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Some financial incentive is needed to assure that States continue to seek appropriate corrective actions to the high number of erroneous payments made to recipients of aid-to-families-with-dependent-children. Findings/Conclusions: Although error rates have declined since 1973, nearly $500 million a year in Federal funds is being misspent. The Department of Health, Education, and Welfare (HEW) presently lacks the means for withholding funds and will continue to encounter problems in implementing any financial incentive provision administratively. Through 1976, HEW has overstated accomplishments in reducing errors. Changes in administrative practices reduced errors, but they did not necessarily reduce welfare payments. Recommendations: To improve the quality control program administration, the Secretary of Health, Education, and Welfare should revise HEW's basis for determining program accomplishments so that savings are determined on the basis of valid statistical projections and by considering only error reductions that directly reduce program costs; base HEW reporting of State errors on dollar amounts rather than case error rates; and assist States in identifying cost-effective corrective actions. Congress should enact legislation to establish an incentive to encourage better administration and cost control for the program. Such legislation should provide for a payment error rate rather than a case error rate as the basis for measuring State accomplishments in reducing error. (Author/SC)

REPORT TO THE CONGRESS

BY THE COMPTROLLER GENERAL OF THE UNITED STATES

Legislation Needed To Improve Program For Reducing Erroneous Welfare Payments

Department of Health, Education, and Welfare

In March 1977, as a result of court decisions, HEW eliminated a 4-year-old provision to withhold funds from States that did not meet goals for reducing erroneous payments in the aid-to-families-with-dependent-children program.

Although error rates have declined since 1973, nearly $500 million a year in Federal funds is being misspent. HEW presently lacks means for withholding funds and will continue to encounter problems in implementing any financial incentive provision administratively. Therefore the Congress should enact legislation to provide financial incentives to States to effectively control errors.

Through 1976, HEW has overstated accomplishments in reducing errors. Savings estimates have not been based on valid statistical projections. Changes in administrative practices reduced errors but did not necessarily reduce welfare payments.

HRD-76-164

AUGUST 1, 1977

COMPTROLLER GENERAL OF THE UNITED STATES
WASHINGTON, D.C. 20548

B-164031(3)

To the President of the Senate and the
Speaker of the House of Representatives

For several years, the Congress has expressed concern about the high incidence of error in the Aid to Families with Dependent Children program. In 1973, the Department of Health, Education, and Welfare responded to this concern and established a timetable in its quality control program requiring States to achieve specified error tolerances to avoid possible loss of Federal funds. In March 1977, as a result of court decisions, the Department revoked the fiscal disallowance provision.

We reviewed the quality control program to determine the extent States were reducing errors and to evaluate the accomplishments being cited by HEW.

This report describes actions that HEW should take to improve the quality control program and the reporting of its accomplishments. It also discusses the Congress' need to enact legislation to provide fiscal incentives to States to effectively control errors.

We made our review pursuant to the Budget and Accounting Act, 1921 (31 U.S.C. 53), and the Accounting and Auditing Act of 1950 (31 U.S.C. 67).

We are sending copies of this report to the Director of the Office of Management and Budget and to the Secretary of Health, Education, and Welfare.

Elmer B. Staats

Comptroller General
of the United States

COMPTROLLER GENERAL'S REPORT TO THE CONGRESS

LEGISLATION NEEDED TO IMPROVE PROGRAM FOR REDUCING ERRONEOUS WELFARE PAYMENTS
Department of Health, Education, and Welfare

D I G E S T

The Congress has become increasingly concerned about the high number of erroneous payments to people receiving assistance under the aid-to-families-with-dependent-children program.

BACKGROUND

In 1973, the Department of Health, Education, and Welfare (HEW) sought improvement in its quality control program by providing financial incentives to the States. Each State was required to operate a quality control program designed to keep error rates below established levels (3 percent for ineligibility and 5 percent for overpayment). HEW said it would not reimburse States for overpayments or payments to ineligible persons if the payments exceeded those error levels.

The first quality control reports under the new program covered April to September 1973. For the first time, all States fully complied with HEW requirements for implementing quality control programs. The national error rate was about 10 percent for ineligible participants and about 23 percent for overpayments. States were then given until December 1975 to reduce errors to 3 and 5 percent to avoid having funds withheld from them (fiscal disallowance).

The fiscal disallowance provision has been the center of controversy between HEW and the States. This provision has been challenged in three court actions. In each case, U.S. district courts ruled that HEW could disallow funds. Two of the actions also addressed the reasonableness of HEW's 3- and 5-percent levels. In those actions, the courts ruled that, because the levels were not established on empirical evidence, the fiscal disallowance regulation was arbitrary and invalid. (See pp. 7 and 8.)

In March 1977, HEW removed the fiscal disallowance provision from its regulations in recognition of the court decisions. As of June 1977 HEW had not reached a decision on the establishment of any alternative fiscal disallowance provision.

LEGISLATION NEEDED

The fiscal disallowance provision HEW added to its quality control program motivated States to increase their efforts to reduce errors and has provided much information about these errors. Although error rates have been reduced, they are still at relatively high levels in many States. As of the June 1976 reporting period the error rate for ineligibility was 5.5 percent and ranged from 0.6 percent to 14.6 percent among the States. The overpayment error rate was 13.9 percent, ranging from 3.4 percent to 25.7 percent. Nearly $500 million a year in Federal funds is being misspent in the aid-to-families-with-dependent-children program.

Some financial incentive is needed to assure that States continue to seek appropriate corrective action. HEW has encountered legal problems in attempting to implement a financial incentive administratively. GAO believes HEW will continue to have difficulty if it decides to establish any new incentive, especially in satisfying the courts that it had a reasonable basis for the incentive provision. GAO believes it would be more appropriate for the Congress to determine the control that would best provide the desirable financial incentive to the States for reducing errors. In May 1977 a bill was introduced in the House of Representatives to authorize such fiscal incentives.

In recent years, the Congress has established incentives to encourage better administration and cost control for other activities covered by the Social Security Act, and should establish similar legislation to provide incentives for the welfare program. (See pp. 12 to 15.)

GAO recommends that the Congress enact legislation to establish such an incentive for controlling payment errors. Such legislation should provide for a payment error rate rather than a case error rate as the basis for measuring State accomplishments in reducing error. HEW's case error rate does not directly show the money spent in error.

OVERSTATED ACCOMPLISHMENTS

Since the quality control program was initiated in 1973, HEW has continually overstated the program's accomplishments. Estimates of savings resulting from error reductions were not based on valid statistical projections and included actions which did not necessarily produce direct savings in welfare payments. HEW's estimates assume a direct relationship between reduced error rates and program savings. A State, however, can eliminate certain errors which do not necessarily produce savings in welfare payments. (See pp. 38 to 42.)

HEW did not consider the administrative costs associated with implementing corrective actions. In addition, States generally did not conduct cost-effectiveness studies before starting corrective actions, although required by HEW. Some State officials said the fiscal disallowance program did not provide enough time for testing possible corrective actions. (See pp. 42 to 45.)

RECOMMENDATIONS

To improve quality control program administration, the Secretary of HEW should:

--Revise HEW's basis for determining program accomplishments. HEW should determine savings on the basis of valid statistical projections and should only consider error reductions that directly reduce program costs. Savings should take into account the increased administrative costs of implementing corrective actions.

--Base HEW reporting of State errors on dollar amounts rather than case error rates.

--Assist States in identifying cost-effective corrective actions. (See p. 46.)

AGENCY COMMENTS

With some qualifications, HEW agreed with GAO's recommendation for revising the basis for determining program accomplishments. HEW agreed to include tests of statistical significance but stated that its method may differ from what GAO recommended. HEW said such tests would be made on national rates only. GAO believes that, since the quality control samples are taken separately for each State, tests should be made for each State. (See p. 47.)

HEW agreed in principle that the determination of savings should include (1) the effect of error reductions that do not directly produce savings and (2) the administrative costs incurred to achieve error reductions. HEW said that it could not calculate true net savings, but agreed to study whether such data could be obtained. GAO believes that, in the meantime, savings reported by HEW should be qualified to show they do not necessarily represent that level of reduction in welfare costs. (See p. 47.)

HEW said the emphasis on cost effectiveness tends to prevent a better understanding of the program's accomplishments. GAO recognizes that much has been accomplished, but believes that HEW's method of attributing savings to quality control detracts from the credibility of its positive accomplishments. (See pp. 47 to 49.)

HEW agreed with GAO's recommendation to base its reporting of errors in dollars rather than case errors and agreed to use this approach in future reporting.

HEW said it is constantly striving to more effectively assist States in identifying cost-effective corrective actions and identified several publications it issued to the States describing actions by selected States. GAO believes, however, that HEW should be more than a conduit for exchanging information among States; it should learn more about which actions are effective and assist States in adopting such practices. (See pp. 49 and 50.)

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ABBREVIATIONS

AFDC	Aid to families with dependent children
GAO	General Accounting Office
HEW	Department of Health, Education, and Welfare

CHAPTER 1

INTRODUCTION

Aid to families with dependent children (AFDC) is one of the largest public assistance programs of the Federal Government. This program, which is directly administered by the States, provides financial assistance to needy children and their parents or relatives to encourage the care of dependent children in their or relatives' home. The program is administered at the Federal level by the Department of Health, Education, and Welfare (HEW). Federal and State payments during fiscal year 1976 amounted to $9.6 billion, of which the Federal share was $5.3 billion--55 percent of the total.

HEW and the Congress have been concerned for several years with the high incidence of erroneous payments to AFDC recipients. HEW has attempted to reduce the error rates by encouraging States to implement a quality control system designed

--to monitor and report on the eligibility of recipients and correctness of payments and

--to identify corrective actions needed to keep error rates at acceptable levels.

QUALITY CONTROL DEVELOPMENT 1964-1970

In June 1962 the Senate Appropriations Committee reported (S. Rept. 1672, 87th Cong. 2d sess.) on the HEW appropriation bill for fiscal year 1963, and expressed strong concern about the eligibility of AFDC recipients and called for a thorough nationwide examination of the AFDC program for the following year. In 1963 an HEW investigation of the program showed that some States had high rates of ineligibility. HEW and State welfare officials agreed that vigorous action was needed to improve the program's administration.

In response to this need, HEW developed a quality control program to help make sure of correct payments to qualified AFDC recipients. The early program focused on case worker performance and monitored decisions made by the worker. The program was not designed to report primarily on ineligibility rates in the total caseload. During this period, States were slow in setting up separate quality control units, and the HEW staff at both central and regional offices carried quality control responsibilities in addition to numerous other duties. The effectiveness of quality control by the States and the monitoring and technical assistance by HEW varied nationally.

In the late 1960s, HEW completely reassessed the quality control program to make it more responsive to State agency needs and decided that more emphasis had to be given to the program to make it a viable management tool for corrective action.

QUALITY CONTROL REVISIONS 1970-1973

A revised quality control program went into effect in October 1970, providing for:

1. Increasing sample sizes for more precise data.

2. Establishing tolerence limits of 3 percent for ineligibility, 5 percent for overpayments, and 5 percent for underpayments.

3. Identifying the specific factors contributing to the errors.

4. Distinguishing between client error and agency error.

5. Formalizing a Federal monitoring program.

6. Emphasizing data analysis to take corrective action.

In spite of the concerted effort to improve quality control, many States failed to respond positively to the program. In 1972, we reported 1/ that all eight States we had reviewed had encountered problems. The States' quality control units were understaffed, required sample sizes were not completed, and required reports were not submitted. Also, according to HEW, in early 1973, 19 States did not have operational quality control programs.

In December 1972 HEW proposed regulations to take effect in January 1973 which would exclude from Federal financial participation all expenditures for payments to ineligible families and overpayments to eligible families. This action represented an abrupt change in the quality control program.

1/"Problems in Attaining Integrity in Welfare Programs" (B-164031 (3), March 16, 1972).

At the time case error rates in many States far exceeded the original 3- and 5-percent tolerance levels. For example, a February 1973 report on tolerance levels prepared for HEW by Westat Research, Inc., showed that as of June 1972, 10 States had error rates for ineligibility of 9 percent or more, while nearly half of the States had overpayment error rates of 18 percent or more. An HEW national quality control sample for March 1972 showed a national average of 6.8 percent of all cases ineligible and 13.8 percent receiving overpayments.

After receiving numerous comments and suggestions from several States, HEW announced in April 1973 that it had modified its proposed regulations and would implement a program intended to require each State to attain the original 3-percent tolerance for ineligibility and 5-percent tolerance for overpayments. Fiscal disallowances--Federal funds withholdings--would be imposed against States not meeting the tolerances. Little information was available on how these tolerance levels were established. The Westat Research report indicated that these levels were based on previous experience with other systems, tempered by judgments of available evidence of what might be feasible and what the public might regard as acceptable. The report further indicated that the 3-percent tolerance on ineligibility seemed to be attainable but that the 5-percent tolerance on overpayments should have been 9 percent given the number of overpayment cases in 1972. HEW concluded that, given a vigorous corrective action program, the established tolerances were reasonable and attainable.

1974-1976 CONTROLS

The modified quality control program called for each State to establish a "base error rate" using quality control findings for the April-September 1973 review period. Improvements were to be measured against the base error rate over successive 6-month periods beginning January 1, 1974. All States were expected to reduce by at least one-third the amount by which their base error rate exceeded the 3- and 5-percent tolerance levels in each of the first three 6-month periods. Thereafter, States were not expected to exceed the tolerances.

Also, as part of the modified program, HEW expanded its monitoring to include re-reviews of subsamples of each State's periodic quality control reviews. The purpose of the re-review process was to make sure that State quality control programs were operating in accordance with federally established requirements and to confirm the validity of State error rates.

The results of the January-June 1974 review showed that few States had achieved considerable reductions in error rates. The States believed little progress had been made because the corrective actions implemented after the base period review had not had time to be effective. The States requested that HEW--before considering reduction in Federal financial participation--allow them additional time to measure their error rates more accurately and permit more time for their corrective action plans to produce error reductions.

HEW revised the basis for applying fiscal disallowances in October 1974. The revised regulations provided that

--the base period error rate be determined by combining the results of the April-September 1973 and January-June 1974 review periods and

--States would incur disallowances of Federal financial participation if they did not proportionately reduce their error rates toward the 3- and 5-percent tolerance levels during the July-December 1974 and January-June 1975 review periods.

The revised regulations also established a tolerance level of 5 percent for underpayments. HEW stated that this revision emphasized its commitment to the proposition that individuals participating in the AFDC program should receive the amount of assistance for which they are eligible. There would be no fiscal consequences to States, however, because no method for excluding Federal participation for amounts underpaid to recipients was available. HEW believed, however, that implementation of States' corrective actions would resolve the underpayment problem while reducing overpayments, since many of the errors which cause overpayments also cause underpayments.

The first fiscal disallowances were to be reflected in the April 1975 quarterly grant awards. In March 1975 HEW decided to delay imposing fiscal disallowances until after July 1, 1975, thereby eliminating interim reductions. HEW decided to give the States an additional grace period to reduce their error rates because of the States' increased financial commitments due to high unemployment rates and the uncertain state of the economy. Fiscal disallowances were to be applied in those States with error rates exceeding 3 percent for ineligibility and 5 percent for overpayments based on the results of the July-December 1975 review period.

The fiscal disallowance provision of the quality control regulation has been a controversial issue between HEW and the States. In May 1976 the U.S. District Court for the District of Columbia ruled on a suit brought by Maryland and 14 other jurisdictions challenging that regulation. The court ruled that although HEW had the authority to disallow funds, the regulation was invalid because the established tolerances were arbitrary. In November 1976, a similar ruling was made by the U.S. District Court for the Northern District of Georgia on action brought by the State of Georgia.

In a related action brought by Ohio, the U.S. District Court for the Southern District of Ohio in June 1976 agreed with the Maryland ruling citing that HEW had authority to withhold funds. That court, however, did not address the issue of the reasonableness of tolerances.

In March 1977 HEW removed the fiscal disallowance provision from its regulations in recognition of the above court decisions. As of June 1977 HEW had not reached a decision concerning the establishment of any alternative fiscal disallowance provision.

SCOPE OF REVIEW

We made our review at HEW headquarters, Washington, D.C.; HEW regional offices in Denver, Kansas City, New York, Philadelphia, and San Francisco; and in seven States--California, Colorado, Maryland, Missouri, Nebraska, New York, and North Dakota. In fiscal years 1975 and 1976 these States represented about 30 percent of the total AFDC caseload. Our fieldwork was conducted between April 1974 and March 1975 and focused on the results of quality control reviews through December 1974. Additional information was obtained at HEW headquarters on the results of quality control reviews conducted through June 1976.

CHAPTER 2

ELIMINATION OF CONTROVERSIAL FISCAL DISALLOWANCES

UNDER QUALITY CONTROL

The fiscal disallowance provision which HEW revoked in March 1977 had been incorporated into its quality control program by administrative regulation. Although the Social Security Act (42 U.S.C. 301 et. seq.) does not specifically authorize such action, it does not specifically preclude such action. HEW based its regulations on the Department's general authority to issue rules and regulations necessary to efficiently administer the AFDC program and were an attempt to deal with a basic question of the extent of the Federal Government's obligation to participate in improper or erroneous payments under Federal grant programs.

HEW AND STATE POSITIONS

HEW has taken the position that the Social Security Act requires HEW to exclude from Federal financial participation erroneous payments to ineligible recipients and overpayments to eligible recipients above reasonable limits established by the Secretary. The basis for this interpretation is provided by HEW in the preamble to proposed regulations for quality control included in the Federal Register of May 19, 1975 (40 F.R. 21737).

HEW stated that the act specifically authorized Federal financial participation only in specified payments as defined in the act and only in the amounts specified in each State's plan. Thus, the act does not specifically authorize Federal participation in payments to persons not eligible or in payments greater than provided for in the State plans. HEW expressed the view, however, that because the act authorizes HEW to establish rules for efficiently administering the AFDC program the Secretary of HEW can, therefore, permit Federal financial participation at a certain level of erroneous State payments below which he determines most States are incapable of reducing their error rates.

State officials, on the other hand, have argued that fiscal disallowances or sanctions are not appropriate in the quality control program. They emphasized that quality control was designed to improve AFDC program management and that error rates were never intended to measure program results. They stated that error rates are properly used only in the context of management information rather than as a basis for Federal financial penalties or disallowance of participation.

LEGAL ACTION INITIATED BY STATES

As of May 1976, 17 jurisdictions (16 States and the county of Los Angeles) had filed suit in three separate court actions against the Secretary of HEW challenging the legality of the AFDC fiscal sanction regulation. The suits contended that the regulation penalizes the States for errors that they cannot reasonably be expected to correct and that the terms of the regulations are unfair and arbitrary.

On May 14, 1976, the U.S. District Court for the District of Columbia reached a decision on the action brought by Maryland and 14 other jurisdictions. The court ruled in favor of the States by declaring the challenged regulation to be arbitrary, capricious, an abuse of discretion, contrary to and inconsistent with the act, and invalid. The court stated that under the Secretary's rulemaking power to assure efficient administration of the act, a regulation establishing a withholding of Federal financial participation based on a tolerance level is consistent with the act. However, the tolerance level must be reasonable and supported by a factual base.

The basis for the court decision was primarily that, because the tolerance levels were arbitrarily established at 3 percent and 5 percent without benefit of an empirical study, the regulation was framed in an arbitrary and capricious manner. The regulation as it concerned the tolerance levels was thereby inconsistent with the act, and therefore invalid, by unreasonably withholding funds intended to fulfill the act's purposes and by preventing the States from furnishing assistance as far as practicable, given the conditions of the State, it was therefore invalid.

Also, on June 25, 1976, the U.S. District Court for the Southern District of Ohio ruled on an action brought by the State of Ohio. The Court agreed with the ruling in the Maryland decision that HEW had the authority to establish a regulation for disallowances based on a tolerance level. However, the Court did not address the issue of the reasonableness of the HEW tolerances in this case because it was not presented with that question.

On November 10, 1976, the U.S. District Court for the Northern District of Georgia ruled on an action brought by the State of Georgia. The Court reached the same decision as was reached in the Maryland action.

On March 10, 1977, HEW revoked the fiscal disallowance provision of its quality control regulations due to the ruling on the Maryland and Georgia decisions. As of June 1977 HEW wa considering establishing new tolerance levels for fiscal disallowance in the future. However, no decision had been reached on specific action to be taken.

CONGRESS NEEDS TO ESTABLISH FISCAL CONTROLS

For the past several years, the House and Senate Subcommittees on HEW Appropriations have supported various Federal initiatives, proposed by HEW, aimed at controlling welfare costs through improved program management, particularly for reducing overpayment and eligibility errors. In May 1972 HEW informed the Senate Committee on Appropriations that it was studying fiscal sanctions as well as alternatives for controlling ineligibility and incorrect payments. In subsequent years HEW continued to provide information to the appropriations committees on the status of its quality control program. Appropriation committee reports during this period have continued to support plans to reduce welfare errors.

We believe that HEW's decision to impose fiscal disallowances encouraged States to implement programs to identify error rates and reduce errors. Early in 1973, 19 States that accounted for more than half the AFDC program payments did not have fully operational quality control programs. After HEW announced its intention to impose disallowances, all States, for the first time, completed the required review of sample cases for the April-September 1973 period and developed corrective action plans to address those problems causing errors.

Although error rates have been reduced, nearly $500 million in Federal funds is being misspent in the AFDC program every year. Some financial incentive is probably needed to assure that States continue to seek appropriate corrective action.

HEW has already encountered legal problems in attempting to administratively implement a financial incentive program. Also, several States have argued over the reasonableness of fiscal disallowances and the considerable impact that any form of disallowance could have on State program financing. Although HEW could establish a new financial incentive by regulation, we believe HEW would probably have to study the issue in some depth to be able to demonstrate to the courts' satisfaction that any such provision was not arbitrary and capricous.

For the reasons above, we believe that HEW will continue to encounter problems in attempting to establish any financial incentive. We believe that, under these circumstances, it would be more appropriate for the Congress to determine the control that would best provide the desirable financial incentive to States for reducing errors, and the Congress should enact appropriate legislation. Certain aspects of the current program as discussed below should be considered in establishing the basis for any incentive provision.

Tolerance levels

The tolerance levels established by HEW were not based on empirical data of the States' ability to control errors. Several States have said that they are unreasonably low. State officials also believe that HEW's tolerances do not properly consider State differences, and that any tolerances should reflect the following differences:

--States with large urban populations have more difficulty controlling errors than States with predominatly rural populations, primarily because of the extent of client misrepresentation concerning sources of income.

--The State's welfare regulation is the criterion for determining whether a case is in error. States with regulations that allow a great deal of flexibility in determining a recipient's grant amount would tend to have lower error rates than a State with less flexible rules.

Our study showed the need to consider the circumstances in each State because of the effect that a State's policies can have on the error rate. Two important differences are noted below.

Basic budgetary allowance--States can determine the basic budgetary allowance for shelter and utilities on the basis of standards or actual costs. States that use standards have less potential for errors in determining allowances. This is illustrated by comparing the incidence of error in New York and California. New York based the shelter allowance on rent schedules, which considered such things as the number of rooms and whether furnishings were included; California included the shelter allowance in a consolidated standard that only considered the number of persons in the grant. For the January-June 1974 period, the error rates attributable to basic budgetary allowance errors were 16.8 percent in New York and .2 percent in California.

<u>Percent of need met</u>--The extent to which the AFDC grant meets clients' recognized needs varies among States. The potential for error is partially related to the difference between the recognized need and the grant. The smaller the difference, the greater the potential for error, as illustrated:

	Missouri	Nebraska
Recognized need for a family of one adult and three children	$346	$354
Maximum grant authorized for above family	150	245
Unmet need	196	109

For quality control purposes, an error is reportable only if it affects the amount of the welfare payment by $5 or more. In each of the above States, an error resulting from unreported income would affect the payment only when it exceeded the unmet need. For example, an unreported $130 income could cause a reportable error in Nebraska but not in Missouri. Thus, because a larger amount of unreported income is required to cause an error in Missouri than in Nebraska, Nebraska's system is more error prone. Also, the potential for error in a State that pays 100 percent of need would be even greater than in either of the above States.

Differences such as those described above should be considered in determining the reasonableness of tolerance levels used as a basis for judging a State's performance. In February 1973, an HEW consultant in a report evaluating the tolerance levels stated that little is gained from setting a goal which is unrealistically high and which can be dismissed by State administrators as impossible to achieve. The consultant also stated:

> "Tolerance levels should be established as goals to be achieved or standards for comparison. The goals or standards should be reasonable--ones that some States are achieving currently and other States can reasonably be expected to reach.* * * Moreover, the tolerances should depend on the conditions of the systems to which they are applied and should be adjusted as these conditions change."

The consultant's report implied that tolerances should be based on empirical evidence of what States can be expected to accomplish, and we agree with that concept.

Payment vs. case error

HEW reports show both the payment error rates and the case error rates in each State for each reporting period. The case error rate, however, is the primary indicator used by HEW for determining the extent of error in the AFDC program and was to have been the basis for assessing any disallowances against States.

We believe that payment error rates are a more appropriate indicator of the extent of error in the AFDC program. We noted that, particularly with overpayment errors, the case error rate is on the average about three times greater than the payment error rate. For example, for the period January-June 1975 there were overpayment errors in 17.5 percent of the sample cases; however, the amount paid in error was 5.4 percent of the total payments. In our view, the use of case error rates overstates the degree of error in the AFDC program.

Further, case and payment error rates among the States are not necessarily directly related. For example, in several cases, States with equal payment error rates have widely differing case error rates. This situation is particularly important in determining the basis for any fiscal disallowance.

HEW procedures for determining the amount of any disallowance for a particular State were not based directly on the amount of erroneous payments. Rather, disallowance was to be determined on the basis of the State's case error rates, which are adjusted according to the State's ratio of payment error rate to case error rate. This method would result in disallowances based not only on the amount of erroneous payments but also on the incidence of error cases:

State	Error rates for disallowances (percent) Payment	Case
A	2.0	5.6
B	2.0	9.7

On the basis of HEW's formula for determining disallowance, State A would be disallowed about .2 percent and State B about .9 percent of total expenditures. The difference is due solely to the greater number of errors in State B. Although both States had erroneous payments equal to 2 percent of their total expenditures, State A would be disallowed about 10 percent of its erroneous payment while State B would be disallowed about 45 percent.

Since the primary objective of the quality control program is to reduce erroneous payments, we believe that the direct use of a payment error rate would be a better indicator of the States' accomplishments in reducing errors and would provide a more appropriate measure on which to base any disallowance.

On May 12, 1977, a bill was introduced in the House of Representatives (H.R. 7153) to amend the Social Security Act to provide legislation for taking fiscal disallowances. The proposed legislation addresses several issues discussed in this report. The legislation would establish tolerance levels based on the median error rate for all States, and would provide for use of a payment error rate rather than a case error rate. The bill would also provide for excluding errors that are procedural and do not necessarily affect welfare payments. This issue is discussed in chapters 4 and 5 of this report.

FISCAL CONTROLS PREVIOUSLY ENACTED BY THE CONGRESS

In recent years, the Congress has specifically established within the Social Security Act various penalties and incentives for improved administration and cost control for several aspects of the AFDC and Medicaid programs. 1/ It may be appropriate to establish similar legislation to provide incentives for controlling ineligibility and payment errors under the AFDC program. The following sections describe some of the major incentive provisions included in the Social Security Act for AFDC and Medicaid.

Medicaid--utilization control

As a result of congressional concern with continued reports of substantial overutilization of costly institutional care under Medicaid, a financial incentive provision was added to title XIX of the Social Security Act by the Social Security Amendments of 1972 to reduce Medicaid long-term care payments to States that do not comply with utilization control requirements. The amendment provided that, effective July 1973, there was to be a one-third reduction in Federal matching payments to a State for long-term stays in hospitals, nursing homes, intermediate care facilities, and mental institutions, unless the State demonstrated satisfactorily to HEW that it had an effective program of control over utilization of institutional services.

Medicaid--health screening for children

The Social Security Act requires States to provide health-screening and treatment services to all children eligible for Medicaid. In its report on the Social Security Amendments of 1972, the Senate Finance Committee said many States had either failed to or only partially implemented these services. The committee believed that establishing a penalty for failing to provide such services would underline the committee's intent that the States fully implement health-screening programs. The penalty provision included in the 1972 amendments required HEW to reduce AFDC payments to the States by 1 percent starting in fiscal year 1975 if a State failed to (1) inform all AFDC families of the availability of child health-screening services, (2) provide or arrange for such services, or (3) arrange for needed corrective treatment.

AFDC--child support enforcement

In January 1975 title IV-D of the Social Security Act was created to authorize greater Federal participation in

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1/Medicaid is a medical assistance program for low-income persons; it is authorized by title XIX of the Social Security Act and administered by HEW.

various activities related to child support and paternity. In its report on the legislation (S. Rep. 93-1356, Dec. 14, 1974), the Senate Finance Committee stated that because most States had not meaningfully implemented the provisions of existing law relating to child support, it believed that stronger legislative action was required. The legislation mandated more aggressive administration by providing various incentives for compliance and penalties for noncompliance.

The new legislation required that HEW annually audit each State's child support program established under an approved State plan to determine whether (1) the actual operation of the program conforms to requirements of title IV-D, and (2) a financial penalty should be imposed on a State for failing to have an effective program in operation. The penalty, which could have been assessed beginning with the quarter ended March 31, 1977, would reduce by 5 percent the amount of AFDC Federal support received by a State.

The Congress should consider the need to provide assurance that incentive provisions are implemented in an orderly and timely manner. For example, under the Medicaid utilization control incentives program, reductions in Medicaid payments were required beginning July 1, 1973, for any quarter a State failed to satisfactorily demonstrate compliance with the legislative requirements. HEW did not take necessary action to assure State compliance until the quarter ending June 30, 1976. Since that time HEW has acted to withhold funds from States which have not demonstrated satisfactory compliance. 1/ It should be noted, however, that HEW did not full comply with this legislative provision for nearly three years.

Also, beginning July 1, 1974, HEW was required to reduce payments to States that failed to meet the requirements for child health-screening and treatment services. Beginning June 1975 HEW notified States that had not met the requirements for such services that funds would be

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1/In June 1977 HEW announced reductions of about $142 million for 20 States because of unsatisfactory showings applicable to the quarter ended March 1977. HEW also recommended legislation to make the amount of reduction more equitable. We made a similar legislative recommendation in a report to the Chairman, Subcommittee on Oversight and Investigations, Committee on Interstate and Foreign Commerce, dated March 1, 1977 (HRD 77-56).

withheld. However, because of States' requests for reconsideration, as of May 1977 no funds had yet been withheld.

RECOMMENDATION TO THE CONGRESS

The Congress has, on several occasions, required that HEW provide various fiscal incentives to States to assure that certain provisions of the Social Security Act are properly and effectively implemented. To assure that States take appropriate action to keep payment errors in the AFDC program within controllable levels may require that HEW provide some similar form of fiscal incentive.

The Congress should determine the control that would best provide desirable financial incentives and should enact legislation to establish such incentives to effectively control AFDC payment errors. In developing such legislation, the Congress should seek HEW's assistance to determine an appropriate and feasible incentive. Such legislation should provide for using a payment error rate as the basis for setting goals for measuring States' accomplishments in reducing error.

CHAPTER 3

STATE ERROR RATES AND

CAUSES OF ERRORS

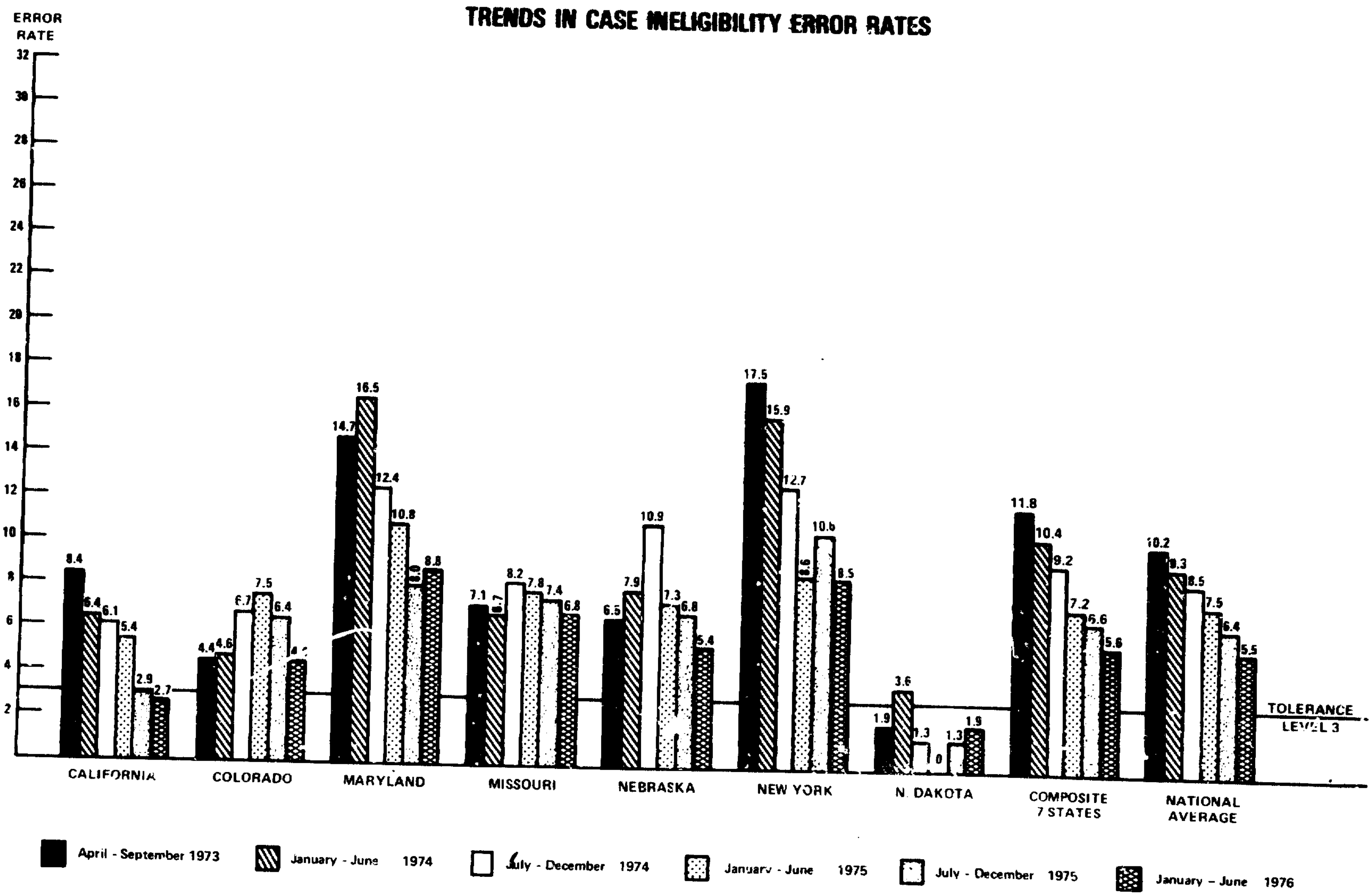
We reviewed the AFDC programs of seven States to determine how errors are caused and State actions to correct the causes of such errors. Of the seven States visited two achieved the ineligibility tolerances by the January-June 1976 sampling period. One of these States achieved the overpayment tolerance during previous sampling periods, but regressed during the 1976 period.

STATE ERROR RATES

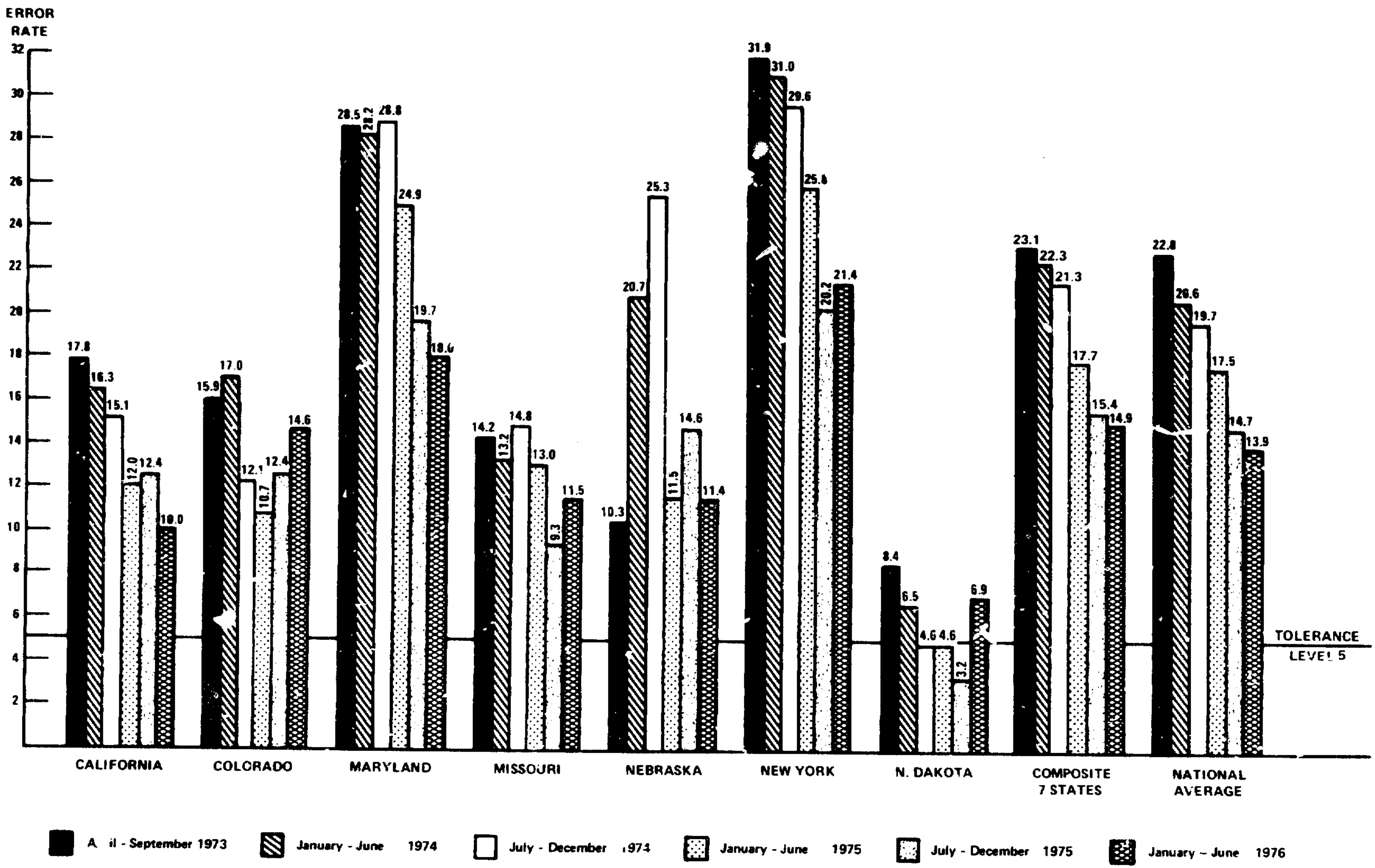
A case is considered to be in error if a welfare family is totally ineligible to receive payment during the review month or if there is an error of either an overpayment or underpayment of $5 or more. Case error rates are computed for each 6-month review period for ineligibility, overpayments, and underpayments. Under the fiscal disallowance regulation which HEW had intended to impose, any disallowances would be applied against only ineligibility and overpayment errors. Thus, we focused this report primarily on issues concerning those two forms of error.

The following graphs show error rates in the seven States for each review period through June 1976. We have included composite weighted averages for the seven States as well as national averages reported by HEW. The graphs show that as of June 1976 error rates in the seven States, and nationally, were generally well above the 3- and 5-percent tolerances established by HEW.

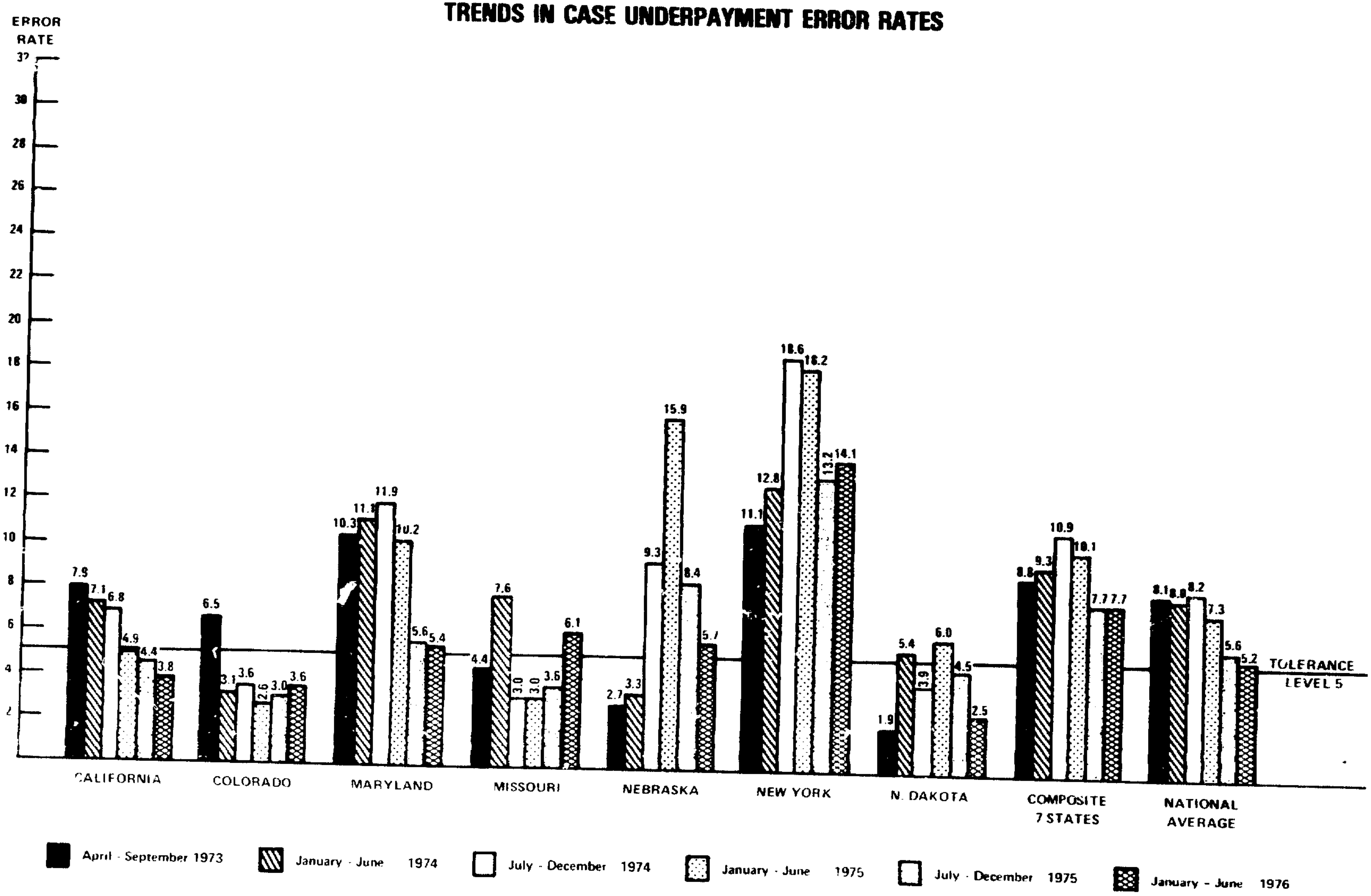
TRENDS IN CASE INELIGIBILITY ERROR RATES



TRENDS IN CASE OVERPAYMENT ERROR RATES

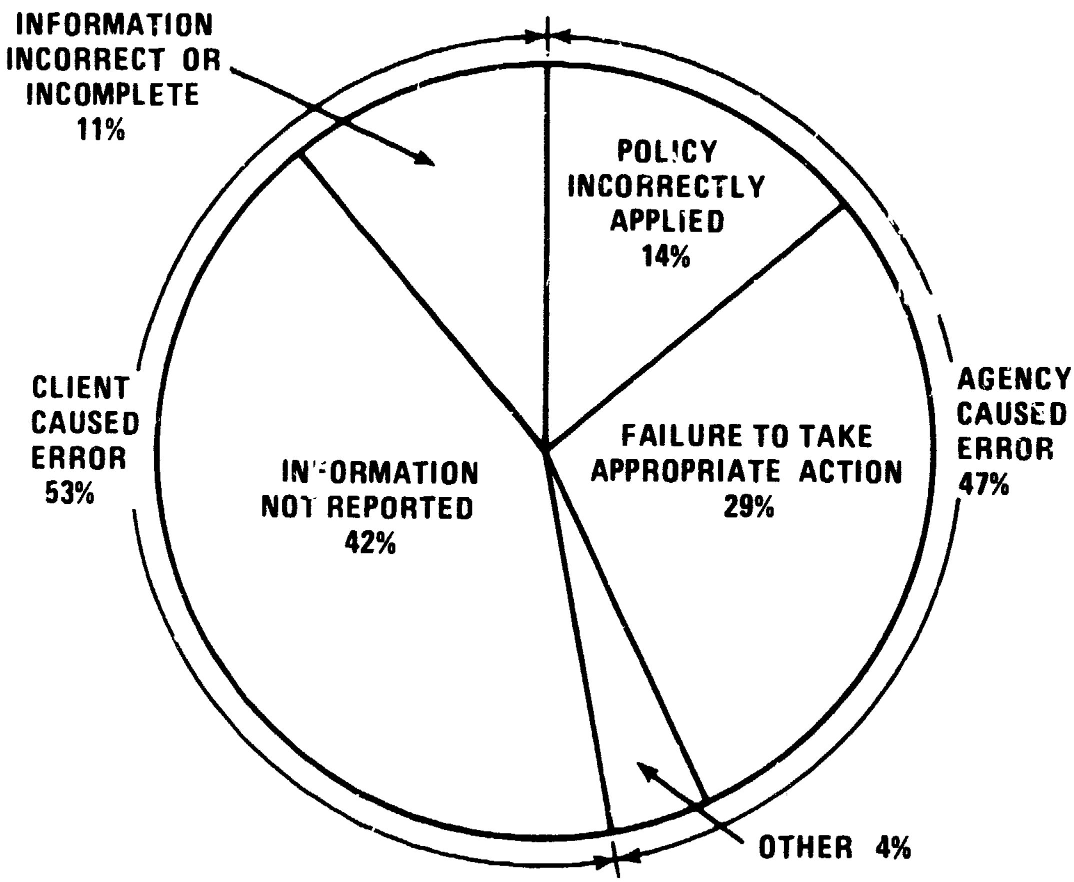


TRENDS IN CASE UNDERPAYMENT ERROR RATES



CAUSES OF ERRORS IN THE AFDC PROGRAM

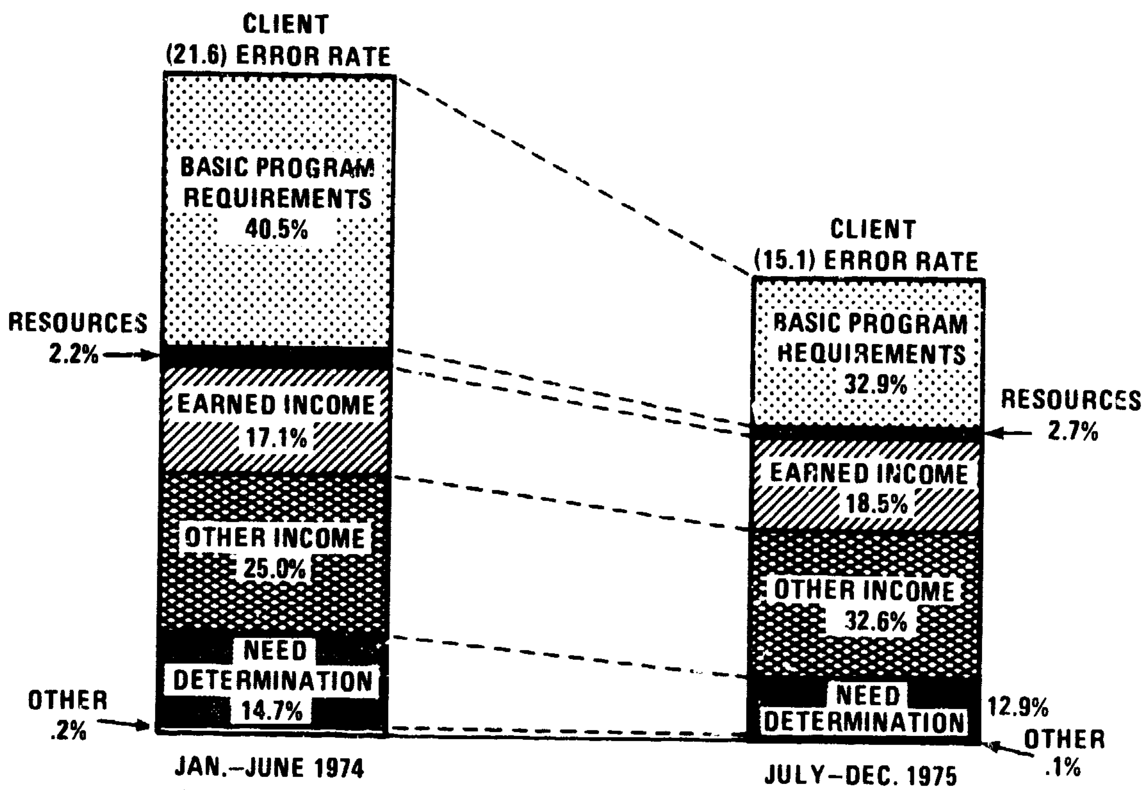
The quality control program identifies errors according to two categories--error responsibility and program area affected. Errors are classified on the basis of responsibility as either client- or agency-caused with subclassifications showing how the error occurred. The following chart shows for January-June 1974 (the time during which this review was initiated) the composition of errors on this basis for the States visited. Our analysis of more recent quality control reports showed that as of the July-December 1975 reporting period, while error rates had decreased, there was little change in the composition of errors.



Errors are also classified according to 45 basic eligibility or payment determination elements, grouped under the following 5 areas--basic program eligibility requirements (e.g., family composition), resources, income, grant or need determination, and other (e.g., computational errors). The following sections discuss the principal errors caused by the client (welfare recipient) and by the agency.

Client-caused error

HEW regulations define client-caused errors as those which occur because the information an AFDC recipient or applicant provides the State or county welfare department is incomplete or incorrect or because the information is not reported at all. The following graph shows where most client-caused errors occurred in the seven States in January-June 1974 and, for comparison, in July-December 1975: 1/



1/Overall error rate decreases for the 1975 period account for the smaller bar. The percentages total 100 percent in both columns and show the composition of errors for each period.

Although the following examples illustrate client errors causing ineligibility and overpayment, it should be noted that in many cases the information that the client provides or fails to provide may cause a lower payment than the person is entitled to.

Earned income - The largest client-caused error was inaccurate reporting of income, particularly earnings. Errors occured because welfare applicants or recipients

--indicated that they were not employed although they were employed,

--indicated when applying for welfare that they were employed but understated their earnings,

--did not report a change in earnings after going on welfare, or

--obtained employment after going on welfare and did not report it.

The errors caused by a misrepresentation of earnings are illustrated by the following actual cases.

Case A--unreported earnings. On January 28, 1974, a recipient declared that she had no income. The agency eligibility technician accepted the declaration and approved her family for a grant of $217 a month.

This case was selected in the State quality control sample for February 1974. The State reviewer's investigation disclosed that the recipient was employed from November 1973 through the review month under a different surname. The reviewer computed that the recipient had a net deductible income of $110 and cited the case for an overpayment error in that amount.

Case B--understated earnings. The agency calculated a family's grant on the basis of declared earnings of $2.00 an hour. The State quality control reviewer found that the client earned $2.50 an hour. The understated earnings resulted in an overpayment of $34 a month.

Case C--unreported change in earnings. The agency approved a family's grant for $174 a month. The agency determined the grant amount from information obtained from the client which showed that he earned $21 a week as a part-time bookkeeper.

The State quality control reviewer made a home visit and learned that the client had become fully employed three months earlier, but failed to report the change in employment status to the welfare agency. The reviewer computed the client's net deductible income based on the new earnings and determined that this family was ineligible for assistance.

Nonearned income

Welfare recipients receive nonearned income from such sources as child support payments, pensions and benefits, and income in kind. Errors in nonearned income occur primarily because a recipient fails to inform the welfare agency that resources are present and available for support. Thus the uninformed welfare agency cannot reduce a grant by the amount of nonearned income available to the family unit, and an error is cited when a State or Federal quality control reviewer obtains evidence of such income.

Case D--unreported support payments. A recipient stated on the welfare application that she had no other income. The recipient signed a form certifying that all her statements were true and indicating an awareness of the requirements to report income and of provisions relating to fraudulent receipt of assistance. She also stated that her ex-husband's address was unknown. The agency accepted the applicant's statements and determined the welfare grant accordingly for her family.

The State quality control reviewer located the absent father and ascertained that he had been making support payments of $150 a month, which constituted monthly overpayments in that amount.

Case E--unreported pensions or benefits. A recipient was not receiving social security benefits when she went on welfare and did not report the subsequent receipt of benefits to the welfare department.

The State quality control reviewer verified benefits with the Social Security Administration and learned that she and three of her four children each received $16.50 a month drawn on the deceased father's social security number. When confronted with this fact during a home visit by the State quality control reviewer, she denied any knowledge of it. Nevertheless, the reviewer rendered a decision of misrepresentation of facts and found the case to involve an overpayment of $66 in the review month.

Case F--unreported income in kind. A recipient declared on the welfare application that she paid all utilities. The agency accepted this statement and computed the grant accordingly.

During a home visit the State quality control reviewer asked the recipient to produce utility bills. The recipient could not produce any bills and stated that her boyfriend, who sometimes paid the utility bills, probably had them. She promised to have him contact the State reviewer but declined to reveal his address. The boyfriend did not contact the reviewer.

The State reviewer made several trips and calls to the recipient's home but was not able to contact either the recipient or the boyfriend. The reviewer found that the utilities were in the boyfriend's name on the public utilities company records and concluded that the recipient had received income in kind of $14. Thus the case was deemed to have an overpayment error of $14.

Unreported changes in composition of welfare family.

Many errors occur because the father is not absent from the home as required by welfare regulations or because a grant includes a child who is not eligible for assistance.

Errors occur primarily because a recipient fails to give the welfare agency correct information concerning the living arrangements of the children or does not report changes in circumstances concerning members of the family.

Case G--parent not absent from the home. A recipient declared on her welfare application that her spouse was not in the home. She stated that he had been deported to Mexico. The agency accepted this statement without verification and computed the grant accordingly for the recipient and her three children.

The State quality control reviewer contacted the State Department of Employment and learned that the recipient's husband was employed in the same city in which the recipient lived. The reviewer contacted one of the husband's recent employers and learned that his address was the same as the recipient's. A check with the Motor Vehicle Bureau also showed that his address was the same as hers.

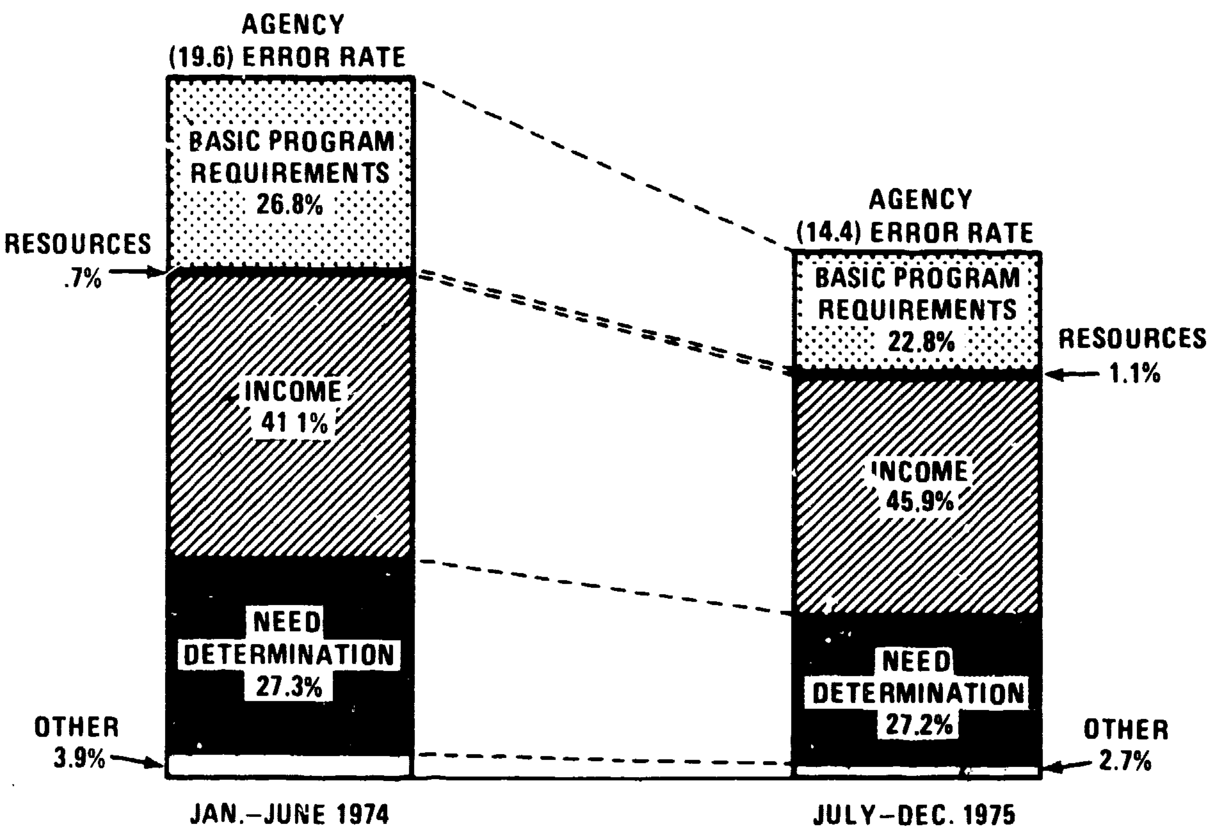
The reviewer interviewed the recipient and she repeated the statements made on her welfare application. However, on the basis of the evidence obtained the case was determined to be in error. Since it was on the assumption of deprivation and absence of the breadwinner that the family had originally become eligible, the case was declared totally ineligible.

Case H--ineligible child included in grant. A recipient declared on her welfare application that the children were living at home. The agency accepted the statement and computed the grant accordingly for a family of two adults and two children (father was incapacitated and was therefore in the grant).

The State quality control reviewer ascertained that the oldest boy was living away from home. Investigation revealed that the family with whom the boy was living had not received any money from his parents for support. Thus, the boy should not have been included in the grant of the family receiving assistance. This case involved an overpayment of $49 a month.

Agency-caused error

Agency-caused errors occur because welfare eligibility technicians incorrectly apply policy, apply the wrong policy, or fail to take appropriate actions. The following graph shows where agency-caused errors occurred during the January-June 1974 reporting period in the seven States reviewed, and also for the July-December 1975 reporting period: 1/



1/Overall error rate decreases for the 1975 period account for the smaller bar. The percentages total 100 percent in both columns and show the composition of errors for each period.

Determining income

The amount of a welfare grant is determined by deducting from the family's financial needs income that is available to the family. The complexity of welfare regulations makes the computation of net deductible income an involved mathematical exercise.

Agency errors occurred in determining income because eligibility technicians erred in computing the amount of income to be excluded from the grant or because they failed to consider information in the files. The types of circumstances that cause errors are illustrated below.

<u>Case I--computation error</u>. A Federal quality control reviewer found that eligibility technicians made a $10 error in subtraction when computing net nonexempt earnings.

<u>Case J--transportation costs computed incorrectly</u>. State and Federal quality control reviewers found that a technician had erred in determining the allowable deduction from income for work expenses related to transportation. The eligibility technician based the transportation deduction on mileage allowance. The reviewers found that public transportation was available to the recipient. The transportation deduction based on public transportation was $20 less than that computed by the technician.

<u>Case K--failure to correctly establish monthly income</u>. An eligibility technician computed a net income of $117.88 based on a recipient's declared earnings of $326.40 a month. The State quality control reviewer obtained the earnings directly from the employer and found that the recipient was paid biweekly and that the declared earnings had been based on the sum of her two most current paychecks.

The reviewer computed the recipient's monthly income by dividing one biweekly pay period by two and multiplying the result by 4-1/3 (average weeks per month). This produced a net income of $147.33 and consequently an overpayment of $29.

Determining need

Determining need involves determining a family's financial requirements for basic needs such as food, clothing, shelter, utilities, and incidentals. Agency errors occurred primarily in allocating shelter and utility costs. The following case shows a type of error that occurred.

Case L--housing costs not allocated. A seven-member family included four dependent children from the mother's former marriage. Her current husband was not supporting the four children, and they were the family members included in the grant.

The family's housing cost was $107 a month. The eligibility technician allowed $67 (the maximum) for the family's shelter costs without prorating the actual shelter cost, as required by the agency manual. The State reviewer prorated the housing cost among seven persons and computed a per person cost of $15.28 a month. Thus the four-member family should have been allowed $61.12 (4 x $15.28) for shelter allowance instead of $67. The case was cited for a $6 overpayment error. Agency error was cited because the eligibility technician did not follow stated policy.

Determining basic eligibility requirements

The primary cause of error in the basic eligibility requirements area was the failure to register persons for the work incentive program. This program was to provide certain AFDC recipients with job training and employment opportunities. Federal regulations require that all AFDC recipients register for training unless they are specifically exempted from registration. The following recipients are exempt from registering for the program:

--A mother or other relative who is caring for a child under 6 years of age.

--A child who is under age 16 or who is attending school full time.

--A person who is ill, incapacitated, or of advanced age.

--A person whose presence in the home is required because of illness or incapacity of another member of the family.

--A person living so far from a work incentive project that the distance would preclude his/her effective participation.

An error is detected by the quality control program when a case includes a nonexempt person who had not been registered.

CHAPTER 4

STATE ACTIONS TO CORRECT ERRORS

By using their quality control findings, States were to develop corrective actions which would deal with the problems causing errors in welfare payments. These problems varied from AFDC applicants' and recipients' misrepresentation of eligibility and grant entitlement information to complex regulations affecting administration at the county welfare department level. States have greatly increased their efforts to reduce the rate of error attributed to payments to ineligible recipients and overpayments and underpayments to eligible recipients.

HEW reported that the States collectively had taken 650 actions from April 1973 to June 1975. However, although error rates have declined, several States have not reduced error rates to the tolerances which HEW had established as target goals.

STATES' CORRECTIVE ACTIONS

Cases included in the quality control samples which are determined ineligible or for which an incorrect payment is made are referred to the local agency for individual corrective action. While correcting individual case errors is necessary, the ultimate goal of the quality control system is to identify and eliminate the causes of these errors.

The following were the most common types of corrective action taken in the seven States visited. These actions were based on the quality control reports for the April-September 1973 and January-June 1974 reviews.

Type of action	Number of States in which action taken
State policy revisions	7
Staff training	7
Increased client contacts or reporting	6
Increased verification	6

State policy revisions

Of all the corrective actions listed, State policy revisions were particularly effective in reducing errors. Some States recognized that errors occurred because of difficulties in applying too restrictive or complicated policies. The States tried to eliminate such errors by liberalizing certain requirements and by developing standards that are easier to administer.

We recognize that in most instances the State policy revisions were beneficial from an administrator's viewpoint. They simplified operating procedures and practices. However, many of the changes reduced errors by redefining what constituted an error. Examples of the types of revisions made are presented below.

Change in method of determining shelter allowance

Colorado's regulations required that a family's shelter allowance be based on actual costs. Because of this provision eligibility technicians made computational errors. Colorado revised its regulations to minimize the erro· potential by providing for a standard allowance. Under the revised regulations, a family's shelter and utilities allowance is based on the number of persons on assistance rather than on costs incurred. This regulation change was primarily responsible for reducing the State's aggregate error rate from 26.8 percent in September 1973 to 21.8 percent in December 1975. The nature and effect of this change is further discussed in chapter 5.

Caretaker payments

Missouri's welfare regulations provided for caretaker payments to individuals who met the State's definition of a "caretaker" and did not work over 20 hours a week. This policy was error prone, and the State removed the 20-hour restriction from its regulations.

Income tax regulation change

Welfare regulations in California formerly required a working recipient, as a condition of eligibility, to claim with his employer the maximum number of legal dependents for tax deductions. The purpose of this regulation was to discourage recipi ts from understating their exemptions to reduce their net i me and thereby increase their need for public assistance while developing a concealable source of one-time income in the form of a tax refund. Many errors occurred because the recipient did not claim the maximum number of tax exemptions allowable on earned income.

The State revised its regulations to eliminate the requirement that a recipient claim the maximum exemptions for tax purposes as a condition of eligibility. The revised regulation requires a recipient to claim only one exemption plus any other exemptions that are reasonable. Thus, understating exemptions will not cause an error if the recipient claims at least one exemption.

The above change was made although a State official had previously advised HEW:

> "Federal monitors found in the April-September 1973 sample that 20 percent of our ineligible case error findings were directly attributable to our income tax claiming regulations. This represents an $8 million a year Federal offset in terms of the fiscal sanctions associated with the Federal tolerance levels.
>
> "We know that by removing the ineligibility sanction from our regulations and adhering to IRS exemption claim allowances permitting employed persons to claim only themselves, we could avoid a substantial portion of future Federal ineligible case payment error findings. However, I do not believe this would serve the purpose of the quality control program of maintaining an effective, viable, and responsible welfare program while reducing errors."

<u>Changes in definition of in-kind income</u>

Nebraska's regulations provided that in-kind income include any payment made by a third party toward the recipient's costs for shelter, food, clothing, utilities, sundries, home supplies, garbage removal, and laundry. This policy was constantly misinterpreted and thus the regulation was revised. Payments toward the above costs are no longer considered income in kind unless a third party pays the full amount.

<u>Change in limit on resources</u>

North Dakota's regulations provided that a family was not eligible for an AFDC grant if its cash reserves exceeded

$350. The quality control reviewers were finding errors because of this provision. North Dakota amended its regulations in 1974 to increase to $1,000 the amount of cash reserves that a family can have before being ineligible for welfare.

Staff training

All States visited provided additional training to their eligibility technicians to reduce errors.

Training should improve employee skills, but it does not deal with the problems of worker turnover and high caseloads. California made a study to determine if there was a relationship between error rates and eligibility technician turnover and caseload. The findings were, in part, that

--high turnover was generally related to high error rates and

--heavy workload was moderately related to error rate.

The study identified several issues (such as hiring practices and educational requirements) which were being further pursued by the State.

Most State officials believed that eligibility technician inexperience (due to a high turnover rate) was a direct cause of some errors. The problem of worker turnover was attributed by some States to the low pay of eligibility technicians. Only one of the seven States (Missouri) had addressed this problem by increasing the pay level of its eligibility technicians equal to its social services workers. State officials believed this action would prevent losing experienced staff solely on the basis of salary.

Our analysis of Missouri's quality control reports shows that except for the decrease in caretaker payment errors (see p. 30) there has been little change in agency-caused errors since the beginning of the quality control program.

Increased client contacts and reporting

The information needed to compute the amount of an AFDC grant is furnished primarily by the client. State efforts to improve the reliability of such information involved requiring more face-to-face interviews with a welfare applicant or a recipient whose eligibility is being redetermined, and more frequent reporting of any change in circumstances by the welfare recipient. A requirement that the eligibility technician have personal contact with the welfare applicant was implemented by five of the seven States.

Errors due to nonreporting of client information in the seven States represent the most prevalent type of error, accounting for about 40 percent of the total errors. We believe that a basic problem in States' efforts to encourage welfare recipients to report information is the degree of client misrepresentation. Quality control reports prepared by the seven States showed that, collectively, there was indication of misrepresentation in about 75 percent of the client-caused ineligibility and overpayment error cases as of December 1975. These cases alone would account for an average combined ineligibility and overpayment error rate of nearly 10 percent.

Four of the seven States were implementing various actions designed to get people on welfare to report changes in their circumstances which affect the amount paid them.

California implemented a monthly AFDC eligibility and income reporting system. The system requires AFDC recipients to report changes in those factors affecting their eligibility and grant by completing a form and returning it to their welfare department. The recipients must return the form or their grant will be terminated. A county official said this had created a problem because 800 to 1,000 cases were terminated monthly in that county due to nonreceipt of the form. Most of the cases were subsequently reopened when the form was received.

Nebraska was testing a "check stuffer." This is a form sent with the welfare check on which the recipients report changes in their circumstances. The State was testing two methods of using the form. One method made returning the form mandatory regardless of whether any change was to be reported. The other method required the recipient to return the form only if a change had occurred. A comparative analysis was to be made of the two methods to determine which should be used.

North Dakota and Maryland were also using a check stuffer. The form was to be returned only when the recipient had changes to report. No information was available during our review on how many recipients were returning the form when required.

Increased verification of income

Problems in nonreporting or incorrect reporting of income are also major causes of errors. Although the seven States have taken measures such as described below to control errors related to income, such errors have not been reduced to the same degree as other categories of error. Thus, income-related errors represent an increasing portion of the total error rate in these States. In September 1973 such errors accounted for about 38 percent of the errors; by December 1975 they accounted for 49 percent of total errors.

Earnings verification system

Three States took actions to enable eligibility technicians to verify earnings by using records of earnings maintained by States for unemployment compensation programs. In one State, this system had been in effect since 1971. However, State officials said these records were of limited usefulness for the reasons below.

First, the State employment records do not contain information on certain categories of employees such as State or local government workers. Second, State employment security agencies get earnings reports only on a quarterly basis and thus cannot provide earnings data for a given month. Third, information from these State agencies is 3 to 6 months old when it becomes available. Because of the time lag involved in obtaining earnings data, it cannot be used for validating current earnings and thus cannot aid eligibility technicians when a person applies for welfare. Such information can, however, be used during the redetermination process in verifying past earnings and thus provide a basis for further investigation.

Verification of pensions and benefits

The Beneficiary Data Exchange System enables States to verify pensions and other benefits through the use of information available in Social Security Administration files. Five of the seven States were making an effort to use the system. However, using this system for AFDC clients is a long-term corrective action. Several States that attempted to use the system had difficulty because it operates from social security numbers. For example:

--County welfare departments do not have social security numbers on all adult AFDC recipients.

--Many recipients are children who do not have social security numbers.

In July 1975 HEW revised its regulations (45 C.F.R. 206.10) to require that welfare recipients provide their social security number to welfare agencies as a condition of eligibility, or obtain a number if they do not have one. This should help to alleviate the problems noted above.

EFFECT OF STATES' CORRECTIVE ACTIONS

The following table shows changes in error rates for those eligibility or payment determination categories that were primarily responsible for errors in the States visited:

ERROR RATES IN MAJOR CATEGORIES FOR SELECTED PERIODS

ERROR CATEGORIES	CALIFORNIA			COLORADO			MARYLAND			MISSOURI			NEBRASKA			NEW YORK			N. DAKOTA		
	APR.-SEP. 1973	JULY-DEC. 1974	JULY-DEC. 1975	APR.-SEP. 1973	JULY-DEC. 1974	JULY-DEC. 1975	APR.-SEP. 1973	JULY-DEC. 1974	JULY-DEC. 1975	APR.-SEP. 1973	JULY-DEC. 1974	JULY-DEC. 1975	APR.-SEP. 1973	JULY-DEC. 1974	JULY-DEC. 1975	APR.-SEP. 1973	JULY-DEC. 1974	JULY-DEC. 1975	APR.-SEP. 1973	JULY-DEC. 1974	JULY-DEC. 1975
	PERCENT OF SAMPLE CASES																				
PERSONS IN GRANT	4.8	2.3	1.5	2.5	.4	2.4	7.7	5.3	4.6	3.3	2.8	1.9	2.4	2.6	1.3	7.8	7.1	6.1	.6	–	–
EARNED INCOME	5.4	3.8	3.6	9.9	6.5	5.3	7.5	9.7	9.2	2.5	3.9	3.7	12.0	13.8	3.9	6.7	6.5	5.3	4.5	1.3	1.3
OTHER INCOME	4.8	6.9	2.8	.9	3.6	3.0	1.7	.9	.7	.3	.5	.7	.3	2.2	.6	.7	1.2	.6	–	.7	.6
FATHER IN HOME	.8	.7	.2	.4	1.7	1.7	3.5	3.1	2.2	4.7	4.5	2.7	.7	3.8	3.2	10.4	9.6	7.3	.6	–	.6
BASIC BUDGETARY ALLOWANCE	.6	.2	.2	9.0	.7	.6	8.0	10.9	.4	1.3	1.8	1.9	2.4	5.1	.3	14.7	16.8	9.3	1.3	.7	–
WIN PROGRAM	–	3.2	1.3	2.6	2.9	2.6	6.9	4.6	3.5	–	4.7	.1	–	.6	1.0	8.4	4.6	2.8	–	.7	–
PENSION/BENEFITS	2.3	1.9	3.2	1.2	1.0	1.2	2.7	3.0	2.0	3.0	2.5	3.9	.3	3.5	4.2	2.6	3.4	3.8	.6	–	–

At the time of our review in the seven States, the corrective actions taken by the seven States had slightly reduced the overall error rates between the April-September 1973 and July-December 1974 review periods. However, in some instances the corrective actions taken had greatly reduced errors in certain individual categories of eligibility or payment determination.

Two of the largest reductions that had occurred at that time involved State policy changes, which we believe have a limited effect in directly reducing welfare payments. (See p. 30.) For example, the Colorado policy revision authorizing standard allowances reduced the error rate in basic budgetary allowance from 9.0 percent during the April-September 1973 review period to .7 percent during the July-December 1974 review period. The Missouri policy revision, which eliminated the restriction on the number of hours a caretaker could be employed, reduced caretaker payment errors from 6.4 percent during the April-September 1973 review period to 1.4 percent during the July-December 1974 review period.

A more substantial reduction in error rates occurred in the next two review periods after our field visits. We have not determined the extent that actions with limited impact on reducing welfare payments have contributed to more recent error reductions. However, because such actions may have a substantial and immediate effect in error reductions, we believe it is important that they be considered in determining the extent error reductions are producing reduced welfare payments.

CHAPTER 5

QUALITY CONTROL PROGRAM

ACCOMPLISHMENTS OVERSTATED

Since the quality control program was initiated in 1973, HEW has continually overstated the program's accomplishments. Savings estimates resulting from error reductions were not based on valid statistical projections and included actions which did not necessarily produce direct savings in welfare payments. HEW did not consider the administrative costs that would be associated with implementing corrective actions. In addition, States generally did not conduct cost effectiveness studies before starting corrective actions, although required to do so by HEW.

OVERSTATED SAVINGS ATTRIBUTED BY HEW TO QUALITY CONTROL

In April 1974 HEW officials, testifying before the House Subcommittee on Labor and HEW, stated that while HEW had not made a cost-benefit analysis of the quality control program, the benefits were considered about 15 times greater than cost. This estimate was based on total Federal and State costs of about $41 million yearly for operating the quality control program and estimated benefits of $607 million yearly. The benefits estimate was based on the premise that the States would reduce their error rates to the tolerance levels by July 1, 1975.

More recent savings estimates attributed by HEW to the quality control program have also been based partly on assumptions that have not been validated. For example, in December 1976 HEW reported that between January 1974 and June 1976 the quality control program had saved about $1 billion in Federal and State funds. The savings were not based on valid statistical projections and did not consider the costs associated with operating the quality control program and implementing corrective action. We further question the validity of such savings because of HEW's assumption that all reductions in case error rates involve a related dollar savings. Our review showed that reductions of certain kinds of error would not necessarily produce savings. We believe that the savings that have been reported by HEW have considerably overstated the savings that could reasonably be attributed to a reduction in error rates.

Failure to determine whether the reduction in the case error rate was statistically significant

HEW savings are based on comparisons of percentages of error (case error rates) in one period with those in prior periods. These percentages are estimated from welfare case samples. Estimates obtained from samples are subject to random variation. As a result, any difference in error rates between two periods may be statistically significant or caused solely by the random selection of sample cases.

For example, HEW reported that the program had generated savings of $71 million during the first 6 months of 1974. HEW determined these savings by comparing the results of the April-September 1973 and January-June 1974 periods for each State and computing a savings based on each State's average error cost for any reduction in case error rates attributed to ineligibility and overpayment. HEW, using the same method, estimated additional savings of $62 million during the second 6 months of 1974.

Between the April-September 1973 and January-June 1974 periods, case error rates for ineligibility had declined in 29 States and for overpayment in 34 States.

HEW attributed savings to error rate reductions in each of those States regardless of whether the change was statistically significant. Also, HEW did not consider any States which increased case error rates. We found that the ineligibility and overpayment error rate decreases were statistically significant in only seven and eight States, respectively. In addition, there were statistically significant ineligibility error rate increases in five States and overpayment rate increases in three States.

Our analysis showed that after including States with increases in error rates and considering only those States with statistically significant changes, the estimated savings computation using HEW's method would be $26 million for the period January-June and $42 million for the period July-December 1974, compared with HEW estimates of $71 million and $62 million, respectively.

These examples show the effect that our suggested method can have on estimated savings computations. In any given time period, the extent this method would effect HFW's determination of savings would depend on the degree of error reduction or increase in each State. The greater the change in either direction, the greater the likelihood that the change could be statistically significant.

Invalid assumption that all reductions in case error rate involve a savings

HEW's method of computing savings has also assumed that there is a direct relationship between a reduction in case error rates and savings to the program. This assumption is incorrect because, as demonstrated below, a State can eliminate certain errors which will not necessarily produce direct savings in welfare payments.

Elimination of errors due to nonregistration for work incentive program

Federal regulations require, as a condition of eligibility, that all AFDC recipients register for work incentive training unless they are specifially exempted from registration. Failure to get persons registered was a major cause of error in five of the seven States.

States with the registration problem made a major effort to inform eligibility technicians of the registration requirement. In effect, this corrective action was designed to get persons registered for the program. Many cases would therefore continue to receive welfare payments and no immediate cost reduction would result from it.

Missouri advised HEW that it would not report nonregistration errors after the January-June 1974 period. State officials contend that such errors should not be counted because there is no dollar savings when they are corrected. As of March 1977, this matter was unresolved.

The effect of nonregistration errors was also questioned by Maryland officials. They stated that quality control applied the strictest interpretation in determining error and, therefore, counted as errors unregistered employed or pregnant clients among the mandatory clients who must register for the work incentive program. They stated that to include such cases in a public disclosure as an "error rate" was to seriously distort the public's impression of how many ineligibles were receiving public assistance.

It is thus evident that little direct savings can be attributed to eliminating nonregistration errors. We recognize that these errors should receive the States' attention, but no direct savings can necessarily be attributed to their reduction.

Elimination of errors in basic budgetary allowance

Budgetary allowances pertain to those items of basic need (food, clothing, shelter, fuel, utilities) for which allowances have been established. Allowances are established either on the basis of individual need or on predetermined standards. Three States had numerous errors in basic budgetary allowances, primarily in shelter and utility allowances. Quality control reviews disclosed errors in these States because

--the amount of rent paid was reported incorrectly on the application,

--the recipient's rent increased or decreased and it was either not reported to the welfare department or was reported and not acted on, and

--the agency and the recipient disagreed about whether the rental charge included the cost of utilities.

All these States have reduced or are planning to reduce allowance errors by including the grant amount for shelter and utilities as a standard allowance based on the number of recipients in the grants. The following case demonstrates how this corrective action can eliminate errors but does not produce any direct savings.

Case M--A recipient declared that there were six household members and that the house payment was $97 a month plus utilities. Only four household members were on public assistance. The agency prorated a monthly cost of $64.68 for shelter and $13 for utilities for the four persons on public assistance and based its grant on these costs.

The State quality control reviewer found that the house payment had increased to $102 and that the payee's daughter-in-law had moved into the household. He recomputed the pro-rata share of rent and utilities for the four persons on assistance on the basis of the increased house payment and the fact that there were now seven household members. The revised payee's cost was $58.28. Since this was $6.40 less than the amount included in the grant by the agency for such costs, the case was determined to be in error.

The State in which this error occurred acted to eliminate allowance errors by determining the amount to be included in the grant for all items of basic need, including shelter and utilities, on the basis of a consolidated standard. The change in circumstances that caused the error cannot cause an error under this method of determining need. In effect, the State has reduced its error rate by redefining what constitutes an error. For instance, this household was receiving a welfare grant under the old system of $223 a month, determined as follows:

Basic needs	$145.00
Shelter	65.00
Utilities	13.00
Total	$223.00

Under the new system, this household was entitled to $240.00 a month. Thus, no direct savings can be attributed to the case error rate reduction that occurred because the State changed to standard allowances.

Need to assure that corrective actions are cost effective

HEW's reported savings have not considered the overall cost of State actions to reduce error rates. HEW has not identified with its savings estimates the administrative costs that States would have incurred in implementing corrective actions. Also, HEW has not included HEW and State costs for operating and monitoring the quality control program.

Likewise, the States visited were implementing corrective actions without determining their cost effectiveness in accordance with HEW requirements. HEW's fiscal disallowance provision was designed as an incentive for States to use the information obtained from quality control reviews to take corrective actions that would subsequently reduce their error rates. As a result, States increased their efforts after the April-September 1973 base review. However, all the States visited were taking corrective action with little knowledge of the cost effectiveness of their actions.

HEW regulations state that the case error rate determines whether a State will be subject to reductions in Federal financial participation. Thus, a primary consideration in planning and implementing corrective actions was the extent to which these actions would eliminate case errors.

Although State officials doubted that HEW tolerance levels of 3 percent for ineligibility and 5 percent for overpayments could be attained with cost-effective corrective actions, none of the seven States had determined the cost effectiveness of any of the actions taken.

Some of the reasons given by the States for not determining cost effectiveness were:

--HEW's fiscal disallowance provision caused States to emphasize reducing errors.

--The time established for imposing disallowances was too short to test corrective actions before they were implemented.

--HEW made no followup inquiry to determine whether such studies had been made.

State officials said that many errors disclosed by the quality control reviews can be prevented only by requiring that the eligibility technician make as extensive an investigation as the quality control reviewers.

They doubted, however, whether it was cost effective for them to do so. Some comments made in this regard follow:

--An official from Sacramento County, California, stated that if home visits and third party verification are required to determine eligibility, approximately 1,000 additional eligibility workers would have to be hired and trained.

--An official from Maryland stated that quality control discovers errors by using practices that are too expensive and time consuming for the local welfare agency.

--An official from Missouri questioned whether the cost of staff increases would be offset by savings attributable to a reduction of errors.

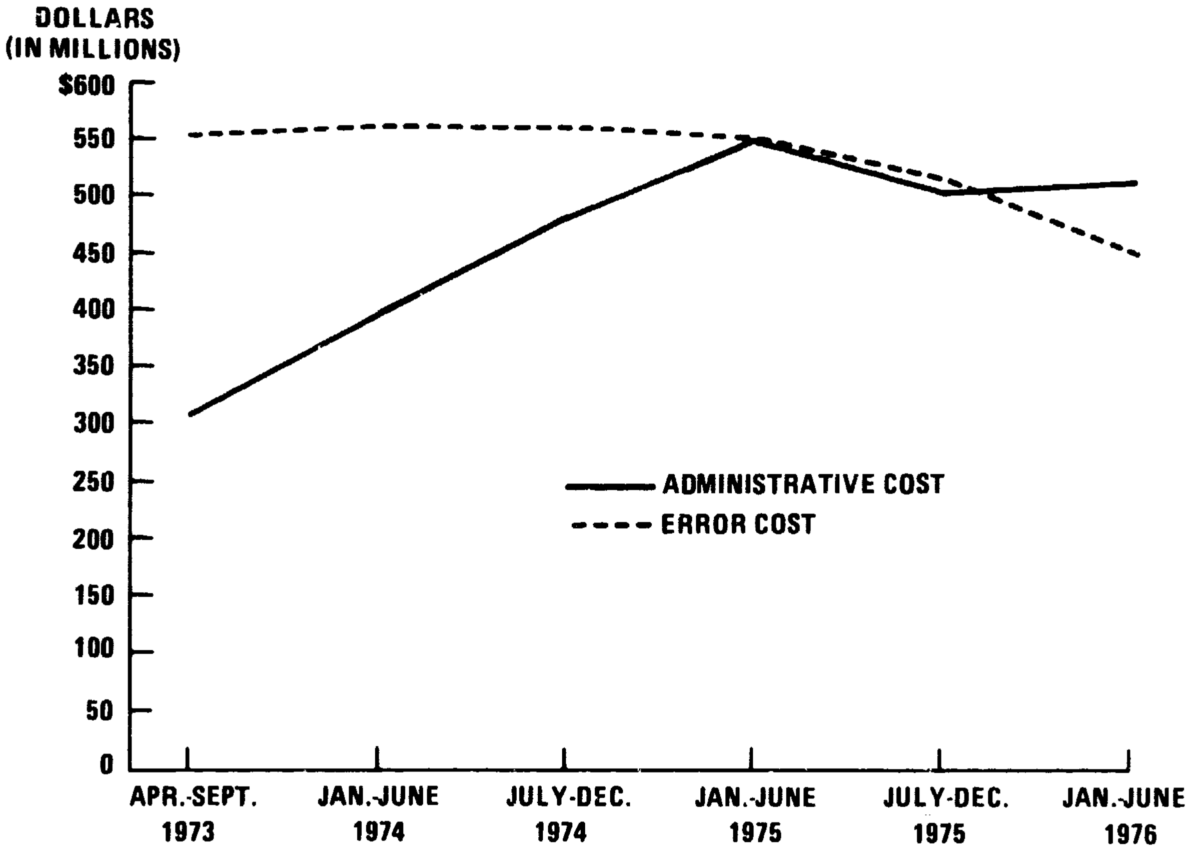
--An official from New York stated that client-caused errors could not be totally controlled unless all cases were completely field investigated with access to all information necessary to determine client eligibility. The officia doubted that such extensive work would be cost effective.

The subject of cost-benefit studies was discussed in an HEW consultant's February 1973 report on the quality control program. The report stated that if the corrective action is basically simple and can be put into effect at little or no cost, the decision to implement the action might reasonably be made on the basis that its effect is promising. The consultant also stated that more extensive corrective actions should be tested before full implementation (even when the theoretical advantages appear so evident that implementation on a statewide basis appears a foregone conclusion) to provide a basis for anticipating costs, benefits, and administrative problems.

HEW has recognized the need for such studies by requiring that States perform such analysis in conjunction with their corrective action program. HEW's quality control manual states that a thorough cost-benefit study of corrective actions is necessary for management to determine whether to commit agency resources for detailed development and implementation of any particular action. The manual also includes information concerning the scope and nature of the analysis needed to assess the economic feasibility of corrective actions.

We believe that determining the administrative costs associated with quality control and corrective action is particularly important in view of the increasing administrative costs of the AFDC program. In fiscal year 1974, total costs for State and local administration for the AFDC program were about $700 million. In fiscal year 1975 administrative costs were more than $1 billion, an increase of about 48 percent in a year. During the same period, however, the cost attributed to welfare payment errors remained relatively stable at about $1 billion.

This cost trend is further demonstrated by the following chart which shows the total administrative and error costs nationally for each of the six quality control sampling periods through June 1976. 1/



1/Data obtained from HEW except error costs that were not reported prior to 1975. We estimated earlier figures on the basis of HEW quality control data.

SAVINGS SHOULD BE RECONSIDERED

Corrective actions taken by the States have, in our opinion, produced some savings in the welfare program and should be continued. However, we believe HEW and the States must consider the costs associated with these actions to assure the maximum savings potential. We also believe that HEW's method of computing savings is statistically unreliable and based on invalid assumptions, producing reports which can distort the amount of savings attributed to the quality control program and thus detract from the credibility of those bona fide program accomplishments.

We found that about one-third of the error reduction through December 1975 for the seven States reviewed occurred in the categories of work incentive registration and basic budgetary allowance. Although we have not determined the extent that these items have contributed to the total error reduction in other States, we believe that this demonstrates a situation of sufficient magnitude for HEW to reconsider the basis for determining savings.

RECOMMENDATIONS TO THE SECRETARY OF HEW

We recommend that to improve the administration of the quality control program, the Secretary of HEW:

--Revise HEW's basis for determining accomplishments resulting from States' efforts to reduce errors. HEW should determine savings on the basis of valid statistical projections and should consider only those error reductions that directly result in reduced program costs. Such savings should also account for the increased administrative costs, where applicable, of implementing corrective actions.

--Base reporting of State errors on dollar amounts rather than on case error rates.

--Assist States in identifying corrective actions that can be demonstrated to be cost effective.

HEW COMMENTS AND OUR EVALUATION

In a letter dated December 3, 1976, HEW commented on our recommendations. (See app. I.)

HEW concurred with our recommendation for revising the base for determining program accomplishments, with some qualifications. HEW agreed to include tests of statistical significance in future savings calculations but added that its method may differ from that recommended by us. HEW said that tests of significance would be performed on national rates only because the national savings figure would include error rates for all States, including those where error rates increased as well as decreased.

In this regard, we disagree with HEW and believe the approach suggested in our report to be more appropriate. The savings calculation is based on a comparison of error rates between periods for each State. Since the quality control case samples are taken separately from each State's caseload rather than a national caseload, we believe that tests of significance should be performed for each State as discussed on p. 39.

HEW agreed in principle that the determination of savings should consider the impact of those error reductions that do not directly result in savings and the administrative costs that have been incurred to achieve such reductions. HEW said, however, that calculating true net savings may be impractical, given the present quality control program and State accounting system capabilities. HEW said it will assess several States to determine whether it is possible to capture such data. Also, HEW has a $500,000 study underway to examine the cost effectiveness of corrective actions. Until these studies are complete, HEW believes its method of calculating savings should be continued.

We recognize that these studies are directed toward obtaining a truer measure of actual savings resulting from error reduction and should be responsive to the issues raised in our report. In the meantime, however, we believe that savings reported by HEW should be qualified to show that they do not necessarily represent that level of reduction in welfare costs.

HEW said our report's emphasis on cost effectiveness tends to confuse and prevent a better understanding of the quality control program and its positive accomplishments. HEW contends that the sharp decline in error rates and erroneous payments indicates that corrective actions have been cost effective.

We recognize the many ways the quality control program has had positive accomplishments. As we have stated previously, States have directed greater attention to reducing the incidence of errors; since the program began, error rates have declined considerably. Furthermore, the program has provided HEW and the States with substantial data regarding the extent and nature of errors in the States' welfare programs. HEW has also received extensive reporting on States' efforts to reduce the incidence of error.

We believe, however, that the issues presented in this report raise serious questions about the relationship between error reduction and reduced program costs. The examples in this report show that certain corrective actions can have a substantial impact on error reduction but have little direct impact on reduced cost.

HEW's method of determining savings attributed to the quality control program detracts from the credibility of the accomplishments that have been achieved. HEW and the States should concentrate on determining the results of specific corrective actions to identify which actions can be most effective in reducing program costs, and the extent to which true savings can be achieved.

In this regard, better enforcement of HEW requirements regarding cost benefit studies is needed. HEW's instructions to the States on corrective action planning require that a thorough economic evaluation be conducted for each proposed action which will identify and consider all continuing and one-time costs and benefits to determine its economic feasibility. As we stated previously, however, we recognize that there are situations when corrective actions may involve little or no additional cost and the economic feasibility of such action may be readily apparent.

HEW said that it strongly rejected the notion that a cause and effect relationship exists between the implementation of quality control and the near doubling of State and local administrative costs. We have not stated that such a relationship exists. Our basic concern is that administrative costs attributable to the quality control program be considered when measuring the savings resulting from such a program.

We highlighted the large increase in AFDC administrative costs to emphasize the need for HEW to determine the extent such an increase could be attributed to the corrective actions taken by the States. As previously stated, HEW has undertaken a study of the cost effectiveness of corrective actions costing an estimated $500,000. Two major questions to be addressed in that study are the extent to which administrative costs have risen as a result of the States' endeavors to reduce errors and whether such costs could exceed savings. HEW said that insufficient data was available from the corrective action process to answer such questions.

HEW also addressed this question in connection with a $223,000 contract issued in September 1976 for an analysis of AFDC administration and management. HEW said that administrative efficiency had been brought into question because of the substantial error rates and soaring administrative costs. HEW added that errors and administrative costs are not necessarily independent; one untested hypothesis is that the quality control program, implemented to reduce errors, has substantially increased administrative costs. Thus, it seems evident that HEW is concerned about the relationship between administrative costs and error reductions.

HEW concurred with our recommendation to base its error reporting in dollars rather than case errors and agreed to use this approach in future reporting.

In response to our recommendation that HEW assist the States with identifying cost-effective corrective actions, HEW said that it is constantly striving to make its work in this key area more effective. HEW cited several ways it had provided States assistance, such as issuing publications, holding workshops, and engaging contractors. HEW said it had issued several documents to States describing proven cost-effective techniques for reducing errors, and it encouraged States to adapt these techniques to their own error problems.

These publications describe various practices implemented, usually by one State. In many cases, these publications discuss management techniques that have recently been adopted and do not provide any evidence of their cost effectiveness in practice. We recognize the value of providing a forum for ideas among States. However, each State is independently operating its own welfare program, many aspects of which differ among States. Thus, techniques adopted by one State may not necessarily be readily adaptable to other States.

We believe that HEW should focus on those States having the greatest difficulty in reducing errors. In general, States with larger welfare caseloads have tended to have the greatest incidence of error, and thus account for a substantial share of the error costs of about $500 million in Federal funds. HEW should concentrate on identifying corrective actions that have proven effective in other States and providing assistance in implementing such action in those States which have not been as successful in reducing errors.

APPENDIX I

DEPARTMENT OF HEALTH, EDUCATION, AND WELFARE
OFFICE OF THE SECRETARY
WASHINGTON, D.C. 20201

December 3, 1976

Mr. Gregory J. Ahart
Director, Manpower and
Welfare Division
United States General
Accounting Office
Washington, D. C. 20548

Dear Mr. Ahart:

The Secretary asked that I respond to your request for our comments on your draft report entitled, "Problems in Reducing Erroneous Payments through Quality Control". The enclosed comments represent the tentative position of the Department and are subject to reevaluation when the final version of this report is received.

We appreciate the opportunity to comment on this draft report before its publication.

Sincerely yours,

Charles Miller
~~John D. Young~~
Acting Assistant Secretary, Comptroller

Enclosure

COMMENTS OF THE DEPARTMENT OF HEALTH, EDUCATION, AND WELFARE ON THE COMPTROLLER GENERAL'S REPORT TO THE CONGRESS OF THE UNITED STATES ENTITLED "PROBLEMS IN REDUCING ERRONEOUS PAYMENTS THROUGH QUALITY CONTROL" B-164031(3) dated July 30, 1976.

GAO Recommendation

> That HEW revise its basis for determining accomplishments resulting from States' efforts to reduce errors by determining savings on the basis of valid statistical projections and considering only those error reductions that directly result in reduced program costs. Such savings should also consider the increased administrative cost, where applicable, of implementing corrective actions.

Department Response

We concur with this recommendation with some qualifications. Specifically, the GAO's first recommendation consists of three separate sub-recommendations, which we address individually:

1. Determining Savings

The Department's present practice is to report accomplishments resulting from the AFDC QC program in terms of reductions in case errors (ineligibility, overpayment) and the dollar savings that result from these error reductions.

The GAO recommends that before HEW calculates dollar savings from reductions in error rates, a test of statistical significance be applied to the change in error rate to see at what level (99.9, 95.0, 90.0%, etc.) the change is significant. In the past, this sort of testing has not been done. The Department will in the future calculate savings using statistical tests of significance. The method may differ from that recommended by GAO. It will involve calculations of statistical variation for each State, regardless of the direction of the change, and tests of significance will be performed on national rates only. This is the most accurate approach because the national savings figure will include error rates for all States including those where error rates increased as well as decreased.

2. Calculating "Net" Savings

GAO recommends considering only those error reductions that directly result in reduced program costs i.e. savings minus the administrative costs of the corrective actions which reduced errors and savings which omit the error reductions caused by policy changes which correct an error but do not necessarily change the total outflow of program dollars.

In principle we agree with this recommendation..

We should know not only what savings have been achieved due to reductions in erroneous payments but also what administrative costs (or savings) were incurred simultaneously. We also should know which changes in policy reduce errors and which of these have program cost impacts and which do not.

However, calculating true net savings may be impractical given the present QC system and State accounting system capabilities.

Specifically, the cause-effect relationship between multiple corrective actions and changes in a specific error element is complex. It is difficult to isolate the impact of a single policy change on an error element when this change was only one of a number of corrective actions addressed at the problem. To do this would entail delineating the numerous corrective actions taken in terms of those that impact error rates and those that do not; and for those that do impact errors, to further determine which have program cost impact and of what magnitude. All of this then would need to be related to the administrative costs of each individual corrective action. Neither the present QC system nor State accounting systems are capable of this. We seriously question if any practical QC system can ever monitor to the needed level of precision the cause-effect linkages between a specific corrective action and error element. This is because of the multitude and varied corrective actions focused on a single error element. In this context, therefore, attempting to segregate out a particular corrective action, i.e., policy change and determine its impact on an error to the exclusion of all other corrective actions and their interrelationship may not be possible short of a controlled laboratory setting.

However, the Department will undertake an assessment in several States to determine whether it is methodologically and practically possible to capture such data and whether, in fact, the end result will significantly alter reported savings.

In addition, SRS already has a study underway in 16 States which will examine the cost-effectiveness of corrective actions in terms of the cost of the corrective action and the savings resulting from the reduced error.

Results from these two studies should show whether it is possible to: (1) isolate the effect on error rates of individual corrective actions; (2) whether the degree of effect is measurable; (3) whether a specific cost can be assigned to the action; and (4) whether a truer net saving figure can be calculated.

In summary, until the results from these studies are in, the Department believes its method of calculating cost avoidance savings on the basis of the total reduction in errors is the most realistic approach.

3. Considering Administrative Costs

HEW believes that concern for the relationship between AFDC errors and the administrative costs of reducing these errors is valid. We have examined this relationship and will continue to examine it as better data becomes available. Our preliminary examination of this relationship indicates that only a small fraction, less than 17 percent, of administrative costs can be attributed to QC and its related corrective actions. As State accounting systems become more accurate and achieve a capability of isolating QC related corrective actions and their costs, we will obtain more accurate data on the potential trade-offs between further reduction of errors and associated administrative costs.

GAO Recommendation

> That HEW base its reporting of State errors on payment errors rather than case errors.

Department Response

The Department concurs in this recommendation and will include in future reporting this approach of focusing on payment errors rather than case errors.

GAO Recommendation

> That HEW direct its attention to assisting the States in identifying corrective actions that can be demonstrated to be cost-effective.

Department Response

This is already being done to a considerable degree, and we are constantly striving to make our work with the States in this key area more effective.

The Department already provides technical assistance to States on cost-effective corrective actions. Specifically, the Department has issued 13 "How-they-do-it" publications and 22 State Management Practices Aids to assist States in adopting effective corrective actions. Each of these documents describes a proven, cost effective technique for reducing errors through corrective action. States have been encouraged to adapt these techniques to their own error problems. Also, the Department has held workshops and training sessions for State staff and has engaged contractors to assist States and has funded numerous demonstration grant proposals for States to develop innovative techniques for reducing errors. The Department will continue to provide advice and work directly with States to help reduce errors and improve program management by adoption of cost-effective corrective action and management improvements.

GAO note: Comments pertaining to matters discussed in draft report are not included in final report and have been omitted.

Additional Department Comments

The Department finds that the emphasis in the GAO report on cost effectiveness tends to confuse and prevent a better understanding of the AFDC-QC program and its very positive accomplishments.

First, the GAO report does not provide a working definition of cost effectiveness, making it difficult to judge what the GAO is examining. Second, the GAO report does not say that the corrective actions implemented by States have not been cost effective. The GAO report simply says that the States did not conduct cost-benefit studies prior to adopting many of these corrective actions. This statement erroneously implies that these actions were not cost effective, while evidence indicates quite the contrary. The sharp decline in error rates and erroneous payments indicates that corrective actions have been highly cost effective.

The GAO report acknowledges that cost-benefit studies are not necessary in all instances (page 39) and that they should be done only in "more extensive corrective actions". But GAO never defines what is "extensive." The Department contends that most of the corrective actions taken by States were obvious and simple corrective steps and required no cost-benefit studies; i.e., income maintenance worker training, policy simplification and revision, increased verification techniques, etc.

Also, it is important to note that States' welfare programs must be responsive to many outside influences which limit their ability to control administrative costs or conduct cost-benefit studies prior to implementing administrative changes. For example, court decisions and Federal and State legislation can either constrain or mandate agency actions irrespective of cost. Secondly, there often are extenuating circumstances that require an agency to undertake a particular course of action even though there may not be a clear cost-benefit relationship. Thirdly, the very nature of the AFDC program (in dealing with human needs within a highly politicized framework) makes for very short lead-time in implementing program changes and makes it difficult to complete cost-benefit studies before implementation. Considering all of these factors, and the absence of any evidence to the contrary, we believe there is a high benefit-cost ratio in the QC program.

Finally, the Department strongly rejects the notion that there is a cause-and-effect relationship between the implementation of quality control in 1973 and the near-doubling of State and local administrative costs (pages 61 and 62). We examined the rise in administrative costs since 1973 and found that less than 17% (or $81 million dollars) of this (495 million dollar) rise can be attributed to quality control and its associated corrective action costs. There is no evidence to support the GAO claim. Actually, available evidence indicates an exceptionally high benefit-cost relationship between QC (and QC-generated corrective actions) and the very solid reduction in erroneous payments that the QC program has achieved in its 2½ years operating history.

PRINCIPAL HEW OFFICIALS RESPONSIBLE FOR ADMINISTERING ACTIVITIES DISCUSSED IN THIS REPORT

	Tenure of office	
	From	To
SECRETARY OF HEALTH, EDUCATION, AND WELFARE:		
Joseph A. Califano, Jr.	Jan. 1977	Present
David Mathews	Aug. 1975	Jan. 1977
Caspar W. Weinberger	Feb. 1973	Aug. 1975
Frank C. Carlucci (acting)	Jan. 1973	Feb. 1973
Elliot L. Richardson	June 1970	Jan. 1973
ADMINISTRATOR, SOCIAL AND REHABILITATION SERVICE (note a):		
Don I. Wortman (acting)	Jan. 1977	Mar. 1977
Robert Fulton	June 1976	Jan. 1977
Don I. Wortman (acting)	Jan. 1976	June 1976
John A. Svahn (acting)	June 1975	Jan. 1976
James S. Dwight, Jr.	June 1973	June 1975
Francis D. DeGeorge (acting)	May 1973	June 1973
Philip J. Rutledge (acting)	Feb. 1973	May 1973
John D. Twiname	Mar. 1970	Feb. 1973
ASSOCIATE ADMINISTRATOR FOR MANAGEMENT, SOCIAL AND REHABILITATION SERVICE (note a):		
Clarence M. Coster	July 1974	Mar. 1977
Samuel E. Martz (acting)	Dec. 1973	July 1974
Francis D. DeGeorge	Dec. 1972	Dec. 1973
COMMISSIONER OF SOCIAL SECURITY (note a):		
James B. Cardwell	Sep. 1973	Present

a/On March 8, 1977, the Secretary of HEW announced a reorganization of HEW. The Social and Rehabilitation Service was abolished as of that date. Responsibility for the AFDC program was assigned to the Social Security Administration.