). To ensure compliance with policies and procedures, internal controls, and professional standards, the OIG also has a comprehensive Professional Responsibility and Quality Assurance program.

Office of Audit

OA conducts financial and performance audits of the Social Security Administration's (SSA) programs and operations and makes recommendations to ensure program objectives are achieved effectively and efficiently. Financial audits assess whether SSA's financial statements fairly present SSA's financial position, results of operations, and cash flow. Performance audits review the economy, efficiency, and effectiveness of SSA's programs and operations. OA also conducts short-term management reviews and program evaluations on issues of concern to SSA, Congress, and the general public.

Office of Investigations

OI conducts investigations related to fraud, waste, abuse, and mismanagement in SSA programs and operations. This includes wrongdoing by applicants, beneficiaries, contractors, third parties, or SSA employees performing their official duties. This office serves as liaison to the Department of Justice on all matters relating to the investigation of SSA programs and personnel. OI also conducts joint investigations with other Federal, State, and local law enforcement agencies.

Office of the Counsel to the Inspector General

OCIG provides independent legal advice and counsel to the IG on various matters, including statutes, regulations, legislation, and policy directives. OCIG also advises the IG on investigative procedures and techniques, as well as on legal implications and conclusions to be drawn from audit and investigative material. Also, OCIG administers the Civil Monetary Penalty program.

Office of External Relations

OER manages OIG's external and public affairs programs, and serves as the principal advisor on news releases and in providing information to the various news reporting services. OER develops OIG's media and public information policies, directs OIG's external and public affairs programs, and serves as the primary contact for those seeking information about OIG. OER prepares OIG publications, speeches, and presentations to internal and external organizations, and responds to Congressional correspondence.

Office of Technology and Resource Management

OTRM supports OIG by providing information management and systems security. OTRM also coordinates OIG's budget, procurement, telecommunications, facilities, and human resources. In addition, OTRM is the focal point for OIG's strategic planning function, and the development and monitoring of performance measures. In addition, OTRM receives and assigns for action allegations of criminal and administrative violations of Social Security laws, identifies fugitives receiving benefit payments from SSA, and provides technological assistance to investigations.