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October 1996

# CHILD SUPPORT ENFORCEMENT

## States' Experience With Private Agencies' Collection of Support Payments



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

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**Health, Education, and  
Human Services Division**

B-272184

October 23, 1996

The Honorable John R. Kasich  
Chairman, Committee on the Budget  
House of Representatives

Dear Mr. Chairman:

Between 1980 and 1995, the national child support enforcement (CSE) program's caseload more than tripled—from 5.4 million to 20.1 million cases.<sup>1</sup> In addition, the amount of uncollected support from prior years increased from \$8.8 billion in 1986 to \$30.8 billion in 1994. Federal responsibility for the CSE program lies with the Department of Health and Human Services' (HHS) Office of Child Support Enforcement (OCSE). State child support enforcement agencies have responsibility for administering the program at the state and local levels. This includes providing services to locate noncustodial parents, establish paternity and support orders, and collect support payments.

To service this large and growing caseload, some state CSE programs are contracting with private organizations for child support services, including the collection of support payments. Collection services are aimed at obtaining the financial child support legally owed by noncustodial parents to their children. Recent enactment of welfare reform legislation—the Personal Responsibility and Work Opportunity Reconciliation Act of 1996—strengthens the CSE program by providing additional tools to enhance the collection of child support. Among many provisions, the act requires the federal and state governments to establish automated registries of child support orders and a directory of new employees for quickly tracking and locating parents owing support.

This report responds to your request for information on (1) the reasons why states are contracting for CSE collection services and (2) the factors affecting the financial outcomes of collection contracts for families and the federal and state governments. To develop the information in this report, we (1) interviewed CSE officials in nine states identified in our November 1995 report as having collection contracts for which we were

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<sup>1</sup>The caseload figures presented include only those child support cases enforced under Title IV-D of the Social Security Act—cases of Aid to Families With Dependent Children recipients and individuals who requested services.

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able to obtain cost and collection data;<sup>2</sup> (2) analyzed cost and collections data for 11 collection contracts in these states in fiscal years 1994 and 1995; and (3) analyzed state data, compiled by OCSE, on CSE caseloads and support collections in fiscal years 1980 through 1995. We did not compare the contractors' performance with that of state collection efforts because data were not available. Appendix I contains more detailed information on our scope and methodology.

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## Results in Brief

States are turning to private firms to collect child support payments because they are finding it increasingly difficult to service their growing CSE caseloads with available staff and budgetary resources. Most commonly, states contract with the private sector for the collection of past-due support,<sup>3</sup> especially that considered hard-to-collect. Privatizing collections has enabled states to collect support that they would have been unable to collect without hiring additional staff. Under the terms of most collection contracts, states pay contractors only if collections are made and payments to contractors are often a fixed percentage of collections. For example, in fiscal years 1994 and 1995, contractors in nine states collected nearly \$60 million and were paid about \$6 million.

Whether or not these collections provide financial benefits for the states and for the federal government depends on whether the families receiving child support services had received welfare and on the specific financial arrangements that exist between the federal government and each state. For families receiving Aid to Families With Dependent Children (AFDC) benefits,<sup>4</sup> most of the child support collected is retained by the government; in effect, the government is reimbursed for AFDC payments made to families. Families not on AFDC get most of the support collected. The split in collections between the federal and state governments depends first of all on the federal government's share of welfare payments within each state. The more the federal government pays in relation to the state, the more it gets back from child support collections. However, the

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<sup>2</sup>The nine states are Idaho, Kansas, Maryland, Michigan, Missouri, Nevada, New Mexico, Texas, and Virginia. See *Child Support Enforcement: States and Localities Move to Privatized Services* (GAO/HEHS-96-43FS, Nov. 20, 1995).

<sup>3</sup>Any child support legally due but unpaid is considered past-due. Of the nine states that we reviewed, some refer to contractors cases that are 60 days or more past-due, while others refer cases that are 2 years or more past-due.

<sup>4</sup>AFDC provides benefits to economically needy families with children who lack support from one or both of their parents because of death, absence, incapacity, or unemployment. AFDC is funded with federal and state dollars. In fiscal year 1995, the AFDC program provided about \$22 billion in cash benefits to nearly 14 million adults and children. As of July 1, 1997, the AFDC program will be replaced by the Temporary Assistance for Needy Families (TANF) program.

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net amount actually returned to the federal government also is reduced by performance incentives paid to the states and the share of CSE program administrative costs paid by the federal government. In the 11 contracts we reviewed, the federal government's financial outcomes ranged from a net cost of about \$242,000 to revenues of \$1.2 million.

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## Background

Concerned about the cost of AFDC, the Congress established the CSE program in 1975 as Title IV-D of the Social Security Act to help families obtain the financial support that noncustodial parents owe their children and to help single-parent families achieve or maintain economic self-sufficiency. It was anticipated that government welfare expenditures would be reduced by recouping AFDC benefits from noncustodial parents' child support payments. In addition, earlier enforcement of child support obligations for families not receiving AFDC would prevent such families from needing government support.

CSE services provided through the program include locating noncustodial parents; establishing paternity and support orders; updating support orders to be current with a noncustodial parent's income; obtaining medical support, such as medical insurance, from noncustodial parents; and collecting ongoing and past-due support payments. All AFDC recipients are required to participate in the CSE program so that the federal and state governments may recover some portion of the AFDC benefits paid to families.<sup>5</sup> In the case of non-AFDC families, participation in the program is voluntary and most collections are distributed to custodial parents.<sup>6</sup>

The federal and state governments retain collections on AFDC cases as recoupment of AFDC benefits paid to families. More specifically, the government retains all past-due support collected and all but \$50 of each month's current support collected on AFDC cases, up to the amount of the family's monthly AFDC benefits. If the current support collected together with family income makes families ineligible for AFDC, all current support is distributed to the family and the monthly AFDC benefit is not paid.<sup>7</sup>

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<sup>5</sup>A parent who requests AFDC for his or her child is required as a condition of eligibility to assign his or her rights to child support to the government and to cooperate with the CSE program in identifying and locating the noncustodial parent of the child.

<sup>6</sup>If there is unpaid support from prior periods during which the family received AFDC benefits, the governments retain collections in excess of the current monthly amounts due the non-AFDC family.

<sup>7</sup>If there is unpaid support from prior periods during which the state provided AFDC benefits, the governments retain current payments in excess of the monthly support due, up to the limit of assistance paid to the family.

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The federal and state governments share retained collections on AFDC cases by the same percentage as they funded AFDC benefits to families in the state.<sup>8</sup> The percentage of AFDC benefit payments that is funded by the federal government is inversely related to state per capita income and varies from state to state, ranging from 50 percent in states with high per capita incomes, such as California, to close to 80 percent in a state with relatively low per capita income, such as Mississippi.

Collections on non-AFDC cases, though generally not retained by the federal and state governments, might indirectly benefit them. The receipt of these collections by non-AFDC families might preclude the need for these families to seek AFDC benefits, thus enabling the governments to avoid incurring the cost of paying AFDC benefits.

Under the CSE funding structure, the federal government reimburses states for 66 percent of their CSE administrative costs for both AFDC and non-AFDC services.<sup>9</sup> States are responsible for the remaining 34 percent.

The federal government also pays performance incentives to states on the basis of their efficiency in collecting support on both AFDC and non-AFDC cases.<sup>10</sup> These incentives are calculated separately for AFDC and non-AFDC collections. Collection efficiency is determined by dividing AFDC and non-AFDC collections each by total administrative costs. Incentives are paid on the basis of the resulting ratios and range from 6 percent of collections for ratios less than 1.4 to 10 percent of collections for ratios of 2.8 or higher. In practice, all states earn at least 6 percent on AFDC and non-AFDC collections. The total amount of non-AFDC incentives paid, however, is limited to 115 percent of the amount of incentives paid for AFDC collections. The incentive formula seeks to ensure that states provide equitable treatment for both AFDC and non-AFDC families. All but two states had reached the 115-percent cap on non-AFDC incentives in fiscal year 1994.

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<sup>8</sup>As of October 1, 1996, under recently passed welfare reform legislation, retained collections will be shared by the same percentage as the federal and state governments were funding AFDC benefits on September 30, 1996.

<sup>9</sup>The federal government also pays 90 percent of states' costs for certain other services related to paternity establishment. In addition, states are reimbursed for 90 percent of their management information systems' development costs incurred before fiscal year 1996 and 66 percent for such costs in fiscal year 1996 and thereafter.

<sup>10</sup>As discussed later in this report, a new performance incentive system will be created under the Personal Responsibility and Work Opportunity Reconciliation Act of 1996.

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The federal and state governments' net financial revenues or costs from the CSE program are determined by their respective share of (1) AFDC collections retained, (2) CSE administrative costs incurred, and (3) performance incentives paid or received for both AFDC and non-AFDC collections.

Privatized child support contracts in the states cover one or more services and, in general, either supplement state or local program efforts or replace them with privatized offices. As we reported in our November 1995 report, one or more child support services had been privatized statewide in 20 states and at the local office level in 18 states as of October 1995. There were 21 contracts for full-service child support operations, 41 contracts for collections and related parent location services, 9 contracts for payment processing services, and 8 contracts for location services only. Most of these services were being provided by four major contractors.

As evident from our November 1995 report, the most widely privatized service was for the collection of support payments. Services provided under the 41 contracts for support payment collection are typically those performed by debt-collection agencies. These include sending letters and making telephone calls to persons owing support, often after searching various sources, such as credit bureaus, utility companies, and telephone books, to locate parents and obtain their current addresses and telephone numbers.

Under the terms of most collection contracts, contractors are paid only if collections are made. Payments to contractors are often calculated as a percentage of collections—on both AFDC and non-AFDC cases. The payment rates identified for collection contracts in our November 1995 report range from about 8 percent to 24 percent and largely depend on factors such as contract case volume, case collection difficulty, type of cases referred (AFDC or non-AFDC), and the use of multiple or single contractors. States are eligible for federal reimbursement of 66 percent of the payments to contractors as CSE administrative costs.

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## Growing Caseloads and Fiscal Constraints Encourage States to Privatize Collections

When states contract with private firms to provide child support collection services for portions of their caseloads, they often do so to help service their growing caseloads. Some have found it difficult to hire additional staff in an environment of staff and budgetary constraints brought about by increased pressures to downsize government. Recent estimates of CSE caseloads nationwide range from 300 cases to as many as 2,500 cases per

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worker. In 1994, states were able to collect only 55 percent of support due that year and only 7 percent of support due from prior years.

State CSE officials said that contracting with the private sector allows them to service portions of their caseloads without hiring additional staff and to obtain support payments they have been unable to collect. For example, an official from Virginia told us that past-due AFDC cases are sent to contractors because state staff rarely have time to work them. Also, an official from New Mexico said that cases the state sends to contractors for collection services are ones on which the state would not try to collect, believing them difficult to collect and, therefore, not cost-effective to pursue.

Another reason that state officials cited for privatizing was that contracting collections allows their staff to concentrate on paternity and order establishment, functions that the officials believed state employees are more adept at handling than collections. Similarly, some state officials believed that collection agencies have greater expertise and proficiency at collections than state employees.

States are predominantly privatizing collections of past-due support. Of the 41 collection service contracts identified in our November 1995 report, 35 provided for collection of past-due support; 12 of these focused strictly on collecting past-due support for AFDC cases, while the remainder provided for collection of past-due support for both AFDC and non-AFDC cases. Of the remaining 6 contracts, 3 provided for collection of both current and past-due support for AFDC and non-AFDC cases and 3 allowed individual caseworkers discretion to decide what type of child support cases to send to collection contractors.

All nine states we reviewed had criteria for selecting cases to refer for private collection services that were intended to identify cases on which support was hard-to-collect or uncollectible. All the criteria specified minimum periods of time for which collections had not been made, minimum accumulated amounts of past-due support, or both.<sup>11</sup> For example, in Missouri, the criteria specified that cases with at least 6 months of support past-due that was in an amount in excess of \$500 and for which no payments had been made in a year should be referred to the contractor. In addition to the minimum time and past-due support criteria, Kansas and Idaho referred only closed AFDC cases—those involving

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<sup>11</sup>Cases that are not classified as hard-to-collect or uncollectible could also meet the criteria if states had not worked on them or not tried to collect support for a period of time. We did not sample referred cases to determine if the states had attempted collection efforts.



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custodial parents who were not currently receiving AFDC, but in which the noncustodial parent owed support to the state from prior periods when the state paid AFDC benefits to the custodial parent.<sup>12</sup> An official from Kansas said that closed AFDC cases referred for collection are ones the state had tried unsuccessfully for several years to collect on and were not currently receiving attention.

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### Type of Cases Referred and AFDC and CSE Funding Structures Determine Extent of Collections

State decisions about what types of cases to refer for privatized collection determine whether and the extent to which families and the federal and state governments benefit from collection contracts. Collections on AFDC cases benefit governments directly because they retain some of the support collected, while collections on non-AFDC cases benefit families directly because most collected support is distributed to them. Whether the federal or state governments experience net CSE revenues or costs from collection contracts is principally affected by (1) AFDC cost-sharing ratios, (2) states' efficiency in making collections that earn incentives under the CSE program, and (3) the CSE administrative cost-sharing ratio. We did not assess whether the contracts were cost-effective compared to increased state efforts to collect.

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### Governments Retain Collections on AFDC Cases, While Families Receive Collections on Non-AFDC Cases

The federal and state governments benefited from collections under all 11 contracts that we analyzed because all the states involved referred AFDC cases for collection, as shown in table 1. On AFDC cases, the federal and state governments retained all collections of past-due support and all but \$50 of current support collected up to the amount of each families' monthly AFDC benefit. Furthermore, states earned performance incentives from the federal government on both AFDC and non-AFDC collections.

Families also benefited from collections under five contracts that collected on AFDC, non-AFDC, or both types of cases. Contractors in Maryland and Michigan collected support that was distributed to both AFDC and non-AFDC families, while the contractor in Missouri collected support distributed to only AFDC families and the contractor in Texas to only non-AFDC families.

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<sup>12</sup>When they first began privatizing collections, Virginia and Texas also referred only closed AFDC cases, but have since expanded to referring all past-due support cases.

Table 1: Financial Outcomes of 11 Child Support Collection Contracts, by Number and State

Fiscal year	Payment terms <sup>a</sup>	Collections			Total	Federal share of retained AFDC collections <sup>b</sup> (percent)	Contract costs	Net CSE financial revenues (costs)	
		Retained by federal and state governments	Distributed to families					State	Federal
			AFDC	Non-AFDC					
<b>1-Idaho</b>									
1994	21	\$250,913	c	d	\$250,913	71	\$52,692	\$87,418	\$110,803
1995	21	283,343	c	d	283,343	70	59,502	100,927	122,914
<b>2-Kansas</b>									
1994 <sup>e</sup>	17	30,359	c	d	30,359	60	19,488 <sup>f</sup>	9,580	1,291
1995	17	51,789	c	d	51,789	59	33,408 <sup>f</sup>	16,607	1,774
<b>3-Maryland (covers only Prince Georges County and Baltimore City, Maryland)</b>									
1995 <sup>g</sup>	12.85	1,945,489	\$3,928,277	397,762	6,271,528	50	654,307	1,052,559	238,622
<b>4-Michigan (covers only Bay County, Michigan)</b>									
1994	20	2,127,808	9,626,403	23,900	11,778,111	56	992,981	891,450	243,377
1995	20	2,145,932	10,149,685	21,525	12,317,142	57	384,078	1,098,500	663,354
<b>5-Michigan (covers only Midland County, Michigan)</b>									
1994	20	988,530	6,035,909	15,650	7,040,089	56	997,947	232,328	(241,745)
1995	20	1,059,471	6,555,550	14,650	7,629,671	57	920,781	294,311	(155,621)
<b>6-Missouri</b>									
1995 <sup>g</sup>	9.9	631,288	c	9,400	640,688	60	64,005	314,286	252,997
<b>7-Nevada</b>									
1995 <sup>g</sup>	20	121,501	c	d	121,501	50	50,000 <sup>h</sup>	59,424	12,077
<b>8-New Mexico</b>									
1995 <sup>g,i</sup>	22	123,590	c	d	123,590	73	25,954	40,105	57,531
<b>9-New Mexico</b>									
1995 <sup>g,i</sup>	21	241,679	c	d	241,679	73	50,753	78,425	112,501
<b>10-Texas</b>									
1994	13.24	3,133,976	1,153,247	d	4,287,223	64	569,244	1,333,330	1,231,402
1995	13.24	2,342,073	1,799,648	d	4,141,721	63	548,364	974,990	818,719
<b>11-Virginia</b>									
1994	20	1,334,555	c	d	1,334,555	50	254,013	753,071	327,471
1995	20	3,139,372	c	d	3,139,372	50	494,113	1,806,666	838,592

(Table notes on next page)

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Notes: Contract costs may be understated; thus, net CSE financial revenues or costs also may be overstated or understated, respectively. In addition to amounts paid the contractor for collections, Kansas and Nevada also reported other administrative costs associated with the contract. No other state reported such costs.

Contract collections and costs were reported to us by the state and local CSE offices; we calculated collections distributed to families and retained by government, and state and federal net CSE revenues or costs. Because in most states past-due support on cases under collection contracts was categorized as uncollectible or expected to be, our net CSE revenue/cost calculations assume that collections under these contracts were additional collections that would not have been made but for the collection contract and contract costs were additional costs invested in collection efforts on these cases. States may have incurred other costs necessary to generate collections on cases under private contract, such as costs for paternity and order establishment, but these costs are not determinable and are not included in our net CSE revenue/cost calculations.

Contracts cover collections statewide unless otherwise indicated.

<sup>a</sup>Payment terms are expressed as a percentage of contractor-generated collections.

<sup>b</sup>Equivalent to the percentage of AFDC costs borne in each state by the federal government.

<sup>c</sup>No non-AFDC collections were made under these contracts.

<sup>d</sup>No current AFDC collections were made under these contracts.

<sup>e</sup>Includes only 7 months of fiscal year 1994.

<sup>f</sup>Contract costs include costs of administering the contract and costs per case of operating the state's parent locator services in addition to contractor payments of 17 percent of collections.

<sup>g</sup>These contracts were not in effect in fiscal year 1994.

<sup>h</sup>Contract costs include state computer programming expenses in addition to contractor payments of 20 percent of collections.

<sup>i</sup>These contracts had different contractors and covered different geographic areas.

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**Governments' Net CSE Revenues or Costs Affected by AFDC Cost-Sharing Ratios, State Collection Efficiency, and the CSE Administrative Cost-Sharing Ratio**

As illustrated in figure 1, the net financial revenues or costs of the CSE program to the federal government are equal to its share of retained AFDC collections, minus performance incentives paid states, minus its share of CSE administrative costs. For state governments, the computation is the same except that performance incentives are added instead of subtracted.

**Figure 1: Equations for the Federal and State Governments' Net CSE Revenues or Costs**

<b>Federal</b>				
Net CSE Revenues or Costs	=	Share of Retained Collections	-	Performance Incentives Paid to States - 66% of Collection Contract Costs
<b>State</b>				
Net CSE Revenues or Costs	=	Share of Retained Collections	+	Performance Incentives From the Federal Government - 34% of Collection Contract Costs

Note: Collection contract costs include payments to contractors and other associated administrative costs.

Retained collections are calculated by multiplying the federal or state government's AFDC cost-sharing ratio by AFDC collections reduced by the amounts passed through to families. For example, if AFDC collections were \$100,000 and \$18,000 was passed through to families,<sup>13</sup> the remaining \$82,000 in collections would be available for sharing by the federal and state governments. If the federal government's AFDC cost share in the state was 60 percent, the federal government's retained collections would equal 60 percent of \$82,000, or \$49,200. The state's share would be 40 percent of \$82,000, or \$32,800.

The performance incentives are calculated by computing the state's collection efficiency ratios for AFDC and non-AFDC collections to determine the percentage of incentives earned, then multiplying the earned percentages by the associated type of collections—most states earn 6 percent incentives and have reached the 115-percent cap on non-AFDC incentives. For example, if AFDC collections were \$100,000 as above, non-AFDC collections \$400,000, and total administrative expenses \$125,000,<sup>14</sup> the collection efficiency ratio for AFDC collections would equal 0.8 (\$100,000 in collections divided by \$125,000 in administrative expenses). Collection efficiency ratios lower than 1.4 earn 6 percent AFDC

<sup>13</sup>Nationwide, current support payments passed through to families were about 18 percent of AFDC collections in 1994.

<sup>14</sup>In the CSE program nationwide, total non-AFDC collections are about three times AFDC collections and total administrative expenses are approximately 25 percent of total collections.

incentives; therefore, AFDC incentives in this example would equal 6 percent of \$100,000, or \$6,000. The non-AFDC collection efficiency ratio in this example equals 3.2, \$400,000 divided by \$125,000. This ratio would earn incentives of 10 percent of collections. However, since non-AFDC incentives cannot exceed 115 percent of AFDC incentives, non-AFDC incentives that can be received in this example would be limited to 115 percent times \$6,000, or \$6,900. Thus, the federal government would pay the states \$12,900 in performance incentives on the \$500,000 in collections.

Contract costs are calculated by multiplying the contract percentage rate to be paid the contractor for collections by total collections. Continuing the above example, with total collections of \$500,000 and a payment rate of 25 percent, contract costs would equal \$125,000. The federal government would reimburse the states for 66 percent of these costs, or \$82,500.

Accordingly, in this example, the federal government would experience net CSE costs of \$46,200, after receiving \$49,200 in retained AFDC collections and paying \$12,900 in performance incentives and \$82,500 in contract costs. The state on the other hand would experience net CSE revenues of \$3,200, after receiving \$32,800 in retained AFDC collections and \$12,900 in performance incentives and paying \$42,500 in costs.

Table 2 summarizes the several factors that affect the calculation of the federal and state governments' respective shares of retained collections, performance incentives, and contract costs.<sup>15</sup>

**Table 2: Factors That Determine the Federal and State Governments' Net CSE Revenues or Costs**

Equation variables	Factors
Retained collections	<ul style="list-style-type: none"> <li>- AFDC or non-AFDC collections</li> <li>- current or past-due support on AFDC cases</li> <li>- AFDC collections distributed to families</li> <li>- AFDC cost-sharing ratios</li> </ul>
Performance incentives	<ul style="list-style-type: none"> <li>- AFDC and non-AFDC collections</li> <li>- contract costs</li> <li>- incentives earned (6 to 10 percent of collections)</li> <li>- 115-percent cap on non-AFDC incentives</li> </ul>
Contract costs	<ul style="list-style-type: none"> <li>- total collections</li> <li>- percent of collections to be paid contractor</li> </ul>

<sup>15</sup>In our calculations of net CSE revenues or costs under the 11 contracts, all collections are assumed to be additional collections that would not have been made but for the contract, and payments to contractors are considered additional costs the states incurred to generate collections.

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## Contracts Illustrate How Various Factors Interact to Influence Net CSE Revenues or Costs

As shown in table 1, collections under 10 of the 11 contracts we analyzed generated net CSE financial revenues for both the federal and state governments.<sup>16</sup> The federal government's net revenues were less than the states' under the seven contracts in Kansas, Maryland, Michigan (number 4), Missouri, Nevada, Texas, and Virginia and greater than the states' under the three contracts in Idaho and New Mexico. Under one contract in Michigan (number 5), the federal government experienced net CSE costs, while the state experienced net revenues.

The influence of case type on retained collections and of total collections on contract costs can be seen in the outcomes under the two contracts in Michigan. As shown in table 1, under contract number 5, the federal government experienced net CSE costs in part because most of the collections were for non-AFDC support, none of which was retained by the federal or state governments. Furthermore, the non-AFDC collections were about six times as great as AFDC collections, contributing to higher contract costs but not retained collections. Consequently, under this contract, the federal government's share of retained AFDC collections was not large enough to offset its share of contract costs and performance incentives paid to the state based on AFDC and non-AFDC collections.

In contrast, under contract number 4 in Michigan, even though non-AFDC collections were greater than contract number 5, the federal government experienced net CSE financial revenues. This occurred because AFDC collections were a larger share of total collections than under the other contract. In addition, contract costs as a percentage of collections were lower on contract number 4—8 percent and 3 percent compared with 14 percent and 12 percent of collections on contract number 5.

The influence of whether collections are AFDC or non-AFDC is also apparent in the outcomes of the contracts in Nevada and Kansas. Although contract costs as a percentage of total collections in these two states were relatively high—41 percent to 65 percent, respectively—both the federal and state governments experienced net revenues because all collections under the contracts were past-due AFDC, which are fully retained by the governments. Costs reported to us for these two contracts included state costs for computer programming and administering the contract in addition to the percentage of collections paid the contractor.

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<sup>16</sup>The fact that governments experienced net CSE revenues from collections under most of the contracts we examined does not indicate whether contractors' performance was more or less cost effective than states'. Data on the cost of states' provision of collection services are not available for comparison with contractor performance.

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Another factor influencing the financial outcomes of collection contracts is the AFDC cost-sharing ratio, as illustrated by the financial outcomes under the contracts in Idaho and New Mexico. Under the three contracts in these states, the federal government's net CSE revenues were greater than those of the states, largely because the federal share of retained AFDC collections was relatively high—ranging from 70 percent to 73 percent.

The influence of AFDC cost-sharing ratios on retained collections and of AFDC or non-AFDC collections on contract costs also can be seen in comparing the financial outcomes from the contracts in Maryland and Texas for fiscal year 1995. The federal government gained less net revenue under the contract in Maryland than in Texas. One reason for this result is that the federal government's share of retained AFDC collections was less in Maryland than in Texas—50 percent compared with 64 percent. In addition, contract costs were higher under the contract in Maryland because total collections were greater and non-AFDC collections (not retained) were greater than AFDC collections (retained) by a ratio of about 3 to 2, thus contributing to higher contract costs but not retained collections.

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### Welfare Reform Will Impact Financial Outcomes of Collection Contracts for Families and Government

The financial outcomes of collection contracts for families and government will be impacted by changes to be implemented under recent welfare reform legislation—the Personal Responsibility and Work Opportunity Reconciliation Act of 1996. For example, among several such changes, after September 2000, for families that are no longer receiving government assistance, collection of past-due support that accrued before or after the family received such assistance generally will be distributed first to the family.<sup>17</sup> Furthermore, the pass-through to families of the first \$50 of current support payments collected will no longer be mandatory. If states choose to continue to pass-through the \$50 and disregard it in determining the income of families receiving assistance, the states must pay for the disregard with state funds.

The legislation also affects the incentive payments that states receive. It directs the Secretary of HHS in consultation with the states to develop a new performance incentive system to replace, in a revenue neutral manner, the existing system. The legislation requires the Secretary to report on the new system to the Congress by March 1, 1997, and makes the new system effective on October 1, 1999.

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<sup>17</sup>Currently, under the law regarding distribution of child support payments, the government is generally reimbursed first for any past-due support that is assigned to the state up to the limit of assistance paid to the family, then families are reimbursed for any past-due support owed them.

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## Agency Comments and Our Evaluation

In commenting on a draft of this report, HHS said that it believes that our report should be a useful reference to states as they consider privatizing child support functions. HHS also provided technical comments that we incorporated in the final report as appropriate.

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We are sending copies of this report to the Chairmen and Ranking Minority Members of the Senate Committee on Finance and the House Subcommittee on Human Resources, Committee on Ways and Means; the Secretary of HHS; and HHS' Assistant Secretary for Children and Families. We will also make copies available to others on request.

We will continue to keep you and your staff informed of our progress in reviewing state CSE privatization initiatives. If you or your staff have any questions about this report, please contact David P. Bixler, Assistant Director, at (202) 512-7201 or Catherine V. Pardee, Senior Evaluator, at (202) 512-7237.

Sincerely yours,



Mark V. Nadel  
Associate Director, Income Security Issues



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## Abbreviations

AFDC	Aid to Families With Dependent Children
CSE	Child Support Enforcement
HHS	Department of Health and Human Services
OCSE	Office of Child Support Enforcement
TANF	Temporary Assistance to Needy Families

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# Scope and Methodology

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Using contract cost and collection data provided by state and local CSE offices, we determined the financial outcomes for 11 collection contracts by calculating (1) collections distributed to families and retained by the federal and state governments and (2) net CSE financial revenues or costs for the federal and state governments. The net CSE financial revenues or costs to the governments equal the federal or state governments' respective share of (1) retained collections, (2) performance incentives paid by the federal government and received by states, and (3) contract costs. We did not independently verify the contract cost and collection data provided by states.

We sought data only on collection contracts listed in our November 1995 report in which payment terms were disclosed and stated as a percentage of collections, the most common method of payment in collection contracts. Although we sought data on more than 11 contracts, cost and collection data available from some states were insufficient to determine how support collected was distributed between families and the federal and state governments. Specifically, some states could not separately identify amounts of collections on non-AFDC and AFDC cases and the total amount of current AFDC support distributed to AFDC families on cases with collections. For these reasons, our data analysis and interviews were limited to 11 contracts in nine states: Idaho, Kansas, Maryland, Michigan, Missouri, Nevada, New Mexico, Texas, and Virginia.

Our calculation of net CSE financial revenues or costs constitutes a comparison of additional collections with additional collection costs. Support collected under the 11 collection contracts was classified by the state programs as uncollectible or expected to be uncollectible, and we assumed that collections under the contracts would not have been made by the states. Payments to the contractors represented additional costs that the states invested in collection efforts on cases under the contract. We did not attempt to determine whether the states would have spent more or less to collect the amounts using state employees or through other means.

With the exception of two states, the contract cost data that states provided included only the payments to contractors based on a percentage of collections. Additional state costs associated with the collection contracts, such as for contract negotiation and administration, could not be determined and were not included in our calculations.

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**Appendix I**  
**Scope and Methodology**

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In calculating the governments' respective share of retained collections, we used the AFDC cost-sharing ratios for each state for the same year as the collection contracts. In calculating performance incentives, we used statewide collection efficiency ratios for the states for 1994 as reported in data compiled by OCSE.

We performed our work from November 1995 to August 1996 in accordance with generally accepted government auditing standards.

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# Related GAO Products

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Child Support Enforcement: States and Localities Move to Privatized Services (GAO/HEHS-96-43FS, Nov. 20, 1995).

Child Support Enforcement: Opportunity to Reduce Federal and State Costs (GAO/T-HEHS-95-181, June 13, 1995).

Child Support Enforcement: Families Could Benefit From Stronger Enforcement Program (GAO/HEHS-95-24, Dec. 27, 1994).

Child Support Enforcement: Federal Efforts Have Not Kept Pace With Expanding Program (GAO/T-HEHS-94-209, July 20, 1994).

Child Support Enforcement: Credit Bureau Reporting Shows Promise (GAO/HEHS-94-175, June 3, 1994).

Child Support Enforcement: States Proceed With Immediate Wage Withholding; More HHS Action Needed (GAO/HRD-93-99, June 15, 1993).

Child Support Assurance: Effect of Applying State Guidelines to Determine Fathers' Payments (GAO/HRD-93-26, Jan. 23, 1993).

Child Support Enforcement: Timely Actions Needed to Correct System Development Problems (GAO/IMTEC-92-46, Aug. 13, 1992).

Child Support Enforcement: Opportunity to Defray Burgeoning Federal and State Non-AFDC Costs (GAO/HRD-92-91, June 5, 1992).

Interstate Child Support: Wage Withholding Not Fulfilling Expectations (GAO/HRD-92-65BR, Feb. 25, 1992).

Interstate Child Support: Mothers Report Less Support From Out-of-State Fathers (GAO/HRD-92-39FS, Jan. 9, 1992).

Child Support Enforcement: A Framework for Evaluating Costs, Benefits, and Effects (GAO/PEMD-91-6, Mar. 5, 1991).

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