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ELIMINATING AND RECOVERING IMPROPER PAYMENTS

HEARING

BEFORE THE

FEDERAL FINANCIAL MANAGEMENT, GOVERNMENT INFORMATION, FEDERAL SERVICES, AND INTERNATIONAL SECURITY SUBCOMMITTEE

OF THE

COMMITTEE ON
HOMELAND SECURITY AND
GOVERNMENTAL AFFAIRS
UNITED STATES SENATE

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ELIMINATING AND RECOVERING IMPROPER PAYMENTS

THURSDAY, MARCH 29, 2007

U.S. SENATE,
SUBCOMMITTEE ON FEDERAL FINANCIAL MANAGEMENT,
GOVERNMENT INFORMATION, FEDERAL SERVICES,
AND INTERNATIONAL SECURITY,
OF THE COMMITTEE ON HOMELAND SECURITY
AND GOVERNMENTAL AFFAIRS,
Washington, DC.

The Subcommittee met, pursuant to notice, at 10:48 a.m., in room 342, Dirksen Senate Office Building, Hon. Thomas R. Carper, Chairman of the Subcommittee, presiding.

Present: Senators Carper, Coburn, and McCaskill.

OPENING STATEMENT OF SENATOR CARPER

Senator CARPER. The hearing will come to order. I just want to start off by apologizing for Senator Coburn, myself, and our colleagues for starting about 45 minutes late. The Senate has been voting on the supplemental appropriation to provide largely for additional money for our forces in Iraq and Afghanistan and we have just finished the bill a few minutes ago, so now we are here starting late, but we are grateful to each of you for your patience and for those of you who have come to testify and to respond to our questions.

When I first arrived in the Senate about 6 years ago, we were debating just what to do with a very large budget surplus. Just a few short years later, we find ourselves wrestling with record budget deficits and wondering how we were ever going to get our heads above water again.

I think we took an important step toward addressing our serious fiscal problems last week with the passage of what I thought was a sound budget resolution. Going forward, however, we are going to need to do a lot more difficult work to close the budget deficit and put ourselves on stronger footing in preparation for the difficult fiscal period ahead when the baby boomer generation—that is my generation—begins to retire.

We are going to need to find a way to collect some of the hundreds of billions of dollars in taxes that are owed to the Treasury that are uncollected each year, and we actually began to address that a bit in the budget resolution itself. We are going to need to control spending in some areas and in others to cut or maybe eliminate it altogether. And I am certain we will have a healthy debate about how best to do all of this, but I am equally certain that we

can get just about everyone to rally around an effort to reduce what we call improper payments.

When my staff and I first began our work on this Subcommittee more than 2 years ago, working with Senator Coburn and his staff, we held meetings with, among others, OMB, GAO, and various agencies to learn about some of the financial management challenges that the Federal Government faces and what was being done about them. We were shocked—outraged, even—to learn that at such a difficult time in our Nation fiscally, some Federal agencies were making literally tens of billions of dollars in avoidable improper payments year in and year out.

In fiscal year 2006, agencies made some $42 billion in improper payments, according to OMB's estimates. Most of these improper payments were overpayments. Similar amounts of money were wasted in fiscal year 2004 and fiscal year 2005, the first 2 fiscal years that agencies were required to report on the improper payments that they make.

What Senator Coburn and I have learned through our oversight work is that, unfortunately, these estimates aren't always very meaningful. In fact, to a large extent, they are only the tip of what could be a pretty large iceberg. The true cost of a number of agencies' inability to implement the kind of sound financial management practices that could prevent improper payments, is likely billions of dollars higher than OMB's estimates.

The official improper payments estimates that OMB releases each year do not include any estimates for Medicaid. They don't include estimates for the Medicare Advantage Program, the Medicare Prescription Drug Benefit, Temporary Assistance for Needy Families, or the school lunch program. They don't include estimates for a number of programs in the Department of Homeland Security, Department of Justice, NASA, and elsewhere that have not even been examined to determine their susceptibility to improper payments.

While we clearly have our work cut out for us, I applaud the focus that OMB and the Administration have placed on the improper payments problem. Eliminating improper payments is now a major initiative under the President's Management Initiative and progress is clearly being made as a result of that emphasis. More programs are reporting improper payments each year, and some programs have seen a sustained reduction in their annual improper payments estimates.

That said, we need to step up our efforts, and by "we," I mean this Subcommittee, OMB, and more importantly, those agencies out there that still don't appear to take their responsibility under the law seriously when it comes to eliminating improper payments.

About 2 weeks from now, taxpayers in Delaware, Oklahoma, and across this country will be rushing to post offices to submit their tax returns just as the filing deadline arrives. I suspect a good portion of them will be none too pleased. They would be even less pleased if they knew that the Federal agencies entrusted with their hard-earned dollars, including some who are represented here today and many who are not, have proven incapable of complying, at least to this point, with even the most basic elements of the Improper Payments Information Act—the main tool that we use to ad-

dress the improper payments problem. Taxpayers also would not be pleased to learn that agencies, including some that report significant amounts of improper payments each year, may not be doing all that they can to recover overpayments that they have made.

A number of agencies are required under the Recovery Auditing Act to review their books each year, identify overpayments, and attempt to collect those overpayments. According to data compiled by GAO, however, less than a third of the overpayments identified by auditors each year are actually recovered. On top of that, the only overpayments made subject to collections under current law are those made to contractors.

It should be clear, then, there is a lot more work to be done. I think we have the leadership now from the Administration. Senator Coburn and I have been working hard, along with our staffs, to provide constructive oversight. We have been joined by Members of our Subcommittee, most especially Senator McCaskill, former Auditor of the State of Missouri.

But what we need to do now is to get agencies to be more transparent about the mistakes they are making, start cleaning up the management and internal controls problems that lead to improper payments, and to work aggressively to recover those improper payments that can be recovered.

I think I speak for all of my colleagues, and I don't need to speak for Dr. Coburn, but I will try to for a moment, when I say that this Subcommittee stands ready to help in the effort to eliminate improper payments in any way that we can. I know that the Administration has already submitted some suggested legislative fixes that we are going to be considering. Senator Coburn and I have already been working together to get two amendments, including this last week in the Senate-passed fiscal year 2008 budget, that would allow us to dedicate the revenues generated from reducing improper payments and increasing recovery auditing to deficit reduction.

My thanks again to our witnesses for taking the time to participate in our hearing this morning to help us find a way to bring agencies into compliance with the Improper Payments Information Act and to reduce as much as we can the amount of money that we waste each year through improper payments.

Senator Coburn.

OPENING STATEMENT OF SENATOR COBURN

Senator COBURN. Senator Carper, thank you so much for having this hearing. Before we start, I want to commend Linda Combs and OMB. They have been highly cooperative. I think from her efforts, we have seen a lot of progress on improper payments. I have some real disagreements with some of the decisions associated with that, but nevertheless, the cooperative nature and the way in which we have been able to work together is very much appreciated.

I also want to thank GAO, and particularly Comptroller General David Walker and McCoy Williams, for their outstanding, fantastic work for the Congress. We would be imminently less effective without both these agencies' help. I think it points to the fact that the Executive and the Administrative Branch, in conjunction with GAO, can have an impact.

I would just like to make a couple of comments. This is our fifth hearing on improper payments and I think we ought to assess what we are seeing. I disagree with Senator Carper. If you do real accounting, one time in the last 50 years, we have had a surplus, other than $3 billion one year in the 1990s, if you do real accounting. The rest of the time, we have never had a surplus and it is the game. It is just like this year we reported a $175 billion deficit. If you use that same accounting technique, we have never had a surplus, if you use the same combined accounting technique.

So the national debt now stands at almost $8.9 trillion. We added $400 billion to it last year. Medicare and Social Security are likely bankrupt for our children and certainly for our grandchildren. Congressional restraint has not improved. As a matter of fact, you don't even have to worry about improper payments. We tried to put some teeth in it with an amendment on the 9/11 bill and the Senate won't enforce it. So consequently, even though we were going to have this hearing, there is not a will in the Senate yet to make sure that there are teeth associated with enforcing the law, not a desire, not a rule, but a Federal law that says the agencies have to comply.

We also see that there is a lack of Congressional restraint. We have an emergency bill that just passed. Although it is controversial, we added $20 billion outside of the budget that will go straight to the deficit with a bill that we just passed that is getting ready to be conferenced with the House.

Mr. Chairman, I have a rather lengthy statement and I think what I would like to do is submit that for the record, since we are late. I would say, and I will get into the area, there are rulings by OMB that go directly against what the law states. The law states that a risk assessment will be formed every year, not every 3 years, but every year. That is what the law states. And I don't believe that, although the spirit of cooperation is great, I think we have a real problem there. I am especially concerned with NASA.

I also would make one final point, as I ask for this to be placed into the record.

Senator CARPER. Without objection.

Senator COBURN. The three testimonies we received, two late yesterday afternoon, one last night—I asked the Chairman that those people not be able to actually give their testimony and just be here, as we do in several other committees within Congress. I think it is highly important—and there is no excuse, this hearing has been on the docket for a long time—for us not to have had that testimony. Whether that is OMB holding it up or who, it doesn't matter to me. The fact is, it is inappropriate for Congress to get testimony the night before a hearing and expect for us to stay up and prepare all night because the Administration doesn't want to get its job done in a timely fashion.

So I would suggest if that happens in the future, I would kindly ask the Chairman that those who are late with their testimony are not allowed to give their testimony and just have to respond to questions.

Senator CARPER. Thank you, Dr. Coburn.

[The prepared statement of Senator Coburn follows:]

OPENING STATEMENT OF SENATOR COBURN

INTRODUCTION

I want to commend OMB and Linda Combs in particular for their efforts to tackle the problem of payment errors. Ms. Combs, your efforts have been Herculean and I appreciate your work. We may not always agree on everything, but I can't thank you enough for how well your office has worked with this subcommittee. It has been a model for how the legislative and executive branches ought to work together to do the very best for the American people.

I also want to thank GAO, particularly Comptroller General David Walker and Mr. Williams, who is with us today. As new Members and their staffs come into the Congress, we would be infinitely less effective on technical issues such as today's topic without the hand-holding and painstaking analysis you all provide us.

CONTEXT

As we embark on our fifth hearing on improper payments in the past two years, let's review the nation's fiscal outlook.

- The national debt stands at $8.8 trillion.
- Medicare and Social Security are likely to bankrupt for our children and certainly for our grandchildren.
- Congressional restraint has not improved since the elections—"exhibit A" is that the House recently passed an emergency war spending bill, but not before saddling this $100 billion spending with $20 billion more of pork and carve-outs for special interests such as spinach and peanut storage.

PROGRESS ON PAYMENT ERRORS

That's the big picture. Let's look at today's part of that picture—payment errors. The Improper Payments Information Act of 2002 requires the following:

- *Perform a risk assessment* to determine whether or not programs and activities are susceptible to making "significant improper payments," (defined by OMB as program where at least 2.5% of all payments are improper AND the absolute dollar figure associated with that 2.5% or more totals at least $10M.)
- *Develop a statistically valid estimate of improper payments* for all programs and activities identified as susceptible to significant improper payments in the risk assessment.
- *Develop a corrective action plan* for all programs where the statistical estimate exceeds $10 million in annual improper payments, The remediation plan must contain annual targets for reducing improper payment levels.
- *Report the results of IPIA activities* on an annual basis to Congress, and in the DHS Performance and Accountability Report.

So that's what the law requires. Where are we?

- In the third year of IPIA reporting, only 18 of the 36 agencies have reported even *reviewing* all programs and activities as part of the risk assessment process.
- In other words, only **half** of all Federal agencies have completed their required risk assessment.
- Twelve agencies provided enough details that indicated some level of review.
- Another six agencies have yet to report **ANY** information on their risk assessment.
- We have also made little progress in finding a proven, reliable methodology to determine accurate risk assessment data.
  - Some agencies still use non-statistical sampling, while others use single audits to identify risk assessments. Others, including witnesses today, are incorrectly claiming that their recovery audits are valid proxies for the statutorily required statistically valid risk assessment.
  - Both methods lack the depth and detail required to determine adequate risk assessments.

So how does this status translate into dollars?

This year, the government-wide improper payment estimate totaled $42 billion, up from $38 billion last year. Yet, given that only **HALF** of the agencies have provided complete risk assessments and that there is a lack of consensus on the methodology used to determine improper payment estimates, we're still in the dark when it comes to understanding the total magnitude of the problem.

RECENT DEVELOPMENTS

One of the more troubling discoveries this year is the fact that OMB revised IPIA implementing guidance in a way that is fundamentally at odds with the law and Congressional intent.

Despite the overwhelming evidence that we're not yet properly identifying risk-susceptible programs, the revised guidance lightens the burden and allows for agencies to perform risk assessments every *3 years* for those programs not deemed susceptible to significant improper payments.

This is alarming for several reasons. First, the IPIA is still in its infancy. GAO reported that for fiscal years 2004 through 2006, "some agencies still had not instituted systemic methods of reviewing all programs and activities or had not identified all programs susceptible to significant improper payments." GAO also reported further that "agencies employ different sampling methodologies to estimate improper payments and certain agencies risk assessments appear questionable." These facts suggest that there's not a consensus that we've got the risk assessment process well-in-hand enough to go easier on agencies in risk assessment.

For instance:

- In 2005, the Department of Agriculture's Marketing Assistance Loan Program had an error rate of 0.7%. This year, it skyrocketed to 20.3%.
- Another example is the Department of State's International Information Program-US Speaker and Specialist Program. In 2005, the improper payment estimate totaled $1.9 million, with an error rate of 81.2%. In 2006, the error rate dropped to 23.8%, HOWEVER, the improper payment amount tripled to $6.7 million.

I don't think we need to spend energy weakening the law and figuring out which programs should be exempt from annual risk assessments until a consistent, statistically valid method is established government-wide to identify payment errors.

RECOVERY AUDITS

I am encouraged by the potential that recovery audits can bring to the problem of payment errors. A provision in the National Defense Authorization Act for FY 2002 requires that agencies that enter into contracts in total excess of $500 million in a fiscal year must carry out a cost-effective program for identifying and recovering amounts erroneously paid to contractors. Recovery audits are a win-win. First, they recapture lost payments. In Fiscal Year 2006, $256 million was recaptured.

Unfortunately, that's only about a third of the amount that was identified as needing to be recovered. But the amount we're talking about here isn't even a billion dollars. With payment mistakes totaling over $40 billion, we need to do more than just recover a billion, which is why the second benefit of recovery audits is so useful.

These audits help us determine weaknesses in our financial systems responsible for the payment errors in the first place. Agencies should pay close attention to the recovery audit reports as they provide useful insights about where their vulnerabilities exist and what effective internal controls can be implemented for prevention.

I do want to note however, that recovery audits are only required on contracts larger than $500 million. They are also generally retrospective beyond the most recently ended fiscal year. In other words, under no circumstances can they serve as legal "proxies" for the statutorily required statistically valid risk assessments for the sake of estimating likely rates of payment errors for agency estimates for previous fiscal years. I am dismayed that some agencies seem to be in error on this point.

Ultimately, transparency and risk assessment data are only the beginning of accountability, not the end. We can conduct oversight hearings until we all turn blue in the face. Exposing the true scope of the problem has been hard enough, and we're still not there with any sort of methodological rigor.

LACK OF POLITICAL WILL

However, even if we were, it grieves me that so far, this Congress has not had the political will to address the problems that have been exposed. I have offered numerous amendments to bills in the past 2 years to address payment errors and most of them have failed.

Things are different here in Washington. If an employee at a private firm made a major payment error, he would probably face disciplinary action, and might even be fired or forced to pay for the lost funds. But if a government official makes a major payment error, or oversees a program which routinely makes payment errors, there is a strong possibility he would face few consequences, and that's assuming that the mistake were even discovered.

Much of our Federal spending is too incoherent to be audited, much less pass an audit. If Members of Congress had to vouch for the integrity of our financial state-

ments the way we require private firms to do under Sarbanes-Oxley requirements, we'd either have to admit we couldn't do it, or else go to jail for deceiving the public.

Although progress has been made by this President, and he inherited the accumulated mess of decades of out-of-control government growth, still, the status quo is shameful. I hope that this Congress will be the Congress that finally finds the courage to bring the painful, but necessary accountability to address this problem.

I want to thank our witnesses for coming today.

OPENING STATEMENT OF SENATOR MCCASKILL

Senator MCCASKILL. Thank you. I do not have an opening statement. I do, however, have to leave and preside at noon. I am hoping that—I am anxious to talk to the second panel about their failure to provide risk assessments. I know you all have worked on this for years and I appreciate both of your work on it and I want to just add to your chorus on this that it is unacceptable that we do not have risk assessments from these departments. If I am not here to hear it, I know that you all will do a great job of asking the questions for me as to what in the world their excuse could be not to have risk assessments in those departments.

Thank you, Mr. Chairman.

Senator CARPER. I hope you will have that opportunity to ask the second panel. Thanks.

Again, I am not going to introduce at any length Ms. Combs and Mr. Williams. We are delighted that you are here. Thank you for your good work that you do and for the spirit of cooperation that you bring to this effort. Ms. Combs.

TESTIMONY OF HON. LINDA M. COMBS,[1] CONTROLLER, OFFICE OF FEDERAL FINANCIAL MANAGEMENT, U.S. OFFICE OF MANAGEMENT AND BUDGET

Ms. COMBS. Mr. Chairman and Members of the Subcommittee, I am very pleased to be here to speak with you today on the progress being made in implementing the Improper Payments Information Act and the Recovery Auditing Act.

Today, I am glad we can discuss accomplishments in implementing the IPIA, the government progress we have made, and how Congress can assist us in achieving our shared objective of eliminating improper payments. The Federal Government is achieving measurable results in meeting the President's goal to eliminate improper payments and fulfilling the requirements of IPIA. Since the first reporting under IPIA in fiscal year 2004, our efforts to eliminate improper payments have been centered on three primary requirements of IPIA: Identifying the risk-susceptible programs, eliminating the annual amount of improper payments in those risk-susceptible programs, identifying the root causes of those improper payments, and correcting the errors.

In fiscal year 2006, agencies strengthened their methods for risk assessing their programs and activities for improper payments. As a result of these improvements, the amount of Federal outlays determined to be susceptible to improper payments increased from $1.4 trillion to $1.7 trillion. This increase reflects the continued commitment of Federal agencies to ensure that all potential sources of error are reported.

[1] The prepared statement of Ms. Combs appears in the Appendix on page 47.

Efforts are continuing to move the Executive Branch to full reporting under IPIA by 2008. Eighty-one percent of all risk-susceptible outlays are being measured for improper payments, and when the fiscal year 2008 results are reported, almost 100 percent of risk-susceptible dollars will report an error measurement.

The amount of improper payments in programs originally reported in 2004 were reduced from a baseline of approximately $45.1 billion to $36.3 billion this year, a nearly $9 billion or 20 percent reduction. These original programs continue to represent a significant majority of the 2006 improper payments. The overall Federal 2006 improper payment rate was 2.9 percent and total improper payments equalled $40.5 billion.

Let me take this opportunity to express my sincere appreciation to the Senate for providing over a billion dollars in adjustments to the discretionary caps for program integrity and tax compliance efforts in the Senate budget resolution, as reported out of the Budget Committee. We would, of course, encourage the House to include these cap adjustments in their budget resolution, as well, and we welcome your leadership, along with ours, in helping to make this happen.

Additionally, we are most appreciative of the Senate's interest in including language to newly authorized bills that stress the importance of program integrity. We also invite your leadership in assisting in the enactment of the other program-specific reforms that are included in the President's fiscal year 2008 budget. Those are listed in my written testimony, which I submit for the record.

This Administration will continue to hold agencies accountable under our tool of the President's Management Agenda Eliminating Improper Payments Initiative, and further build upon recent results to address remaining challenges. We are optimistic that our current efforts, complemented by the enactment of the program integrity reforms proposed in OMB's annual IPIA report, and full funding of the President's request for program integrity efforts will continue to pave a path forward in achieving our shared objectives to eliminate improper payments.

And I will add that the success that we have had to date and the success that we will have in the future would not have been possible without the cooperation of both the Legislative Branch, my colleagues at GAO, as well as our colleagues here on the Hill, and we look forward to continuing to work with you in ways that will, indeed, do the best for every taxpayer and that will focus our resources on the very best return for each dollar we put into this program. Thank you.

Senator CARPER. Thank you, Ms. Combs. Mr. Williams.

TESTIMONY OF McCOY WILLIAMS,[1] DIRECTOR, FINANCIAL MANAGEMENT AND ASSURANCE, U.S. GOVERNMENT ACCOUNTABILITY OFFICE

Mr. WILLIAMS. Thank you, Mr. Chairman, Members of the Subcommittee. I am pleased to be here today to discuss the government-wide problem of improper payments and agencies' efforts to address key requirements of the Improper Payments Information

[1] The prepared statement of Mr. Williams appears in the Appendix on page 51.

Act and Recovery Auditing Act. Our work over the past several years has demonstrated that improper payments are a long-standing, wide-spread, and significant problem in the Federal Government.

At the outset, let me commend this Subcommittee for continuing to hold oversight hearings on this important issue. Also, OMB has played a key leadership role in addressing this problem. For example, OMB continues its commitment to identify and eliminate all improper payments government-wide by working with the agencies to establish corrective action plans to address their root causes. OMB also annually reports on agencies' efforts to address IPIA and Recovery Auditing Act requirements.

Mr. Chairman, my testimony today will focus on three areas: Trends in agencies reporting under IPIA for fiscal years 2004 through 2006, challenges in reporting improper payment information, and agencies' reporting of Recovery Auditing efforts to recoup improper payments.

First, since 2004, agencies have made some progress in reporting improper payment information. The total number of programs reporting improper payment estimates for fiscal year 2004 totaled 41, compared to 60 programs for fiscal year 2006. The total improper payment dollar estimates was $45 billion for fiscal year 2004, $38 billion for fiscal year 2005, and about $42 billion for fiscal year 2006. The increase in the estimate from 2005 to 2006 was primarily attributable to 15 newly reported programs totaling about $2.4 billion, and a $1.6 increase in USDA's Marketing Assistance Loan Program estimate due to improvements in how it measures improper payments. In addition, several programs experienced increases in their improper payment estimates as a result of lax up-front eligibility controls related to benefit delivery to victims devastated by Hurricane Katrina.

Now I would like to highlight some of the major challenges that remain in meeting the goals of the Act and ultimately improving the integrity of payments. First, some agencies have not yet reported for all risk-susceptible programs. For example, the fiscal year 2006 total improper payment estimate of about $42 billion did not include any amounts for 13 programs that had fiscal year 2006 outlays totaling about $329 billion.

Second, certain methodologies used to estimate improper payments did not result in accurate estimates.

Finally, GAO noted that internal control weaknesses continued to plague programs susceptible to significant improper payments. For example, in the Department of Education's fiscal year 2006 PAR, the OIG reported that identifying and correcting improper payments remains a challenge for the agency due to ineffective oversight and monitoring of policies, programs, and participants.

With regard to recovery auditing, Mr. Chairman, again, we have seen some progress. For fiscal year 2004, 12 agencies reported recovering about $53 million, compared to 18 agencies that reported recovering about $256 million for fiscal year 2006. Given the large volume and complexity of Federal payments and historically low recovery rates for certain programs, I would like to emphasize that it is much more efficient and effective to pay bills and provide benefits properly in the first place.

In closing, Mr. Chairman, we recognize that measuring improper payments and designing and implementing actions to reduce them are not simple tasks and will not be easily accomplished given today's budgetary pressures and the American public's interest and increasing demand for accountability over taxpayer's funds. Oversight hearings such as this one today help keep agencies focused on the goals of IPIA and being accountable for results.

I look forward to continuing to work with this Subcommittee as well as Federal agencies and the Administration to address this problem. This concludes my statement. I will be pleased to respond to any questions you or Members of the Subcommittee may have. Thank you.

Senator CARPER. Thank you very much. I think we are going to take 7 minutes for questions and I will try to keep us close to that. I will certainly stay close to that myself.

Thank you very much for your testimony. Let me start, Ms. Combs, with a question for you, if I may. Speaking on behalf of OMB and the Administration, what do you feel is especially good that you all have been doing over the last 3 or 4 years since the law was passed in 2002? What do you feel especially good about and where is the heavy lifting that still remains to be done?

Ms. COMBS. Thank you, Mr. Chairman. I think the thing I feel especially good about is that the trends that Mr. Williams just spoke about are continuing to go the right way. We obviously still have an awfully lot to do. It is clear when we look at the challenges with particularly State administered programs, that is where our challenges remain.

We have some very good things to be proud of. They are included in my written testimony as well as GAO's, so I won't go over those. But probably it serves us all best to concentrate on where the challenges are.

Senator CARPER. If you would, please.

Ms. COMBS. I think that the federally-funded programs that are State administered pose the greatest challenge for our agencies and departments as well as for the work that we are all doing in a more collective way.

Senator CARPER. Can you give me some examples of those? Medicaid and what else?

Ms. COMBS. Well, there are several of those and let me just say where I think the critical challenges are.

Senator CARPER. OK.

Ms. COMBS. The critical challenges, I think, are to make sure that the roles and responsibilities for what is a State responsibility versus what is a Federal responsibility is very important. I think a lot of States have situations where they really need to understand how the money is distributed. They have their own requirements. I think what we have done with meeting with some of the State agencies and some of these State representatives, I personally have met with some of them to try to ferret out what we can do individually with States and collectively and I appreciate the partnerships that we have had with the Association of Government Accountants, for example. We have had additional meetings continue as we work with those groups of people.

And I think that one of the things that we have talked with you and your staff about that we will continue to do and that continues to help all of us is that when statutes are enacted, making it very clear to have the authorization in there that lets the Federal components do what needs to be done in order to work with the agencies and put in program integrity roles and responsibilities, making sure those are clearly defined and that the program integrity funds are set aside so that we can, indeed, assure that we don't have improper payments like we have now.

Senator CARPER. Mr. Williams, it is clear to me, at least, that when you look at the major high-risk programs that have not yet reported improper payment estimates, that some of them have a lot in common. They all spend a lot of money. Many of them seem to involve grants or some shared administrative responsibilities with States, as Ms. Combs has just said. Why do you suppose programs like this have had so much trouble reporting improper payment estimates? What does OMB do to help them along and what can Congress do to help make that job easier? Do we need to make it clear to States or to grant recipients in some way that they have a responsibility to help agencies make sure the program funds are spent properly?

And as sort of an adjunct to that, one of our later witnesses talks about incentivizing States. It is hard, as an old governor, to expect States to do a whole lot of extra work if they don't get something out of it. If there is a shared responsibility to administrate in recovering these funds, I think as sort of an adjunct to that, common sense would be that they ought to share in some of the gain.

So if you could sort of reflect on those series of questions, I would be grateful. Thank you.

Mr. WILLIAMS. Mr. Chairman, we issued a report last year, I believe it was in the spring—I don't remember the exact month—but it looked at those particular programs and we basically reported that there is about $400 billion in grants that the Federal Government issues each year. I think our bottom line message was that this is going to take a coordinated effort between the Federal Government and the States to address this improper payment issue. Everyone has a responsibility to make sure that the funds make it to the intended recipient.

So I think that needs to be taken into consideration, and I think that one of the other components of your question related to why this is such a difficult area to get a handle on. I think OMB has basically stated in its reports, and we would agree, that if you look at the Medicaid program, for example, within the Federal Government framework, each State has its own rules and regulations as to how it operates, so you have to work with these individual States and see if you can come up with the method where you can actually identify a methodology that you can come up with a number that is reasonable and that will give you that baseline that you need to begin identifying and reporting so that the ultimate job of reducing the improper payments can get underway in these particular grant programs.

Senator CARPER. Ms. Combs, you stated that certain methodologies used to estimate improper payments that did not result in accurate estimates. Could you just take a moment and explain to us

what that means and what needs to be done to help ensure that amounts reported by agencies are, indeed, accurate?

Ms. COMBS. The rationale is that any of our guidance documents, we try to ensure that the cost of requirements that we impose on agencies are justified by the benefits that are realized. I think that one of the things that we have an opportunity to do here is, as we mentioned earlier, to do what is best for the taxpayer and to focus our resources on what is the best return possible.

Senator CARPER. We may come back to that one after we go one time through. Dr. Coburn.

Senator COBURN. Thank you, Mr. Chairman.

Do you want to reflect back now and answer the Chairman?

Ms. COMBS. OK.

Senator COBURN. I will give you some of my time.

Ms. COMBS. I was going to mention the 13 programs. They have been mentioned here earlier. And all I wanted to say was that we have all 13 of those programs scheduled to report an error measurement and they all have a timeline for reporting. You have mentioned TANF. That has a component rate coming in this year. One of the components is going to report in 2007, and then the full rate will be in 2008. And CCDF will report a component rate in 2008. Medicare Advantage, Medicare Prescription Drug Benefit are all going to report component rates in 2008. I just wanted to get that on the record.

Senator COBURN. Thank you. Mr. Chairman, I have several questions I would like for us to be able to submit in writing to the witnesses, if we can——

Senator CARPER. Without objection.

Senator COBURN [continuing]. And have a prompt response.

I also want to enter into the record, Public Law 107–300, and here is what it says in Section 2.[1] The head of each agency shall, in accordance and with guidance prescribed by the Director of OMB, annually review all programs and activities that it administers and identify all such programs and activities that may be susceptible to significant improper payments. Estimation: With respect to each program and activity identified, the head of the agency shall estimate the annual amount and submit those estimates to the Congress. It couldn't be more clear.

Ms. COMBS. A proven track record of low rate of improper payments.

Senator COBURN. Like what?

Ms. COMBS. National Science Foundation, education and research programs. They reported in 2004 and 2005 and they have a 0.02 error rate.

Senator COBURN. OK.

Ms. COMBS. VA insurance programs reported in 2004 and 2005 a 0.02 percent error rate. EPA Clean Drinking Water and State Revolving Fund Programs reported in 2004 through 2006, 0.18 percent.

Senator COBURN. OK. I just wanted one.

Ms. COMBS. OK.

Senator COBURN. That's fine.

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[1] Public Law 107–300 appears in the Appendix on page 163.

Ms. COMBS. I realize that there has been some contention over this and we are certainly—we have an open book, as you know.

Senator COBURN. I know you do.

Ms. COMBS. We have offered many times that if there are specific programs that we need to scrutinize more closely, we will do so.

Senator COBURN. Here is the point I am going to. IPIA has only been reporting 3 years, so how do you have a proven track record if we have only been doing this for 3 years.

Senator Carper and I were successful, along with several other Senators, in passing the Transparency and Accountability Act. In 2009, all this stuff is going to be on computer. All this stuff is going to be on a website. There isn't going to be a reason why something can't be reported or followed.

Is all these contracts and all these State-run programs that we supposedly have problems with, like TANF, Medicaid, CDBG, Child Care Block Grant, Food Stamps, and everything else, has to come online at the same time? Otherwise, we are going to be out of compliance with that law like we are this one. So what assurance can you give me that we are on track on the others and staying on track as far as the payment error problem?

Ms. COMBS. Well, I just want to say, Dr. Coburn, I certainly commend the Senate and your efforts, and the Chairman's efforts, in making these things possible because it is through our collective efforts that all of us have been able to work together to give the kinds of pushes that we have needed to make these things happen.

I think all of these new technologies that are coming into play will do nothing but accelerate our efforts. All I am appealing to you today to let happen is let us get the very best dollars we possibly can for the American taxpayer by using the resources we have to make sure that there aren't any huge holes in there like we saw in 2004. I am convinced of that and I do believe that the statistics that we have and that we have worked through play out to that effect, not that we are where we need to be. We can all do more.

Senator COBURN. Right. I understand. We are shooting at a moving target, but we are getting better, and——

Ms. COMBS. Yes, we are.

Senator COBURN [continuing]. I have no complaints with OMB other than on some of the decisions they have made with what is in compliance and what is not.

Explain to me, Mr. Williams, if you will, how you all can find NASA out of compliance and OMB can find them in compliance. How does that happen? I mean, we have 2004 from you all saying they are not in compliance and OMB is saying on the basis of the look-back 10 years ago on a recovery audit that they are in compliance. How does that fit with the law?

Mr. WILLIAMS. Let me just speak for GAO. We took the basic requirements of the law, which basically states that you are supposed to do your risk assessment and then develop your statistically valid estimates, come up with some corrective action plans, and report. We are basically saying that they are not in compliance because the review that was done by the auditors, it questioned the risk assessment. So in our opinion, if you did not do all four of those requirements, then you are not in compliance. So that is how we came up with the non-compliance.

Senator COBURN. So the auditors had a question about the risk assessment that was made——

Mr. WILLIAMS. Yes. On a lot of these agencies that we are talking about, we basically refer to the work that the auditors performed in the area of IPIA while they were performing their financial statement audit. As you know, the law itself basically does not require the IG or an IPA to do an independent review to see as far as the quality is concerned. As you probably noticed in my testimony, we kind of referred to that, that might be a good idea to have that independent set of eyes, because we view the risk assessment as the basic foundation for making sure that you are actually carrying out the steps——

Senator COBURN. So if you have a questionable risk assessment, then, what that means is you can't comment on whether or not you are in compliance or not.

Mr. WILLIAMS. I guess an analogy is kind of like if you miss out on the introduction to accounting, you are probably lost the rest of the way through accounting.

Senator COBURN. I have got you. Thank you. My time is expired.

Senator CARPER. Thank you, Dr. Coburn. Senator McCaskill.

Senator MCCASKILL. Thank you. The estimates that we are using for improper payments, I am uncomfortable with those estimates. I know that there is appropriate back-padding going on as it relates to progress, but if we are using estimates that we know are too low, I don't know that we are really doing anyone a service on this. I want to make sure I understand correctly, Mr. Williams, I think that your testimony is what touches on this because GAO is the one who has done this work—that there are 13 risk-susceptible programs that have outlays of $329 billion in fiscal year 2006 that are not even included in these estimates. Is that correct?

Mr. WILLIAMS. That is correct. That number is approximately $329 billion, and what we are basically saying is that—and I guess our overall message is that, yes, progress has been made, but we are not at the point where we have our hands around the entire picture and these 13 programs are the ones that we are talking about that over the next couple of years, it appears that they will have these risk assessments in place. But until then, we are not for sure what the total number is.

We are using some baseline data based on those agencies that reported in those years, but at no point in time up to now do we have a number that represents the entire Federal Government.

Senator MCCASKILL. And how confident are you of the baseline data? Are you confident of the baseline data? It makes me nervous.

Mr. WILLIAMS. The baseline data is a first step. We have identified problems over the last 2 years with some of the risk assessments, some of the sampling, and we have reported on situations in which agencies have basically said one thing and the independent auditors have gone in and contradicted that statement.

So I think that while there has been progress, there is still a lot of room for improvement. There are a lot of things to be done before I am comfortable with saying that I think we know what we are dealing with. I think we still have work to do in identifying what is our universe of improper payments?

Senator MCCASKILL. Ms. Combs, the significant designation guidance from OMB, the significant improper payment, that you all have indicated that to be significant, it has to exceed $10 million and 2.5 percent of outlays. The "and" in that phrase—I am curious why we need the "and," because we are talking about potentially hundreds of millions of dollars that could not be significant if you are dealing with some of these programs, and frankly, some of the programs that right now are not even part—I mean, we are talking about $329 billion that we haven't even gotten any kind of indication yet.

Ms. COMBS. Well, if we start from the universe of the $2.7 trillion of outlays and we know now that we have a high-risk outlay of $1.7 trillion of that $2.7 trillion, and we look at where are the best places to put our resources in taking care of that $1.7 trillion in high-risk that is currently being tracked today, we decided that the basis for the $2.5 trillion was to make sure that Federal agencies indeed focused on the resources for the programs that would provide the most return on investment for the taxpayer. If you look at the first seven programs we came out with in 2004, those seven programs are still the most significant programs in our 2006 reporting where we have the most improper payments.

So in order to help you with your confidence level a little bit, hopefully, if you look at those and realize that is 95 percent of that $1.7 trillion, then most of that is encapsulated in that. So that is some confidence. Granted, there is still a lot out there, as Mr. Williams just talked about. There are still some things that we don't know. But we do have risk assessments. We have 81 percent of these high-risk programs have measurements today, and by 2008, 100 percent of them will have.

So those are the kinds of things that we know we are making progress on. We are not there yet and we welcome the opportunity to work with you and the Subcommittee to work on specific programs. If you know of some that are out there, we have an open invitation that we will be glad to monitor and follow those——

Senator MCCASKILL. That is a dangerous invitation to extend to me. Very dangerous. [Laughter.]

Calling something that might be more than $10 million insignificant just kind of sticks in my craw and I think that is problematic.

Let me ask both of you about the recovery audits, my experience has been that there are all kinds of companies out there that are willing to do this and absorb the costs in return for a cut of the money. I assume that is the case in the Federal Government, that these contractors that are being used on these recovery audits are being paid a percentage of what they recover?

Ms. COMBS. Yes, that is correct.

Senator MCCASKILL. Well, then why is it not cost effective for everybody to do it?

Ms. COMBS. Cost effective for every agency to do it?

Senator MCCASKILL. And every program. I mean, if the recovery audits are all being done on contingency, in other words, if we don't have to put any money out of our pocket and we hire people and they are the ones that are taking the risk and they are the ones that have to have the overhead, and if they recover money, we get what they recover and they take a piece of it, then why in the

world are we waiting until 2010 in CMS and other places to make it system-wide? Why do we want to do pilot programs? Why don't we say, come one, come all. If you are in the private sector and you think you can recover money for us, sign up, and if you do, we will give you part of it and the taxpayers are the winner there.

Ms. COMBS. Well, I think that those are some things that we could sit down and talk about. There are, as I mentioned earlier, some very complicated issues when it comes to trying to address a one-size-fits-all. It does not one-size-fit-all, so we welcome your suggestions and look forward to meeting with your staff and talking about that.

Senator MCCASKILL. If I could tell one story—when there was a flood in Kansas City and I was a prosecutor, I saw people lined up to get Food Stamps in an area of town where water had not come near. I sent my investigator down to interview people in the line—the line stretched around the block—and started asking people in line if they had flood damage. People readily admitted, no, they just told you to come and sign up and you got Food Stamps.

So I held a press conference the next day and said, if you got Food Stamps and you didn't deserve them, if you turn them in in the next 2 days, we won't prosecute you. It was kind of a recovery program. And we had hundreds of thousands of dollars of Food Stamps that were turned in voluntarily. Now, someone from the Federal Government called me and asked me what the heck I thought I was doing. They wanted to make it complicated. They wanted to know where I asked the people to turn them in and what kind of authority I had to ask them. Well, I just asked people if they got them and they didn't deserve them and they thought they had done it illegally, they should turn them in. I just worry sometimes that we make this more complicated than it needs to be, and that gets in the way of just going after it. Thank you, Mr. Chairman.

Senator CARPER. Thank you very much. I think maybe we will take a couple of minutes apiece for follow-up and then we will turn to our second panel.

A number of high-risk programs have had trouble reporting estimates on the Improper Payments Act. Thus far, they have goals in place to begin reporting, I believe in 2007 and 2008. There are, I think, at least four major programs—we have talked about them already—the Child Care Development Fund, Medicare Advantage, Medicare Prescription Drug Program, and the Temporary Assistance for Needy Families Program—that are not reporting and, as I understand it, don't yet have a timeline in place for coming into compliance with the Act.

This is probably more for Ms. Combs than not—what progress, if any, has been made in bringing those four specific programs into compliance and when you think that we can expect estimated improper payments from them?

Ms. COMBS. TANF will report a component rate by 2007 and a full rate by 2008. CCDF will report a component rate in fiscal year 2008. Medicare Advantage——

Senator CARPER. Say that again.

Ms. COMBS. Fiscal year 2008.

Senator CARPER. For what?

Ms. COMBS. CCDF, Child Care——

Senator CARPER. Yes, but what will they do by 2008?

Ms. COMBS. Child care.

Senator CARPER. What will they do—what will be accomplished by 2008?

Ms. COMBS. They will report a component rate. One of their divisions will report, so they will be reporting what we would call a partial rate.

Senator CARPER. Alright.

Ms. COMBS. Medicare Advantage and Medicare Prescription Drug Benefits will both report component measurements in fiscal year 2008.

Senator CARPER. Mr. Williams, should we take some comfort from that, what Ms. Combs has just responded?

Mr. WILLIAMS. Well, anytime that you have an agency or component within an agency that is not reporting and there is a timeline, that is better than some that we have seen in the past in which there was no information at all, that we were not for sure when anything was going to be reported. So yes, there is some progress there, but as I have stated earlier, the sooner that you are able to get your hands around the entire universe, the better I think we will all be in looking at this particular issue of getting that good base of improper payments government-wide.

Senator CARPER. Alright, thanks. And the only other question I have, I want to go back to how do we incentivize States. When we have these partnership programs, how do we incentivize the States to work with us so they can come out ahead, the Federal Treasury comes out ahead, the taxpayers come out ahead, both in the States and at the Federal level?

Ms. COMBS. I think you are going to hear from the next panel one of the very good success stories of how we incentivize States to do that. Rather than stealing their thunder, maybe you should hear directly from them. But there are some very good ways. When we work collectively with States and hear their concerns, know what it takes for incentives for them to work through these situations, which are very complicated, in their own individual States with their State-administered programs, we really can have some good, positive lessons learned, and I think you will hear that in the next panel coming up from particularly one or two of these.

Senator CARPER. Mr. Williams, I want to ask you the same question. How do we incentive States, more broadly? I appreciate the fact that we are going to hear from at least one witness in the next panel, but how do we do it more broadly, because there are a number of programs where there is this shared partnership, as you know.

Mr. WILLIAMS. Yes.

Senator CARPER. It is those programs where we have some of the biggest problems in recovering improper payments.

Mr. WILLIAMS. Yes. I think we have to look at that particular process, and one of the things that I have seen in the past is that if you take these programs and if money is recovered, for example, and you are able to keep that rather than it going back to another fund or going to another operation, then if there is some incentive there that if I get this money back, I can use it to carry out this

program further, and I think that type of an incentive is something that you really want to have in place. But if you have a program in which there is an improper payment, for example, and if the money is collected it goes back into a fund that cannot be used for the purpose of carrying out that particular program, then there is no incentive there. So you need that type of incentive.

Just from an overall accountability standpoint, one thing that, if I could add to all of this, as far as not just the incentives are concerned, but as I stated in the testimony, the recovery component of it is your second choice. You really want to have systems, policies, and procedures in place——

Senator CARPER. You make that point in your testimony——

Mr. WILLIAMS [continuing]. To prevent this from happening in the first place.

Senator CARPER. Good point. And I am going to come back and ask each of you to reply to that same question again in writing because I want you to think it through. How do we take these specific results that we are going to hear in the next panel and how do we broaden that application throughout this shared partnership. Thank you.

Senator COBURN. Well, first of all, I want to say how pleased I am Senator McCaskill is on this panel.

Senator CARPER. Me, too.

Senator COBURN. It is refreshing and greatly needed to have the help and thank you for being here.

The thing you will notice is that you did not get an answer to your question, and that is not a criticism of Ms. Combs. She doesn't have the ability to agree with you because of the constraints that she operates under. But that is the question that ought to be answered for the American public.

The Recovery Act limits it to $500 million or more, so the first question is how do we change that Act to where we move that down the scale, which is one of the things that needs to be done. But I agree with you, it needs to happen.

I am going to ask almost a rhetorical question, because I think I know the answer, but I would like for both of you to respond. Other than two small programs in the Defense Department, right now, the Defense Department as a whole really isn't reporting under the Improper Payments Act, is that correct?

Mr. WILLIAMS. I will take it. Dr. Coburn, as you know, in last year's legislation, there was a mandate for GAO to take a look at DOD's compliance in the area of travel because of the various reports that we had been issuing about the travel issue. That work is currently underway and we are looking at it very closely from the standpoint of, again, using those basic four criteria that we have talked about here. And we will take those criteria and we will go through and we will look at each one to see what is DOD doing in that particular area. But in addition to that, we are also looking at the Recovery Auditing Act. We got a request from the Subcommittee or the full Committee—I am not sure right now which one—to take a look at the Recovery Auditing Act with DOD and look at other IPIA reporting.

At first glance, you look at an agency that large and I think it would raise the point that was brought up earlier when you talk

about whether this is in compliance or not. You have to take into consideration that there are probably some very large numbers, but when you throw in the 2.5 percent criteria, that might put some of those programs under the radar. So it is difficult for us to say at this particular point in time.

Senator COBURN. So there is no question, I think Senator Carper and I have come to some agreement that we need to modify the IPIA Act to a little degree to address one of the areas that Senator McCaskill raised, and this is this 2.5 percent and $10 million. Congress didn't set that. OMB set that, and there are some practical reasons for why they set it, but I am not convinced that is the threshold that we need to have and I think we need to address that.

Senator CARPER. Thanks very much. Senator McCaskill.

Senator MCCASKILL. I will yield to the Chairman and let these folks go and maybe get a chance to hear from the second panel before I have to leave, Senator Carper. Thank you.

Senator CARPER. OK, fair enough. Alright. Ms. Combs, Mr. Williams, thank you for joining us today. Thank you for your testimony. Thank you for responding, and we will be providing some additional questions and would appreciate your prompt response.

Mr. WILLIAMS. Thank you.

Senator CARPER. Clearly, some progress is being made here. There is a good deal of work for us all to do, as you know. I always like to say, if it isn't perfect, make it better, and this is not a perfect situation and we need to work hard to make it better and obviously we need to work together to make it better. But our job is to try to provide some oversight to hold someone's feet to the fire and we will be endeavoring to do that. When people are doing a good job, agencies are doing a good job, we put a spotlight on them and applaud them. Those that aren't, we will put a spotlight on them, as well, and let the lack of action or inaction speak for itself. Thank you both very much.

Mr. WILLIAMS. Thank you.

Ms. COMBS. Thank you.

Senator CARPER. Mr. Williams, I am just going to ask you if you would take a seat in the front row, if you could.

Mr. WILLIAMS. OK. That is fine.

Senator CARPER. Just don't go away too far. We may want to call you back to the table to respond to some further questions. Thank you.

Mr. Williams, Lee White, who is Executive Vice President of U.S. Operations for PRG-Schultz, is going to testify on a third panel, so he is not going to be needing this seat right now, so we have an extra spot there and just feel free to take that one. We appreciate your flexibility here.

We want to welcome each of our witnesses for our second panel today. I am not going to provide lengthy introductions, but I will say that John W. Cox, who is the Chief Financial Officer of the Department of Housing and Urban Development, we are grateful that you are here. We appreciate your presence and your work.

David Norquist is the Chief Financial Officer of the Department of Homeland Security. Mr. Norquist, one of the things we are going to be asking you is why we didn't get your testimony on time. I am

sorry that Dr. Coburn is not here to hear that response, but I am sure his staff will convey the message. But when you speak, one of the first things I want you to do is to explain that.

We want to welcome Timothy Hill, who is the Chief Financial Officer of CMS. Thank you for coming.

And Terry Bowie, Deputy Chief Financial Officer at NASA. Mr. Bowie, thank you for coming, as well.

I am just going to ask Mr. Cox, if you will, just to lead it off. You have about 5 minutes. Your entire statement will be made part of the record. We welcome your presence and your testimony. Thank you.

TESTIMONY OF JOHN W. COX,[1] CHIEF FINANCIAL OFFICER, U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

Mr. COX. Thank you very much, Mr. Chairman and Senator Coburn, and distinguished Members of the Committee, my name is John Cox, the Chief Financial Officer for Housing and Urban Development. I want to thank you for inviting me here to appear before this Subcommittee today to speak about the results of HUD's efforts to reduce improper payments.

The Department has aggressively complied with the Improper Payments Information Act of 2002 and was the first agency to achieve green status on the President's Management Agenda Initiative for Eliminating Improper Payments. I would like to go over a few of the Department's accomplishments since my office last testified before this Subcommittee on this very topic in September 2005.

We are in the process of updating our Fourth Annual Improper Payment Risk Assessment. Our most recently completed risk assessment covered $58.8 billion in payments made by the Department in fiscal year 2005, and no new high-risk programs activities were identified. Over the past 3 years, the results of HUD's annual risk assessments called for the measurement of improper payment levels in 11 major program areas with the risk potential to exceed the $10 million high-risk program threshold. Those 11 programs constitute about 65 percent of the Department's annual budget and payment activity. Five of the 11 programs measured exceeded the $10 million threshold to require corrective action planning, annual reporting, measurement, and follow-up efforts to reduce improper payment levels.

We completed and verified corrective actions to reduce improper payments to an acceptable level in two of the five programs originally determined to be at risk of significant improper payment levels, payments under the Single Family Acquired Asset Management System and the Public Housing Capital Fund.

We exceeded our internal goals for reducing improper payment levels for HUD's three remaining at-risk program areas, the Public Housing Tenant-Based Assistance and Project-Based Assistance Program, collectively referred to as HUD's Rental Housing Assistance Programs. This reduction, and more importantly the underlying internal control components, was one of the key reasons

[1] The prepared statement of Mr. Cox appears in the Appendix on page 84.

HUD's Rental Housing Assistance Program area was removed from the GAO high-risk list in January 2007.

The reductions in housing subsidy determination errors resulted from HUD efforts to work with its public housing industry partners and multi-family housing projects through enhanced program guidance, training, oversight, and enforcement. The reduction of erroneous payments due to tenant under-reporting of income resulted from improved income verification efforts by housing program administrators, increased voluntary compliance by tenants due to promotion of the issue, HUD's initiation of improved computer-matching processes for up-front verification of tenant income, and an improved methodology for reviewing income discrepancies identified through computer matching to better determine actual cases of under-reported income which impact subsidy levels.

In fiscal year 2006, HUD implemented its new Enterprise Income Verification System for use by public housing agency program administrators in conducting improved verifications of tenant income during the annual recertification process. I want to thank our agency partners at the Department of Health and Human Services and the Social Security Administration for their assistance in this project. This new web-based secure verification system will be expanded to the multi-family housing project-based assistance programs during the current fiscal year. This computer matching capability has the potential to eliminate the majority of the remaining estimated improper rental housing assistance payments. This system is not only fast and more efficient, but just as importantly, it affords more privacy to tenants by eliminating the previous paper income verification letter that was formerly mailed to the assisted tenant's employer.

HUD's long-range strategic goal is to reduce improper rental assistance payments to less than 2.5 percent of total payments by the end of fiscal year 2008. That would be quite an accomplishment given the high degree of complexity of the housing subsidy determinations and the decentralized nature of the program administration.

In conclusion, Mr. Chairman, I want to thank Secretary Jackson, Deputy Secretary Bernardi for their leadership, the employees of HUD, our industry and agency partners for working together to tackle the tough issue of improper rental housing assistance payments. These efforts not only reduced improper payments, which allows more funds to be able to serve HUD's mission, but we also proved that by working together, we could correct these longstanding issues.

I am now pleased to answer any questions you may have.

Senator CARPER. Mr. Cox, thanks very much.

Senator McCaskill, I know you have to go preside at noon. Did you want to ask a question of this panel before you leave? That is a little bit out of order, but I want to afford you that opportunity if you would like.

Senator MCCASKILL. Well, I would appreciate, Mr. Chairman—thank you for this opportunity. Just quickly, I want to make sure that anybody who doesn't have a risk assessment, I would like to know specifically for the record, and you don't need to answer it now, but anyone who has not done a complete risk assessment, and

I know there are several departments represented here who haven't, I would like to know why, and if the law requires it, why it hasn't been done.

And second, specifically for CMS, why wait? If the three pilot programs have been successful, why wait until 2010? Why not just put them all open for contract now and say, go to it?

Mr. HILL. That is what the RFI requires. The 2010 date is in statute, so we are sort of benchmarking ourselves against the statute——

Senator MCCASKILL. You are not supposed to do it until 2010 in the statute?

Mr. HILL. The statute requires it by 2010, and so that——

Senator MCCASKILL. But is there any rule that says you can't do it earlier?

Mr. HILL. Nope, and we would like to get it done earlier if we can.

Senator MCCASKILL. Well, wouldn't that just mean like opening it up for contracts and saying, we want you to propose coming in and doing a contingency recovery audit, like now?

Mr. HILL. The RFI for that contract is on the street as we speak.

Senator MCCASKILL. For system-wide?

Mr. HILL. Yes.

Senator MCCASKILL. And when does it have to be responded to?

Mr. HILL. I can get back to you for the record on that. I don't have all the details with me——

[The information provided for the Record follows:]

INFORMATION PROVIDED FOR THE RECORD

CMS released a Request for Information (RFI) on March 16, 2007. The RFI included a draft Statement of Work (SOW) and capability statements for small businesses. Responses to the RFI are due to CMS on April 9, 2007.

Senator MCCASKILL. The idea that we know that these are going to be successful and we know they are going to recover hundreds of millions of dollars, it seems to me that the minute you have a pilot program—frankly, I don't even know why the pilot was done. Once you know you can do it and it is legal to do it, I don't understand why every department isn't signing up immediately for these recovery audits, because there is absolutely no cost, right?

Mr. HILL. You will get no argument from me. We are very happy with the recovery audit process. The history here was some of the arcania in the Medicare statute not allowing us to do it before we had the demo, but we are very excited about it and we are ready to move forward.

Senator MCCASKILL. Is there any other department that is represented here that does not see the light in terms of recovery audits and how important they are and that they don't cost us anything to do, but they have the potential of recovering lots of money? Is there any other department that is represented here that wants to express some kind of reluctance or reticence to engage in those kinds of contracts?

Mr. NORQUIST. We use those types of contracts and they are effective and they don't cost the taxpayer, and to be clear, we use them even on low-risk programs. The answer is you use high-risk assessments, but even on programs that are low-risk, those organi-

zations bring in teams to go through and look for cases even within a low-risk program where there is an opportunity to recover funds.

Senator MCCASKILL. And, Mr. Cox, do you do it at HUD?

Mr. COX. We do not, Senator. I am very familiar with that from the private sector. Our experience at HUD, we actually had an outside party look at the potential for that and the potential, if I recall from a couple years ago, was very low. It was a couple hundred thousand dollars. And the reason for HUD is most of our contracts are firm fixed-price contracts. We have a a government transaction specialist (GTS), on each one. So we actually did a study to look at the potential, and at least in our case, an outside party conducted that and found that there was very little evidence. In fact, of the $200,000, on further review, the actual number was reduced to zero.

So the potential, and again, I am very familiar with it from the private sector, the potential at HUD, given the nature of our contracts and our funding, was very small. We will certainly look at it again, but it was very small at that time.

Senator MCCASKILL. Well, to me, it would be something that you wouldn't even need to study. I mean, if somebody is willing to do this work at no cost to the government and we get the money back, I don't know what there is to study. Now, maybe if you put it out for proposal and nobody makes a proposal, it seems to me the market has told you——

Mr. COX. Right. That is right.

Senator MCCASKILL [continuing]. That there is no chance for recovery.

Mr. COX. Right.

Senator MCCASKILL. It doesn't seem to me we need to hire anybody or have an outside consultant because the market is going to look at what the program is. All of the privatization that has gone on in our Federal Government under the guise of more efficiencies, and it just is amazing to me that there is any kind of reluctance anywhere just to let the private sector have a whack at this.

Thank you, Mr. Chairman, for giving me that opportunity.

Senator CARPER. You bet, and thanks for being with us today. Good luck in the Chair.

Senator MCCASKILL. Thank you.

Senator CARPER. They will be pretty quiet over there.

Senator MCCASKILL. They will be very quiet.

Senator CARPER. Alright. Mr. Norquist, we have a policy here, as I think the other witnesses know, that testimony should be submitted 48 hours before our hearings begin. Not everyone complied with that. A number of our witnesses did. The most egregious offender was the Department of Homeland Security, and I would just ask why?

TESTIMONY OF DAVID M. NORQUIST,[1] CHIEF FINANCIAL OFFICER, U.S. DEPARTMENT OF HOMELAND SECURITY

Mr. NORQUIST. Sir, there is no acceptable answer. We know the timeline you gave us. We know that OMB needs to review it. It is our responsibility to get it to them enough in advance and we

[1] The prepared statement of Mr. Norquist appears in the Appendix on page 88.

didn't do that. That is my responsibility because the folks working on it worked for me and I apologize to you for that. We will not do that again.

Senator CARPER. Thank you. You are recognized. Proceed with your testimony.

Mr. NORQUIST. Thank you, sir. Thank you, Chairman Carper, Ranking Member Coburn, and Members of the Subcommittee for this opportunity to testify before you regarding the Department of Homeland Security's efforts to reduce improper payments. Secretary Chertoff and I are committed to strengthening the processes needed to implement the Recovery Auditing Act of 2001 and the Improper Payments Information Act of 2002.

I also want to thank you for S. Res. 94. Your statement of support and recognition for the DHS workforce is greatly appreciated.

In 2005, the Department's improper payment testing and reporting was limited. However, in 2006, we improved our process and executed statistically valid sample test plans. They identified two high-risk programs, FEMA's Individuals and Households Program and their vendor payments. We also conducted sampling on 16 other programs across the Department, totaling over $7.3 billion in payments, and determined that these programs were not high-risk.

This year, we expand the scope and quality of our testing, and to ensure the long-term effectiveness of this program, our 2008 budget requests some additional resources so my office can evaluate the components' testing procedures. We are a new department. We will be doing these tests for a long time, and I want to make sure that as we do these tests that we are confident that they have done rigorous risk assessments and they have done quality testing. So while we have outside folks helping us, we are looking to be able to evaluate those and confirm the quality of them.

I would like to now briefly touch on our two high-risk programs. In the wake of Hurricane Katrina, FEMA tested and identified two programs under the Disaster Relief Fund as being high-risk for improper payments, the Individuals and Households Program and vendor payments. This evaluation was designed to determine if improper payments occurred, assess the cost of improper payments, and develop corrective action plans to mitigate the risk of future occurrences.

For the Individuals and Households Program, FEMA selected a statistical sample covering the period of September 2005 through March 2006, the days immediately following the hurricane, resulting in an estimate of 8.6 percent for improper payments. FEMA initiated corrective action plans to address the root causes, and this included preventing duplicate registration, confirming applicant identity, handling a high volume of transactions, and an enhancement to the post-payment reviews. Moving forward, FEMA has taken steps to strengthen compliance with IPIA and to implement OMB guidance, and so a second round of IPIA testing and risk assessment is currently underway for the payment period of March to November 2006.

Regarding vendor payments, FEMA's statistical sampling over the same period estimated 7.4 percent of total payments as improper and they have initiated corrective action plans to include enhanced training guidance for invoice processing, developing a

vendor payment quality assurance program, and reviewing contract language for consistency of similar goods and services.

In conclusion, DHS has made progress on IPIA and we are on track to make more progress this year. We will continue to work closely with Director Paulison and FEMA to strengthen their core capabilities and capacity to manage payments. We will also continue to work closely with the Office of Management and Budget to ensure continued progress in eliminating and recovering improper payments.

I appreciate the support we have had from the Congress and this Subcommittee. Thank you for your leadership and your continued support of the Department of Homeland Security. I would be happy to answer any questions you may have.

Senator CARPER. Thanks, Mr. Norquist. Mr. Hill.

TESTIMONY OF TIMOTHY B. HILL,[1] CHIEF FINANCIAL OFFICER, CENTERS FOR MEDICARE AND MEDICAID SERVICES

Mr. HILL. Good morning, Chairman Carper, distinguished Members of the Subcommittee. I am honored to be here today to discuss with you CMS's efforts to measure and reduce improper payments in Medicare, Medicaid, and the SCHIP program.

When I last testified before this Subcommittee about 18 months ago, I discussed CMS's aggressive targets for reducing improper payments in our programs and I am pleased to be here today to tell you that our efforts are showing substantial results. I want to use my remarks this morning to briefly discuss the status of our measurement programs for Medicare, Medicaid, and SCHIP, describe for you some of our corrective actions, and briefly touch on what I believe is our biggest challenge to continuing our efforts.

On the measurement front, much has been accomplished over the last 18 months. For Medicare, last year, we reported an error rate of 4.4 percent, a significant decrease from the 5.2 percent reported in 2005 and a reduction of greater than 50 percent from the error rate we reported in 2004. This is a cumulative savings to Medicare and the taxpayers of over $10 billion. With continued monitoring and error reducing efforts, our goal is to achieve an error rate of 4.3 in 2007 and 4.1 by 2009. I am happy to report that our preliminary data indicate that we are on track to meet our 2007 goals.

In the coming year, we will be adding payments for Medicare Part D and C into this calculation to bring all of Medicare into full compliance with IPIA. We have completed preliminary risk assessments and are in the process of developing pilot areas to test payment risks across C, D, and the retiree drug subsidy program. We plan to use this information from the risk assessment and pilots to report component level error rates for these programs in the 2008 PAR next November.

In Medicaid and SCHIP, we have made much progress since I was last before the Subcommittee. Last August, we published final regulations creating the Payment Error Rate Measurement Program (PERM), which requires States to assist us in measuring and reducing improper payments in Medicaid and SCHIP. We began implementing this program in 17 States across the country this

[1] The prepared statement of Mr. Hill appears in the Appendix on page 92.

past year and will be reporting an error rate for Medicaid claims in the 2007 PAR, which will be issued this fall. Our efforts will continue through the coming fiscal year as we extend our error rate calculation to Medicaid Managed Care and to the SCHIP program, and we are on track to have a fully compliant report in the 2008 PAR next November.

Let me now turn to our remediation efforts. As you know, calculating the error rates is only one step in the process. Remediation is the key to IPIA compliance. The cornerstone of our remediation efforts in Medicare is our error rate reduction plan, which includes agency-level strategies to clarify CMS policies and implement new initiatives to reduce improper payments. It lays out how we use improper payment information to manage our contractors that process our claims and to target our activities in particularly error-prone benefit-type areas.

We are also using new tools to recover improper payments. In 2004, we implemented a recovery audit contract demonstration to identify improper payments. Based on early results, we see the RAC program is an indispensible tool in reducing and eliminating future improper payments. To date, the RACs have identified more than $400 million in improper payments and have collected $144 million. We have an aggressive time table to meet the statutory requirements for implementing RACs nationwide.

We expect our remediation efforts in Medicaid to be equally robust. To reduce Medicaid improper payments that are identified through the PERM program, we will require States to submit corrective action plans that describe the actions they will implement to address major areas of concern. We expect that the corrective actions taken by States as well as our active monitoring and oversight of States will lead to reductions in the reported Medicaid rates over time.

Finally, let me turn to what I foresee is our biggest challenge as we continue our efforts in this area, and that is allocating scarce resources to fund our activities. Under the PMA, Federal agencies are mobilizing people, resources, and technology to identify improper payments. Consistent with these efforts, CMS is firmly committed to ensuring the highest measure of accountability. Unfortunately, since funding for our efforts has been capped since 2003, we have sustained a huge degradation of our purchasing power relative to inflation. Thus, to preserve our commitment to program integrity, the President's 2008 budget requests an additional $183 million in discretionary funds to build upon our programs so that we can continue our proven record for accountability.

We are proud of our results. CMS is setting the standard in identifying, reducing, and recovering improper payments. But while we continue to make great strides, there is more room for improvement. We look forward to continuing to work cooperatively with this Subcommittee and to strive to protect the taxpayers we serve and ensure financial management of Medicare and Medicaid programs.

I look forward to answering any questions you might have.

Senator CARPER. Mr. Hill, thank you very much. Mr. Bowie, you are recognized. Thank you.

TESTIMONY OF TERRY BOWIE,[1] DEPUTY CHIEF FINANCIAL OFFICER, NATIONAL AERONAUTICS AND SPACE ADMINISTRATION

Mr. BOWIE. Chairman Carper, Senator Coburn, and Members of the Subcommittee, thank you for the opportunity to appear today to discuss NASA's progress in identifying, eliminating, and recovering improper payments. In my testimony today, I will outline the steps NASA has taken to address improper payments, including complying with the Improper Payments Act.

I would like to briefly explain the composition of NASA's contracts and how that affects our payments. Contractors support the execution of many of NASA's research and development programs. The variable and often unpredictable nature of this complex R&D work leaves NASA to use cost versus fixed-price contracts. While both contracts are used in various NASA programs, cost contracts represent approximately 88 percent of payments made and fixed-price contracts represent the remaining 12 percent.

NASA has implemented a multi-pronged approach to oversee integrity of the payments for its R&D programs and associated contracts. Effective contract and financial process controls represent one element of our approach and are the cornerstone of NASA's efforts to ensure proper payments.

As an important second element to our approach, the Defense Contract Audit Agency (DCAA), reviews cost contracts and our contractors' adherence to accounting controls and requirements. For cost contracts, the DCAA also conducts contract close-out audits that may identify questionable costs. Any questionable costs are then reviewed by the NASA contracting officer for resolution.

As a third element complementary to our program integrity activities, the agency has established an Acquisition Integrity Program. This program was formally launched in December 2006 by NASA's Deputy Assistant Administrator, Shana Dale, and this is a collaborative effort among the Office of the Inspector General, the Chief Financial Officer, General Counsel, and procurement.

Finally, in accordance with the Improper Payments Act and consistent with OMB guidance, NASA, as well as other agencies, is required to complete an Improper Payments Risk Assessment. For its fiscal year 2006 risk assessment, NASA used the results of the prior year's recovery audit. Through that process, NASA reviewed approximately $57 billion of cost and fixed-price contracts across all programs dating back to 1997. Based on the results of that assessment, NASA found the total value of improper payments that had not already been identified and reported in prior years to be $256,255. This formed the basis for the amount reported in our fiscal year 2006 Performance and Accountability Report. In that document, NASA reported that the agency's risk assessment and actuals represented for the past 3 years had shown NASA's improper payments to be less than a benchmark 2.5 percent of program payments and less than $10 million.

There have been several observations regarding questioned questions and the relationship to improper payment figures reported in NASA's PAR. Questioned costs are not analogous to improper pay-

[1] The prepared statement of Mr. Bowie appears in the Appendix on page 106.

ments. Rather, they are costs that NASA's Office of Inspector General recommends be reviewed by NASA to determine validity. There are more categories of possible questioned costs than exist for improper payments, and since these audited questioned costs are not always sustained, the IG report would have a higher figure for questioned costs than the amount that would be reported in terms of improper payments.

For fiscal year 2007, NASA's risk assessment approach incorporates all the lessons learned from the prior year's audit, recovery activities, and incorporates OMB's instructions in their memorandum dated August 10, 2006. This risk assessment addresses disbursement activities on programs based for both cost and fixed-price contracts. A statistically valid sample of payment transactions will be obtained and tested, after which NASA will report the results.

We have taken steps to bring our program into compliance with OMB guidelines for implementing improper payments, the Improper Payment Act. We will continue to adopt lessons learned for future recovery audits to make sure that we are making the most of those efforts.

In closing, NASA is fully committed to ensuring that the agency's payments are properly made and that the agency fully complies with the Improper Payments Act. Mr. Chairman, I am pleased to respond to any questions you or other Members of the Subcommittee may have.

Senator CARPER. Thanks, Mr. Bowie.

We have at this table a number of agencies whose improper payments are measured annually not in the millions of dollars or the tens of millions of dollars, but literally hundreds of millions of dollars. We have heard of the efforts that have been launched particularly in HUD and CMS to go out there to identify those improper payments and to reduce them, to recover monies that have been improperly paid.

When I read your testimony and listening to it again today, what I take away from it is that you have identified in your agency—roughly what is your agency's budget on an annual basis?

Mr. BOWIE. Roughly $16 billion.

Senator CARPER. How much? Sixteen billion?

Mr. BOWIE. Sixteen billion, yes.

Senator CARPER. What I took away from it was the belief that there is really not much, given the way that you award contracts and the work of your contracts, in the way of improper payments that are made, and I think I heard the figure $250,000. I don't want to put words in your mouth, but it sounds like you have looked at your payments and you just don't think, at least with respect to your agency, that it is a problem.

Mr. BOWIE. I believe that we have to always be vigilant in terms of ensuring that taxpayer dollars are properly accounted for and we will look and judge every dollar based upon that. We would not automatically assume that there are no problems. There always could be an issue and we will always be vigilant to tackle those issues as they arise.

Senator CARPER. But as you look back at 2004, 2005, 2006, what I take away from your testimony is that you don't believe there are

any really material problems with respect to mispayments, overpayments, or improper payments?

Mr. BOWIE. In looking at the criteria as established by OMB for reporting, the 2.5 percent or over $10 million, that would be the conclusion.

Senator CARPER. Mr. Williams, let me just ask you to reflect on that for a moment, if you would.

Mr. WILLIAMS. Mr. Chairman, in listening to the testimony, as I was reflecting back to the 1980s when President Reagan and President Gorbachev used to get together and President Reagan used to always tell President Gorbachev to trust but verify, and I have this professional skepticism, I guess, that is just basically ingrained in the work I do.

In reflecting back on the point that I made earlier, in listening to some of the statements and looking at what the auditors had reported, it makes me want to reiterate the other point that I made, that while not required, it would be a good idea at each one of these agencies that independent set of eyes would be required to take a look at this process, because I am looking at a couple of the agencies and I think the auditors basically stated that there was a potential non-compliance at NASA, I believe, because of the supporting documentation that they questioned. I think at Homeland Security, the auditors basically stated that the risk assessment was not performed for all of the programs and I also think that there were some questions raised about the sampling at that particular agency.

And I think, in conclusion, we kind of get back to this issue that we talked about earlier, also, of this $10 million and 2.5 percent criteria. As I have stated in previous testimonies before this Subcommittee on that particular issue, I was involved, or I was asked to take a look at the original drafting of the legislation, and as I have stated, it originally started out at $1 million. It was any agency that had improper payments of $1 million would be required to go through the steps that are listed on the board up there. Looking at it from a cost-benefit standpoint, we did suggest, and our suggestion was taken into consideration, to raise it to $10 million.

So I have a little bit of institutional knowledge of what the Congress was intending in this area and I think that not just members on this panel now, but if you look at some of the other agencies that have looked at this issue, I think when you throw in the 2.5 percent criteria and the word "and," it kind of takes some of these issues below the radar screen.

Senator CARPER. Alright. Thank you.

Mr. Cox, if I could come to you. In Ms. Combs' testimony earlier today, I think she held out HUD as an example of an agency that has done a good job in trying to identify improper payments and eliminating them. I just want to ask you to briefly sketch for us some of the best practices and processes you think that you have adopted over the years to address improper payments, to try to reduce them, and is there something in that list that you all have done that maybe some other agencies, including some at the table, but a number who aren't at the table, could emulate?

Mr. COX. Thank you, Mr. Chairman. I think if you look at the large area for us of improper payments, it centers around our Rent-

al Housing Assistance Program, and there are really three areas that we look at to determine improper payments. The first is, is this subsidy itself calculated correctly? Second, is the tenant's income reported correctly? And third, once we have determined one and two, have we been billed correctly for what was determined in step one and two?

The biggest efforts—and I will set aside No. 3 for just a second, but the biggest efforts we have made is to, first of all, educate the public housing authorities and the multi-family owners on the complexity of those calculations. They are very complex. There are over 40 income deductions and exclusions, so that is a very complex, not unlike the tax code.

No. 2, probably our biggest success, and I would say, Mr. Chairman, where other agencies could use it, is our income verification system. Working with the Department of HHS and Social Security, we actually get secure data off-line but then put on-line on a public housing authority by public housing authority basis, and they are able to verify what the tenant has told them is their income, which is a key component of determining what the subsidy could be.

Senator CARPER. Excuse me for interrupting. A long time ago when I was a member of the House of Representatives and served on the Banking Committee Housing Subcommittee, one of the things that I focused on was tenant income verification and we were trying to make sure that, given the fact that you had a lot of people in waiting lines to get into public housing, we wanted to make sure that the folks that were there were actually income-eligible. We tried to figure out, working with the State and local folks, how best to make that verification, do so in a way that was respectful of people's privacy rights but also in a way that would enable us to quickly and regularly make an identification of who was appropriately there and eligible and who was not.

My recollection is that we used Department of Labor data from folks who were employers that were paying, had people on their payrolls, and submitted on a regular basis employment data, and I don't think you mentioned that. I think you said that you were doing it through a couple of other things. How do you do it today?

Mr. COX. We used the National Registry of New Hired Data, which is now captured by HHS, and so we used to use Department of Labor data, but there were some delays in reporting on a quarterly basis and in some cases even on an annual basis. So the information that we have today, Mr. Chairman, is actually more current, or is the most current that we can get.

Senator CARPER. Alright. Do you want to add anything? I interrupted you. Do you want to complete your thought from earlier?

Mr. COX. I would just say, again, any program that is based on income—ours clearly is, the majority of ours, but I would say—you asked the specific question, what can other agencies look to, I would say this is a good example of both interagency cooperation as well as working with our industry partners and that is a big success story here to reduce improper payments by over $2 billion since 2001.

Senator CARPER. Alright. That is a lot of money.

Mr. COX. It is a lot of money.

Senator CARPER. Thank you. Again, if I come over to Mr. Hill for a moment, if I could. We are going to hear, I think, on the next panel some testimony that CMS serves as an example of how a successful government audit recovery program can be run and should be run. I just want to ask you to provide us with your perspectives on why the recovery work underway in Medicare has been successful and describe your plans to expand this program. I know you spoke just a little bit in response to Senator McCaskill's questions, but how do you plan to expand this program beyond the three States which are now underway? And also, do you have any sense for how much money could be saved once you are doing this nationally, not just in three significant States, but in all 50 States?

Mr. HILL. Thank you. We plan on having our national RACs up and running. We are going to chunk the country up a bit. We are not going to have one contractor do the entire country. We will sort of set up some regions and describe in a general way who will be responsible for which area.

There is a procurement, a request for comment on the street. It is a little special in terms of the work that has to be done. It is not like looking at a vendor payment or an invoice. We are looking at actual medical records and claims that are coming in from providers and beneficiaries and so we want to be sure the RACs have the appropriate medical skills on staff to be able to review those claims and to be able to do that work, and so there will be some review of the contracts as they come in.

We expect to be able to have those contracts out and let and beginning to run in calendar 2008. That is our timeline.

A significant issue for us as we roll this out nationally is educating and working with the providers and the beneficiaries we serve, because this is a new entity that is sort of going to interject themselves into the Medicare system, and physicians and hospitals are going to be getting letters from companies that they have never heard of before saying you owe the Federal Government some money, and so we want to be sure that we have done all the appropriate leg work there to be sure that there is no surprises.

In terms of the money to be saved, I mean, we have identified just in the three States in the short time that we have been doing it, $400 million in overpayments, and I think a lot of that has——

Senator CARPER. Say that again? How many?

Mr. HILL. Four-hundred million dollars.

Senator CARPER. And was that for 1 year or several years?

Mr. HILL. Since January 2005, so it is over several years. But again, it has taken a while for them to get up, get familiar with the data, get familiar with the areas that they are going to be working in, so we have seen that grow over time. Month to month, it gets higher and higher. I expect that the recoveries will, I am hoping, certainly get into the "b"s, out of the millions and into the billions, over time. When that will start and how soon we can get there remains to be seen, but we are anxious of get started and we are anxious to continue the relationship we started with these contractors.

Senator CARPER. Thank you. Talk with us again a little bit about improper payments with respect to Medicaid and the SCHIP program. What kind of timeline are you on there?

Mr. HILL. Right now, we are out in the field collecting data and measuring rates in 17 States. We had some sort of fits and starts getting going with Medicaid. We finally got our final regulations out in the summer of 2006, sort of articulating exactly how we are going to implement the IPIA for the State programs, and the way we are doing it is in a phased, cyclical approach. So we will do 17 States each year to get to all 50 over a 3-year cycle. We began the first 17 this past year.

We will be reporting on those rates in this year's PAR and that is for one component of Medicaid, the biggest component, the fee-for-service component. For the Medicaid Managed Care piece, which in some States is big but nationally it is a smaller piece, and SCHIP will be done beginning in fiscal year 2008 for a report next year, in next year's PAR.

The challenge for us here has been, of course, as folks have identified already, is dealing with 50 different States and 50 different entities and setting up a process that ensures we get the data we need to do the appropriate calculations but sort of does it in a way that the State is sort of working cooperatively and has the incentive to be sure that they give us that data. Quite frankly, some of the comments that we got from some of the States on the regulations that we put out were less than favorable in terms of them viewing this as a State activity versus a Federal activity, so it has become quite a challenge to sort of convince them that, yes, this is, in fact, in their best interest to do this measurement and help us do the assessments.

Senator CARPER. Alright. Dr. Coburn is back, so why don't you just jump in and take as much time as you would like.

Senator COBURN. Thank you.

Senator CARPER. We have, I think, one more panel.

Senator COBURN. Mr. Bowie, in your statement, you described that NASA conducted last year's risk assessment—let me put the poster up here—for its 2006 risk assessment, NASA used the results of the prior year's recovery audit. Through that process, NASA reviewed approximately $57 billion of cost and fixed-price contract payments across all programs dating back to 1997. Based on the results of that assessment, NASA found the total value of improper payments that had not already been identified and reported in prior years to be $256,000. This formed the basis for the amount reported in the fiscal year 2006 PAR document. You also reported in that document that the agency's assessed risk and actual results for the past 3 years have shown NASA's improper payments to be less than the benchmark of 2.5 percent of program payments and less than $10 million.

I have some concerns with this risk assessment on several levels. First of all, I am kind of fuzzy on how you conducted this assessment. So what I would like for you to do is break that down for me sentence by sentence. First is, NASA used the result of the prior year's recovery audit. First of all, how is that a valid risk assessment for present? We already had the GAO testify that recovery audits are the more expensive way to do that. The least expensive is have the program integrity there in the first place. It lacks the depth and detail necessary to carry out a thorough and comprehensive review of the entire agency because you are limiting

that to programs of $500 million to begin with. That is what the recovery audit requirements are.

So the IPIA mandates that the entire agency and all of its programs perform an improper payment risk assessment. Do you believe the results of an improper payment, this passes muster for a valid risk assessment?

Mr. BOWIE. For 2007, we will be doing a very robust risk assessment. For 2006, since we did have the recovery audit that examined basically all contracts dating back to 1997 and there was no dollar threshold imposed on that, so it was open, that we felt that if we had, even in doing a risk assessment, we would have still projected similar results as the actual results of the audit themselves.

Senator COBURN. What was found in the recovery audit? How much money was found in the recovery audit?

Mr. BOWIE. For the recovery audit, it was approximately that $256,000.

Senator COBURN. That is all that you found going back to 1997? In your recovery audit, you found $256,000 in payment errors?

Mr. BOWIE. That had not already been resolved or corrected.

Senator COBURN. I know, but that is my whole point. What was the amount that had already been resolved or collected?

Mr. BOWIE. For 2004, it was $70,000. For 2005, it was $617,442.

Senator COBURN. OK. So your testimony is that for NASA, your total payment errors, your estimate of your total payment errors is this $256,000 plus $70,000?

Mr. BOWIE. And the $617,000.

Senator COBURN. Six-hundred-and-seventeen thousand dollars.

Mr. BOWIE. Those are for past years.

Senator COBURN. OK, but your risk assessment by law has to be for every year. So you are using a recovery audit to state an assessment of 2006. Mr. Williams, what do you think about that?

Mr. WILLIAMS. Dr. Coburn, as you know, this Subcommittee has requested GAO to take a look at NASA and the scope of that particular work is basically looking at how well did they go about doing their risk assessment. From looking at the numbers and what we have in our report, in 2004, there was no report, and the $70,000, I guess, is the number, while it wasn't reported.

But when you add these two numbers together—and as I stated earlier, we believe that the risk assessment is the foundation of this whole exercise that we are going through, and using recovery auditing, as I stated in my written testimony, even using the single audits, we don't think that those are good bases for going about doing a thorough risk assessment that is needed in order to do the things that need to be done to properly identify those programs that are susceptible to significant risk.

Senator COBURN. Don't get me wrong. I love NASA, OK. I just hate waste. I have trouble believing that on a $56 billion program, that is the amount of waste that was there in terms of improper payments when I look across all the rest of the Federal Government and don't find hardly anybody that can compare to that. And I know that NASA is good, but they are not that good. So I have real doubts about the accuracy of what you are reporting and also whether or not—and I would tell you, by law, a recovery audit does not pass muster with what the law states on the Improper Pay-

ments Act. You can read that. I have introduced that into the record. You heard me do that.

Is it possible that NASA could commit to fulfilling what GAO would like to see in terms of a recovery audit for next year?

Mr. BOWIE. That is our intention.

Senator COBURN. OK. So you are going to do a true risk assessment next year?

Mr. BOWIE. Correct.

Senator COBURN. Well, that is great to hear.

Mr. BOWIE. That is already in place and we have already done the first phases of that risk assessment by program and we are moving to the test phase.

Senator COBURN. That is great. Mr. Chairman, I have heard what I wanted to hear.

I would like to submit the rest of my questions so that these people don't have to wait such an extended period of time, and I apologize for my absence during your testimony.

Senator CARPER. That is quite alright.

I want just to follow up on what Dr. Coburn said. I hope the amount of improper payments are as low as you have suggested here, and if they are, maybe we will ask you to come back and we can figure out how the rest of the Federal agencies and States can learn from what you are doing.

Mr. Williams, we look forward to the closer scrutiny that you all are going to take with respect to NASA and we will see what we can find.

A couple of questions, if I could, for Mr. Norquist from Homeland Security. First of all, one of the issues that has been raised by GAO, and I think by your auditors, is that your Department has not yet performed risk assessments on all of its required programs to determine whether they are susceptible to improper payments. When do you expect that work is going to be completed?

Mr. NORQUIST. Sure. That is a great question. Two years ago, they asked the components to look at the risk and basically everyone answered, we are not high risk. That was considered not an adequate answer, so last year, they simply used a dollar threshold. Whether you think you are high-risk or not, if you are spending in certain areas over a certain amount of money, do the sample testing, and there were 16 more programs where we did that. The numbers came in with error estimates of less than $1 million, but we felt it was worthwhile to do that test even where people weren't asserting it.

This year, we have issued the guidance to do a proper risk assessment. We will be working with our organizations to make sure they do that. We understand the dollar threshold alone is not an adequate substitute for risk assessment. My predecessor thought it was better than accepting the answers he had been receiving previously about what was risk. But we are going to work with the components to ensure that the risk assessment is done consistent with the law.

Senator CARPER. Alright. Thanks. I understand that as a secondary measure to help improve the Department's improper payments, that recovery audits were being performed at three of the Department's components. At the time of your improper payments

reporting for the last fiscal year, fiscal year 2006, however, the recovery auditing work had progressed but was not yet at a point where it could yield any kind of conclusive results. Discuss with us for a minute or so, if you could, the current status of that work and the results that have been yielded.

Mr. NORQUIST. I would be happy to, sir. At the end of last year, they had a challenge getting some of the recovery audit teams on board. There was a clearances issue. In most of those cases, they are on board and operating, and while we only have them in a few components, those components are service providers and do the finance and accounting for a number of other organizations in DHS, so it is a much broader group.

Those efforts are ongoing at Coast Guard and ICE, and I will have to get the number for the record, but there are several hundred thousand, I believe, that was being reviewed at Coast Guard as potential candidates for recovery. Again, not enormous sums, but sums worth following. These are not high-risk programs, but as I mentioned to the Senator before, they are programs that are worth looking into because there is the opportunity to recover as long as you have the recovery audit teams working alongside you.

We expect to have all those teams in place for this year, and again, they are going back over 2004 and 2005 payments, as well.

Senator CARPER. Alright. A couple of people made the point in their testimony, I think Mr. Williams among them, that it is all well and good that we do risk assessments. It is good that we identify improper payments that were made. It is good that we go out and recover after the fact monies that have been misspent, inappropriately spent. But the best thing we could do is to make sure that we don't make the mistake in the first place. Take a moment and talk to us about what Homeland Security is doing in that regard.

Mr. NORQUIST. OK. Well, let me do a couple of things. The biggest area, the highest-risk area was in FEMA's Individuals and Households payments. That was the program that last year's sample fell right during the start of the response to Hurricane Katrina, and so you had a number of issues that contributed to that.

First of all, given the immediacy of responding to people's needs and the sheer volume of people they had to assist, they relaxed some of the controls to put an emphasis on helping people, in addition to which some of the controls one would like to have in place—a person goes and visits the individual, visits the location—were not possible because of the extent of the damage. So that resulted, when we tested that, as clearly showing up on our high-risk list.

FEMA has put in corrective action plans. We have published those in our PAR. They also include putting in—when you have this surge in applicants, people started coming in registering on the phone and on-line and not all of those had the appropriate controls to check, was it the right individual, were we getting duplicate registrations, and so FEMA has been putting in the controls in those places to both put the strong controls in up front, recognizing they are going to happen during a surge in activity, during a point of urgency, and still trying to strike that balance but yet——

We have a process underway to recoup those funds, but again, it is a long, slow process and it is much more effective to be able to have those controls in place on the front.

Senator CARPER. Alright. Mr. Williams, any comment in response to what Mr. Norquist just said?

Mr. WILLIAMS. Mr. Chairman, it seems like after each one of these, I make the same statement, but we do have a review underway also looking at improper payments at the Department of Homeland Security. That job is currently underway and we are looking at the basic steps that we have talked about up there.

I would like to add that in talking about the last point that you made there, about it is better to prevent improper payments from occurring, I would also like to add to that statement that in our previous testimonies, we have always talked about that if you trace down the root cause of these improper payments, it goes back to a breakdown in internal controls.

There is also another component to that and that is also you get improper payments when programs are poorly designed. So that is something that we also need to take a look at, and by that I mean that if you have got a program that is set up in such a way that you basically open yourself up to improper payments from occurring, we need to take a look at some of those designs, also.

Senator CARPER. Alright. Thanks.

Mr. NORQUIST. If I can join in, that is an excellent point. The entire control environment matters. One of the initiatives that we have started at Homeland Security in our financial field is everyone who is a new hire, regardless of whether they are hired by my office or one of the components, we brought them in last week for a week of training and we gave them, among other things, training on fiscal law and internal controls because they need to be aware of their responsibilities in that area, and if you can do up-front training of the employees, if you can have adequate controls in place, you dramatically reduce the amount of effort we have to put on the recoupment and recovery side, and I think that is a very good recommendation to respond to and that is one we have tried to tackle.

One quick correction. I misquoted on the Coast Guard. It was 19 cases and $134,000 that their recoupment team had identified so far.

Senator CARPER. Alright. Thanks. The last question I will ask, and I will start it with Mr. Hill. Last week when we were debating the budget resolution in the Senate, Senator Coburn and I offered, and it was adopted, legislation that says that to the extent monies are recovered in the next several years from improper payments, those monies should be used for deficit reduction. It was unanimously accepted, without objection.

When I think about our efforts to try to get States to be our partner in some of these programs, Medicaid, SCHIP, and others. I don't want us to be saying that we have somehow tied your hands or the hands of the States or others that are administering these joint programs with States. I don't want to feel that we have tied your hands by saying, none of the monies that have been recovered can be used to incentivize the States to be our partners. I just want

to ask if that is a fear that may be misfounded or not, and Mr. Williams, I would ask you to respond, as well.

Mr. WILLIAMS. I would like to start with it, and I would like to refer to the Food Stamp Program, in which there are bonuses and there are penalties in this particular area. States receive bonuses if they get that number down and there are also penalties that have been mandated by the Federal Government, that if your improper payment rate is above the national average, I believe it is. So the Congress has put some things in place that will, in my opinion, bring the States to the table to realize that we are in this together.

Senator CARPER. As a former governor, I remember full well how those carrots and sticks work. [Laughter.]

Mr. Hill, let me ask you to respond.

Mr. HILL. As Mr. Williams said, I think the carrot and stick approach is one that we have to employ. Unfortunately, I think that to the extent that, say, for example, we have an improper payment recovery in Medicaid and now under the resolution it is going to deficit reduction. The State's first reaction to me is going to be, well, it is not my deficit. It is a State dollar that is now going somewhere else.

So I think the real trick for us is going to be, and it has been and will continue to be sort of being sure the States understand—let us use Medicaid for a minute—a dollar saved on Medicaid or a dollar recovered in improper payments, on average, 50 percent of it is going back to the State and 50 percent of it is going back to us. The more we can sort of build that into the relationship and be sure that the States are seeing the incentive and the pay-back that they are going to get from investing in these kinds of activities, the more likely they are that they are going to invest in them.

At the same time, I do think, ultimately, there will need to be a stop-gap, because you will get a State out there or somebody will say they don't want to make the investment, or they may think that the recoveries that we are getting aren't big enough to make the investment, and I think at some level, the Federal Government is going to need to be able to step in with the stick, if you will, and say, well, you need to. Whether it is a penalty or however we build that policy, there needs to be some of that sort of pain going back the other way if there is not the appropriate reaction, and unfortunately, that is not in the IPIA now. It is the sort of Federal—it is going to require some unique solutions by program to be sure we can be compliance by program.

Senator CARPER. Alright. Thanks. Anybody else want to respond on this particular point? Mr. Cox.

Mr. COX. Senator, I would just say that we have a similar issue, except instead of dealing with States we are dealing with 4,100 public housing authorities and over 22,000 individual private property owners. So again, it is going to be challenging to incent them. Now, we do have, as others have mentioned, Mr. Hill mentioned, we do have some sticks. We believe, like Mr. Williams, the best way to do this is on the up-front and it is a process, an internal control issue, and we do have a couple of sticks there where we can actually monitor use of the Enterprise Income Verification, the new web-based system, and if you are not using it, actually, we can re-

duce some of their administrative fees that they receive. So there is a little bit of a stick there that we can use.

But I would say, in general, your general question of can we assume that they will take some of that or not sit back while we take the rest for deficit reduction, as much as I support it, I think our industry partners and private owners are not going to sign up for that.

Senator CARPER. Alright. My last question for this panel would be, and this is a question I ask of a lot of panels, we expect a lot of the agencies in terms of complying with the law. I think in terms of being able to comply with the law, it has to be a reasonably law, reasonably explained. We need enforcement and someone like GAO looking over the shoulders of the agencies to make sure that you are doing what you are supposed to under the law. There have to be some incentives for you to comply. You need strong leadership in order to comply and you need the kind of systems that will enable you to comply.

And we have a role to play, too, in oversight, in putting a spotlight on those agencies that are doing a particularly good job and to ask of you, how can we learn from your good performance, and from those agencies that aren't doing the kind of job that we want or, frankly, that they know they ought to do, to put them on really a little bit of a hot seat.

The last question that I want answered is what further do we need to do, not just this Subcommittee, not just this Committee, but the Congress and the Legislative Branch? What do we need to do? Mr. Hill, I think you may have spoken to this a little bit in one of your comments, but let me just close by asking, what further do we need to do to better ensure that the Improper Payments Act is complied with, that the monies that are being inappropriately spent, misspent, that we will continue to reduce that, in some cases start reducing it in certain agencies?

Mr. HILL. Right. Two things I think I would say. The first is, I think, your continued oversight is needed. I think it is very helpful. Anybody who sits in a CFO job will tell you that in many ways, our job is as much persuasion as anything else, getting folks in program components or States or others to pay attention to things that we believe they need to pay attention to, even if it is in the statute, and to the extent that the Congress is taking an active role in overseeing and ensuring we comply, that makes our jobs that much more easy to implement this law that needs to be implemented.

The other piece I would mention and I mentioned in my testimony, this is not a cost-less exercise. It is an expensive exercise. The recovery audit contracts are a tool that are helpful when you are recovering overpayments, but they are not a tool that is helpful when you are trying to comply with the other pieces of the statute. The President's budget, as Ms. Combs mentioned and I mentioned, includes some requests for additional funds to continue these activities over time. I know that in both the House and Senate budget resolutions, there has been room included for those activities and I would encourage you to encourage your colleagues to continue to look upon that favorably.

Senator CARPER. Is there anybody at the table who agrees with that? [Laughter.]

Mr. COX. I would just say, Mr. Chairman, we would not have been able to reduce improper payments 60 percent without the use of technology. It just simply would not have happened. And if you look at how we do risk assessments, we have to use technology. So I would echo Mr. Hill's comments. For a relatively low investment, in our particular case in our working capital fund, we get a huge payback for that. So that is one thing that Congress can help us out with.

Senator CARPER. What would be helpful here, and I don't know who to direct this to, I will just direct it to you, what would be helpful in trying to make the point when we get into the back-and-forth on the appropriations bills and how much to actually appropriate in accordance with the budget resolution that we have adopted would be to know what that payback is. For, what did you say, $160 million that the Administration was asking for, for every one of those dollars, what is the return to the Treasury? That would be very helpful. If you could help us with that, I would be grateful.

Mr. COX. Alright.

Mr. NORQUIST. Senator, on that theme, this is—those of us who work on this, this is why we do this for a living. We get to protect the homeland, in my position, and we also get to help protect the taxpayers' dollars. It is sort of the passion we bring to this work.

But the description of the initiatives does not come across as sexy. I mean, phrases like "acquisition workforce training" in a budget request will not grab attention, but it is the front end of the type of controls that GAO and others are talking about. And you will see them in accounts with unexciting names like "management," and so as you are working through this, particularly things like appropriation and authorization bills, keep in mind that some of the initiatives that have these payoffs have relatively unexciting titles and to be able to help ensure that as they go through, that people recognize the payoff there. That would be greatly appreciated by everyone.

Senator CARPER. My colleagues and I don't always appreciate some of the terms that you may have just mentioned, but we do appreciate a $20 return for $1 invested, so that is the kind of thing that could be very helpful as we debate these issues going forward.

This is a work in progress. As you know, we have been working on this for about, I guess this is about the fifth year since the law was adopted. In some respects, I am encouraged here today by the work, the good work that is being done that is represented by a number of your agencies. I think for some of you, you have got a whole lot of work ahead of you, but I am encouraged that you are beginning to take those responsibilities seriously, not seriously enough to help all those folks who are going to be mailing in their tax payments on April 15, but it is good to know that some help is not just on the way, but some help has actually turned up some dollars that we can use to reduce budget deficits and our tax burden.

As I said at the beginning, everything I do, I know I can do better, and I think that is probably true for all of us. We appreciate

the work that you are doing and we just urge you to continue it and to go from those three States with Medicare to another 47 and let us get started on Medicaid and SCHIP, and Homeland Security, you have got your work cut out for you. Mr. Bowie, I hope that NASA is as good as you guys think you are. We will find out in the times going forward. Mr. Cox, thank you for giving a trip down memory lane to recount an old war tale on tenant income verification. Thank you all.

We are now pleased to welcome our very patient third witness, Mr. White. Thank you all.

Lee White, you are a good man to come and to have been as patient as you have been and to share with us your testimony. The room has begun to empty out, but I think in reading the testimony, a lot of it was valuable for me, but I think maybe the most valuable and instructive testimony that I read in preparing for this hearing was your own testimony. While there may not be many people in the room right now, believe me, I very much look forward to what you are about to share with us and you are recognized for 7 minutes. You are the Executive Vice President for U.S. Operations of PRG-Schultz, is that right?

Mr. WHITE. Yes.

Senator CARPER. First of all, tell us a little bit about that, about your firm and what you all do, and after that we will start the clock and you can present your testimony. But thank you for coming and thank you for your patience.

TESTIMONY OF LEE WHITE,[1] EXECUTIVE VICE PRESIDENT FOR U.S. OPERATIONS, PRG-SCHULTZ INTERNATIONAL, INC.

Mr. WHITE. Thank you, Mr. Chairman and other distinguished Members of the Subcommittee. PRG-Schultz is the largest recovery audit firm in the United States.

Senator CARPER. How long have you all been around?

Mr. WHITE. Well over 20 years.

Senator CARPER. OK.

Mr. WHITE. And recovery audit has become an accepted part of American business. Large corporations as well as mid-sized corporations have embraced the process and it has evolved over time. It used to be that people audited literally out of boxes, looking at invoices and contracts, but now it has become quite sophisticated and we literally evaluate billions of transactions that are very data-intensive and we use proprietary methods and approaches for how we do that.

Each year, we audit many of the Fortune 100 and other companies and we review over $1 trillion of their spending transactions representing approximately 7 percent of GDP, and for them, we recover over $1 billion. So it is quite significant and it has evolved, as we discussed. Our corporate clients have really found that the effort that they expend to support this process is justified, and as my testimony indicated, they view that the juice is worth the squeeze.

Senator CARPER. Now, when I read that, the juice is worth the squeeze, where did that come from? Is that yours, or is that——

[1] The prepared statement of Mr. White appears in the Appendix on page 51.

Mr. WHITE. It has been going around our company and our industry for a while, and I think it has everything to do that if you squeeze an orange, you are really looking for the juice.

Senator CARPER. Well, I am going to use that one. I guess I don't have to attribute it to you, though, so——

Mr. WHITE. Absolutely not. You may feel free to use it any way that you see fit.

Senator CARPER. Thank you. Alright. Thanks.

Mr. WHITE. Recovery auditing in government, I think equally represents a great potential. I think the opportunity is to apply the same principles and practices that we have been applying in the commercial marketplace, along with state-of-the-art technology, to the incredible complexity and also volume of spend that is represented by the government agencies, both that previously testified here and then the rest that exist.

We also recognize that recovery auditing is a tool and it is not a panacea. I think that the agencies as well as the GAO and OMB did a good job of describing the other efforts that they are expending. Even the IPIA obviously speaks to the risk assessment and other vehicles that need to be employed to truly get your arms around the totality of the issue. So we are only one tool and certainly should not be viewed as a panacea.

With our successful corporate clients, we find that a number of different things have to be available to create a rich program. They include massive databases of their transaction history. They usually have large and complex spending environments and they do have central management of that spend. The same characteristics exist in government, and therefore, I think that they lend themselves to the same type of approach.

We have entered into contracts with GSA, HHS, the Departments of Justice, Transportation, Defense, Interior, State, and Agriculture, so we do have quite a bit of experience in the government sector, and to date, we estimate that contingency recovery auditors government-wide have returned over $600 million to the taxpayer. However, we believe we could have done much better and we believe that the greatest success will come when agencies make recovery of overpayments a significant priority and where they are willing to provide us access to data and then the support we need to successfully do our jobs. Where that prioritization is not there and where the access to data has been lacking, we haven't had good results.

Our experience is that motivation is key and incentives are really an important part of that motivation. We find that with the profit motivation most of our corporate clients have, and their obligation is to serve their shareholders, they really look to get the money back and it is a very important part of it. So even if they are not trying to do anything else, just recovering the money is a sufficient motivation and causes the behavior that you would expect. If we want the agencies to have that same sort of motivation to use recovery audits as a tool, we believe they need to be incentivized as well.

We did highlight in the written testimony that we believe that to be a very successful program, although it was a pilot program, it was exemplified by CMS. There, as Mr. Hill testified, they identi-

fied over $400 million in recoverable overpayments and they actually have recovered $144 million of that so far. That is only operating in three States, and as a participant in one of those States, there is a significant ramp-up period to get started and to create the relationships, analyze the data, actually identify potential overpayments, and do all the things associated with recovering it. We would be happy to tell you that we have not yet hit our stride, and therefore we don't believe that we're necessarily close to the total potential that exists.

CMS officials have proven to be very motivated and willing partners and they have helped reduce the normal start-up kinds of things that you would expect as well as other impediments that might have kept us from being as successful as we would like to be.

So incentives are a very important element, but they are not the only element, and we believe that access to data, recovering valid claims, and helping resolve any disputes are the rest.

Because I am running short on time, I would really like to bridge to the recommendations we made.

Senator CARPER. Let me say, my time is yours, so if you need a little extra time, you have got it.

Mr. WHITE. Well, thank you very much. I will try to keep it brief.

As part of the Improper Payments Information Act, we think it would be good for agencies to be required to report on their recovery audit efforts; where they have contracts in place, whether they are using internal or external resources, what their results are, what efforts they have made to remove impediments, and then finally, what instances have happened where overpayments were identified but, for one reason or another, they elected not to pursue them. We think that would add teeth and clarity to the Act and, therefore, provide more information for analysis.

We suggest establishment of a joint industry and OMB task force, which would be comprised of key agency officials and recovery audit firms, like ourselves, so that we could establish the scale of collectable overpayments, overpayments that are conducive to recovery audits, to look at standardized protocols that could be applied, contracting vehicles, those types of things, and then ultimately to develop a road map for removing those impediments that might exist so that everybody could benefit from the experience that each group may be having individually.

We also believe that the recovery audit process should be institutionalized as part of the traditional internal government erroneous payment identification techniques. We think it augments the other sampling and risk analysis techniques that exist and can provide collaboration and validation of the amounts that are being identified and may help address some of the questions that were raised about the NASA numbers to see if they could be independently verified as they use recovery audit to generate them in the first place.

Along these lines, we think that a contract vehicle and a standard set of protocols could be developed which could lead to a government-wide disbursement audit of all centralized payment facilities.

Picking up on the CMS theme, we did suggest that we believe the same approach being used in Medicare can be applied to Medicaid. We think the key thing there is to provide incentives to the States. Although in aggregate 50 percent of the dollars that may be recovered could accrue to the States or could accrue to the Federal Government, in practice, sometimes the amount recovered actually accrues directly to the Federal Government and the cost associated with us as well as any resources necessary to support the program accrue to the State. So they actually are hindered and not rewarded for their recovery efforts and we think there are ways to create incentives that would ameliorate that concern.

To provide the incentives we think are so critical for motivation, we believe that agencies should be allowed to keep a portion of the funds that are recovered in order to be able to be reinvested in efforts to reduce erroneous payments. One mechanism would be to create a Government Efficiency Fund, where recovered money would be made available for government efficiency initiatives that would be reported. We would advocate they would be reported for Congressional oversight annually, but they would be earmarked for new programs either around process improvements, policy improvements, new technology, or whatever could be applied directly to reducing improper payments.

We also recommend removal of the restrictions of the Paperwork Reduction Act. Some of those impede the issuance of appropriate documentation requests or payment demand letters. I think this is an area where one well-intended legislative action could be impeding another.

Last but not least, we recommend examination of the Single Audit Act to facilitate recovery audits for programs such as grants to States by Federal agencies that currently are prohibited from a secondary audit under that Act. The provisions of the Act should be reviewed to see if programs where there is evidence of intolerable levels of erroneous payments should be subjected to a secondary audit.

Thank you, Mr. Chairman. I am prepared to answer any questions you might have.

Senator CARPER. Thank you for your excellent testimony.

Let me return to a theme that was sounded a number of times in the course of this hearing, and that is incentives, and particularly with respect to Medicaid borne partly by the Federal taxpayers, borne partly by State taxpayers as we attempt to provide health care to low-income folks, in some cases nursing home assistance for our elderly. The comment I think you made was that as we look at efforts to recover improper payments or monies allocated inappropriately, States tend to bear the costs and the Federal Government tend to keep the dough. Is that a fair characterization of what you said? If it is, there is no wonder not a whole lot is being recovered and I certainly think I see a road map there for changing that.

Mr. WHITE. Not trying to put too fine a point on it, what I said was that although the characterization was made that if there were overpayments, frequently, they were split 50–50. It is not quite always that simple, and in some instances, it is split 50–50. In some instances, it may be that the State recoups the entire amount, and

in other instances, it may be that the Federal Government recoups the entire amount. So what we were advocating was setting up a system where if a State has a good productive recovery audit program, perhaps through some sort of a rate adjustment or something, they would get a better recoupment or keep a better portion of the split for those funds that are recovered.

Senator CARPER. OK. Good. We might want to explore that with you a little bit more.

Mr. WHITE. Sure.

Senator CARPER. Thank you. You have given us a pretty good to-do list for those of us here in Washington, in the Executive and Legislative Branchs, of things that we need to do differently. I am going to ask you to go back and just reiterate those again, if you would, please.

Mr. WHITE. Sure. I really made a series of six recommendations. The first one had to do with the reporting in the IPIA itself, and what we were encouraging Congress to evaluate is whether you could augment that reporting by not only reporting the statistics of what had been identified and what steps have been taken to pursue it, but whether there was a recovery audit program at all. Whether there were impediments that had been identified, and then what steps have been taken to ameliorate them. One of the issues that we have seen is where overpayments are identified, but for one reason or another, they are not pursued and we would request and think it would be wise to get an explanation for why they were not pursued.

The second recommendation was the joint task force with OMB, or OMB leading the task force between the agencies and the industry. The third was basically a standard contracting vehicle to make it easier for agencies to employ recovery audit firms as well as standard protocols and a government-wide disbursement audit.

We talked about the CMS Medicaid extension of their current efforts, and then we talked about incentives quite a bit with the Government Efficiency Fund, the reduction of the Paperwork Reduction Act, and then last but not least, the Single Audit Act and its sometimes effect on not being able to audit grants.

Senator CARPER. Dwell on that one for a little bit. If you had been here at our last hearing, I turned out to be, I think, the author in the House of Representatives when I was a Congressman for the Single Audit Act, encouraged by State auditors like former State Auditor McCaskill. What kind of changes do you think we ought to make in the Single Audit Act?

Mr. WHITE. I think the one that we are recommending is to review particular grant types for high degrees of erroneous payments, and if those thresholds are exceeded, then waive the Single Audit Act and allow a secondary audit.

Senator CARPER. OK. A couple more questions, if I could. You mentioned at a couple of points in your written testimony that you believe that private sector auditing firms can do a better job and be more efficient in recovery auditing than agencies' internal auditors can be.

Mr. WHITE. Yes.

Senator CARPER. I just want to know why you think that is the case.

Mr. WHITE. For a number of different reasons. First, it is all we do. Second, we are used to dealing with the size of the spend categories and the data. Third, we are independent and sometimes just a fresh point of view where you don't have as much ingrained history can be refreshing. This is a standard practice also in the commercial world. I think it has become accepted because of the reasons that I just expressed.

Senator CARPER. OK. Thank you. Senator McCaskill raised the question when we were talking with our earlier question from CMS and we were talking about the pilot work that is being done in three States with respect to recovery of Medicare improper payments. I think you indicated that your firm is involved in one of them. Which State are you all involved in?

Mr. WHITE. We are involved in California.

Senator CARPER. OK. Senator McCaskill asked, well, we are getting such good results in these three States, why don't we just do the other 47? I remember the old, what was it, Nike ad——

Mr. WHITE. Just do it.

Senator CARPER [continuing]. Let us just do it. Why don't we just do it?

Mr. WHITE. I agree with you. I think we should move as rapidly as possible. One of the points that Senator McCaskill made was that basically we bear all the cost and risk, and that is partially true. We do bear the majority of the cost and risk, but these programs are not cost-less nor risk-less for the States and/or for CMS, HHS, or any of the other agencies. They do have to invest resources to put the programs in place. They need to be supported. They have to provide data. They have to help us setting up regulations and protocols. They have to deal with the provider education and all the things that they described. It does take a little bit of time.

Senator CARPER. I can see that.

Mr. WHITE. I do think that CMS, by their approach to the legislation that was passed in December, is moving very aggressively. They do have the RFI already out. It is due April 9. The bid process would ensue apparently shortly thereafter. So I think they are moving very expeditiously and I think their intent is to be in all 50 States ahead of the deadline.

Senator CARPER. OK. Another question, I understand that some agencies that have employed maybe you or a competing firm and sometimes wall off entire portions of their budgets to keep the auditors away and maybe even decline to recover some overpayments that you have uncovered. Let me just ask, how often does that kind of thing happen? Why does it happen, and how can we push agencies to be more open and more aggressive in collecting what is owed to them?

Mr. WHITE. Well, I think we have talked about the incentive side of it enough, so I probably should put that aside.

Senator CARPER. OK.

Mr. WHITE. Why they do it, I think that they perceive there are some areas and programs that are particularly sensitive, and therefore either for security reasons, privacy reasons, or other reasons, they have to be very judicious in who they allow to look at it, and I think is a viable and valid concern.

I think they also, with the OMB interpretation of the legislation that exists, set thresholds, and then whether it is $10 million and 2.5 percent, whether that is exactly the right threshold, I am not really here to comment on it one way or the other, but thresholds do make some sense because if the agency is incurring some effort and if we are incurring some effort, you have to have a reasonable amount of spend in order to make it worthwhile. You can't go look at every dollar cost effectively.

So I can understand why some of those things exist and they are very practical. On the other hand, I think that, frequently, people perceive either people from the outside as being a threat or they perceive any examination of erroneous or improper payments as being critical of their previous efforts and they are naturally protective of their previous efforts and therefore, they may take that to a bit of an extreme.

Senator CARPER. OK. Well, there is an old saying about saving the best for last. I don't know that this testimony and these responses are the best, but they are really good and very helpful. I want to say for myself, for our staff, for the Members that were here and those that had to leave, thank you for sticking around and for your patience today and——

Mr. WHITE. Thank you for all the work that you are doing.

Senator CARPER. Oh, no, we get paid for this, and as it turns out, I guess you do, too. [Laughter.]

But you gave us some really good insights, and as I said, a very helpful to-do list, as well. We thank you for coming and for being with us this morning and this afternoon. There is still plenty of work to do for all of us, but I think we are maybe better informed now as we approach those responsibilities.

The hearing record is going to be open for 2 weeks for the submission of additional statements and questions. I would ask you and our other witnesses who have been kind enough to join us today for your cooperation in getting some prompt responses to any questions that we may submit for the record.

Again, thank you very much for your input and for your patience, and for that of the witnesses that preceded you.

With that, the hearing is adjourned. Thanks very much.

[Whereupon, at 1:13 p.m., the Subcommittee was adjourned.]

APPENDIX

Testimony of the Honorable Linda M. Combs
Controller, Office of Federal Financial Management
Office of Management and Budget

before the

Subcommittee on Federal Financial Management, Government Information, Federal Services, and International Security
of the Senate Committee on Homeland Security and Government Affairs

March 29, 2007

I am very pleased to be able to speak with you and the Subcommittee today on the progress being made in implementing the Improper Payments Information Act of 2002 (IPIA) and the Recovery Auditing Act. Much of the information I will discuss today can also be found in the recently published OMB report, *Improving the Accuracy and Integrity of Federal Payments* (January 31, 2007).

Today, I will discuss our accomplishments in implementing the IPIA, the government progress in recovery auditing, and how Congress can assist in achieving our shared objective of eliminating improper payments.

The Federal Government is achieving measurable results in meeting the President's goal to eliminate improper payments and fulfilling the requirements of IPIA. The IPIA has provided an effective framework for the Administration's efforts in this important area. Additionally, the Recovery Auditing Act, which addresses contract payments for agencies that award $500 million or more in contracts each year, has also been instrumental in recapturing improper contract payments. Since the first reporting under IPIA in FY 2004, our efforts to eliminate improper payments have been centered on the three primary requirements of the IPIA:

1. Identifying risk-susceptible programs;
2. Estimating the annual amount of improper payments in risk-susceptible programs; and
3. Identifying the root causes of improper payments and correcting the errors.

Identifying Risk-Susceptible Programs

In FY 2006, agencies strengthened their methods for risk assessing their programs and activities for improper payments. As a result of these improvements, the amount of Federal outlays determined to be susceptible to improper payments increased from $1.4 trillion (or 62% of $2.4 trillion total Federal outlays in FY 2004) to $1.7 trillion (or 66% of $2.7 trillion total Federal outlays in FY 2006). This year's risk total includes $184 billion in Federal program outlays not previously reported as risk susceptible in prior annual OMB reports.[1] This increase

[1] An increase in high-risk outlays does not mean that improper payments have increased or will increase in the future.

reflects the continued commitment of Federal agencies to ensure that all *potential* sources of error are reported.

Of note, the U.S. Department of Agriculture (USDA) re-assessed its programs and reclassified several within the Farm Service Agency as high-risk. As a result, a large number of previously undetected problems in a known high risk program were identified and reported. The Department has quickly implemented corrective actions to mitigate the documentation inadequacies discovered. This underscores the importance of having agencies continuously evaluate the strength of their risk assessment and measurement practices.

One agency of special focus in FY 2007 will be the Department of Homeland Security (DHS). DHS made progress in their FY 2006 reporting, by including an improper payment measurement for the Federal Emergency Management Agency's Individual and Household Program. This year, DHS is working to strengthen its risk assessments so that there is more transparency into potential improper payments within the Department.

Estimating the Annual Amount of Improper Payments in Risk-Susceptible Programs

Efforts are continuing to move the Executive Branch to full reporting under IPIA by FY 2008. The amount of Federal program outlays that are being measured for improper payments has increased from $1.1 trillion to $1.4 trillion. Therefore, 81% of all risk susceptible outlays are being measured for improper payments ($1.4 trillion of the $1.7 trillion high-risk dollars). When FY 2008 results are reported, almost 100% of risk susceptible dollars will report an error measurement (with the inclusion of over $325 billion in high-risk outlays not currently reporting an error measurement).[2]

	FY 2004		FY 2005		FY 2006	
	Improper Payments	Error Rate	Improper Payments	Error Rate	Improper Payments	Error Rate
FY 2004	$ 45,043	3.9%	$ 37,170	3.4%	$ 36,300	3.2%
FY 2005			$ 1,314	1.1%	$ 2,920	2.0%
FY 2006					$ 1,295	1.1%
Total	$ 45,043	3.9%	$ 38,484	3.2%	$ 40,515	2.9%

The increase in statistically valid national error measurements would not have been possible without the cooperation of representatives from the Federal and State governments, and among the programmatic, financial management, and Inspectors General communities. Such cooperation is critical, especially for the large and complex programs that are at risk for improper payments.

[2] Medicaid will begin reporting a component, or partial, error measurement in FY 2007. By FY 2008, the Temporary Assistance for Needy Families program, the Child Care and Development Fund, and the State Children's Health Insurance Program will also report a national error measurement.

Identifying the Root Causes of Improper Payments and Correcting the Errors

The amount of improper payments in the programs originally reported in FY 2004 were reduced from a baseline of approximately $45.1 billion to $36.3 billion this year, a nearly $9 billion or 20% reduction. These original programs continue to represent a significant majority of FY 2006 improper payments.

The overall Federal FY 2006 improper payment rate was 2.9% and total improper payments equaled $40.5 billion. These numbers represent a reduction in the total rate and amount of improper payments reported since FY 2004 (from 3.9% and $45.1 billion respectively). The decrease in the FY 2006 improper payment rate was driven largely by two factors: (1) a reduction in Medicare improper payments by $1.3 billion since FY 2005[3] and (2) low improper payment rates for programs that reported error measurements for the first time in either FY 2005 or FY 2006. Other significant achievements include:

- USDA reported that the Food Stamps program lowered its error rate (5.84%) for the seventh consecutive year.
- The Department of Housing and Urban Development's Public Housing and Rental Assistance programs have reduced improper payments by nearly $2 billion since FY 2001, a reduction of more than 60%.
- The Social Security Administration's Old Age, Survivors, and Disability Insurance program (OASDI) error rate dropped 1/10 of 1 percent or $401 million.

Departments and agencies have now completed their third year (in several cases their fourth year) of reporting under the Recovery Auditing Act (section 831 of the Defense Authorization Act for Fiscal Year 2002 (Pub. L. No. 107-107)). In FY 2006, 20 agencies reported on their recovery audit efforts in their Performance and Accountability Reports (PARs), an increase of 14 agencies since 2004. Of note, the Department of Defense (DOD) reviewed nearly $300 billion in commercial payments during FY 2006. Approximately $170 million in payment errors were identified in FY 2006. For this same reporting period, approximately $133 million were recovered.

We realize that additional work is required to ensure that the full universe of improper vendor payments is identified. OMB is already working with agencies to look more closely at this area of improper payments.

Outlook for FY 2007 and Beyond

Let me take this opportunity to express my sincere appreciation to the Senate for providing over a billion dollars in adjustments to the discretionary caps for program integrity and tax compliance efforts in the Senate Budget Resolution as reported out of the Budget Committee. We would, of course, encourage the House to include these cap adjustments in their Budget Resolution as well, and welcome your leadership in helping make this happen. As you are aware,

[3] Medicare substantially improved its claims documentation, and reduced its error rate reporting in the Fee for Service portion of the program from 10.1% in FY 2004 to 5.2% in FY 2005. The rate decreased even further in FY 2006 to 4.4%.

these proposals provide greatly needed resources for administrative program integrity and tax compliance efforts in Medicare, Medicaid, Earned Income Tax Credit (EITC) and other Internal Revenue Service (IRS) enforcement activities, Unemployment Insurance (UI), Supplemental Security Income (SSI), and Old Age, Survivors, and Disability Insurance (OASDI).

Additionally, we also appreciate the Senate's interest in including language to newly authorized bills that stresses the importance of program integrity. We also invite your leadership in assisting in the enactment of the other program-specific reforms included in the President's FY 2008 Budget. The President's FY 2008 Budget contains a series of reforms that are needed to ensure greater program integrity and payment accuracy. These proposals include:

- **UI Overpayment Recoveries** – provides tools and resources as financial incentives to States to more aggressively pursue benefit overpayments. If enacted, the proposal is projected to save $3.6 billion over ten years.

- **EITC and Child Tax Credit** – clarifies tax code definitions to reduce filing complexity. If enacted, the proposals would save $487 million in the first year and $6.7 billion over ten years.

- **OASDI** – provides SSA with the tools to conduct improved enforcement of certain statutory provisions and to eliminate the more complicated formulas currently used when calculating certain benefit offsets. If enacted, these two proposals would save $4 million in the first year and $3.6 billion over ten years.

This Administration will continue to hold agencies accountable under the President's Management Agenda Eliminating Improper Payments initiative, and further build upon recent results to address remaining challenges. We are optimistic that our current efforts, complemented by the enactment of the program integrity reforms proposed in OMB's annual IPIA report, and full funding of the President's request for program integrity efforts, will continue to pave a path forward in achieving our shared objective to eliminate improper payments.

United States Government Accountability Office

GAO

Testimony

Before the Subcommittee on Federal Financial Management, Government Information, Federal Services, and International Security, Committee on Homeland Security and Governmental Affairs, U.S. Senate

For Release on Delivery
Expected at 10:00 a.m. EDT
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IMPROPER PAYMENTS

Agencies' Efforts to Address Improper Payment and Recovery Auditing Requirements Continue

Statement of McCoy Williams, Director
Financial Management and Assurance

GAO-07-635T

GAO
Accountability·Integrity·Reliability
Highlights

Highlights of GAO-07-635T, a testimony before the Subcommittee on Federal Financial Management, Government Information, Federal Services, and International Security, Committee on Homeland Security and Governmental Affairs, U.S. Senate

Why GAO Did This Study

The federal government is accountable for how its agencies and grantees spend hundreds of billions of taxpayer dollars and is responsible for safeguarding those funds against improper payments as well as for recouping those funds when improper payments occur. The Congress enacted the Improper Payments Information Act of 2002 (IPIA) and the Recovery Auditing Act to address these issues. Fiscal year 2006 marked the 3rd year that agencies were required to report improper payment and recovery audit information in their Performance and Accountability Reports.

GAO was asked to testify on the progress agencies have made in these areas. Specifically, GAO focused on (1) trends in agencies' reporting under IPIA from fiscal years 2004 through 2006, (2) challenges in reporting improper payment information and improving internal control, and (3) agencies' reporting of recovery auditing efforts. This testimony is based on GAO's previous reports on agencies' efforts to implement IPIA requirements for fiscal years 2005 and 2004 and current review of available fiscal year 2006 improper payment and recovery auditing information. The Office of Management and Budget (OMB) provided technical comments that were incorporated as appropriate.

www.gao.gov/cgi-bin/getrpt?GAO-07-635T.

To view the full product, including the scope and methodology, click on the link above. For more information, contact McCoy Williams at (202) 512-9095 or williamsm1@gao.gov.

March 29, 2007

IMPROPER PAYMENTS

Agencies' Efforts to Address Improper Payment and Recovery Auditing Requirements Continue

What GAO Found

GAO identified several key trends related to IPIA reporting requirements.

- **Risk assessments**. For fiscal years 2004 through 2006, some agencies still had not instituted systematic methods of reviewing all programs and activities or had not identified all programs susceptible to significant improper payments. Further, certain agencies' risk assessments appeared questionable. GAO also noted that OMB's recently revised IPIA implementing guidance, which allows certain agencies to perform risk assessments every 3 years instead of annually, may result in fewer agencies conducting risk assessments in the future.
- **Improper payment estimates.** Since fiscal year 2004, agencies have made some progress in reporting improper payment information. The number of programs reporting improper payment estimates for fiscal year 2004 totaled 41, compared to 60 programs for fiscal year 2006. The total improper payments dollar estimate was $45 billion in fiscal year 2004, $38 billion in fiscal year 2005, and about $42 billion in fiscal year 2006.
- **Noncompliance issues.** Although not currently required by IPIA to do so, some agency auditors continued to report problems related to agencies' risk assessments, definition of programs for IPIA purposes, sampling methodologies, lack of reporting for all risk-susceptible programs, and supporting documentation.

Although showing progress under OMB's continuing leadership, agencies' fiscal year 2006 reporting under IPIA does not yet reflect the full scope of improper payments. Major challenges remain in meeting the goals of the act and ultimately improving the integrity of payments. First, some agencies have not yet reported for all risk-susceptible programs. For example, the fiscal year 2006 total improper payment estimate of about $42 billion did not include any amounts for 13 risk-susceptible programs that had fiscal year 2006 outlays totaling about $329 billion. Second, certain methodologies used to estimate improper payments did not result in accurate estimates. Finally, GAO noted that internal control weaknesses continued to plague programs susceptible to significant improper payments.

From fiscal years 2004 through 2006, the number of agencies reporting recovery auditing information for contract overpayments and the dollar amounts identified for recovery and actually recovered increased. For fiscal year 2004, 12 agencies reported recovering about $53 million, compared to 18 agencies that reported recovering about $256 million for fiscal year 2006. Given the large volume and complexity of federal contract payments and historically low recovery rates for certain programs, GAO emphasized that it is much more efficient to pay bills properly in the first place. Effective internal control calls for a sound, ongoing invoice review and approval process as the first line of defense in preventing erroneous payments.

Mr. Chairman and Members of the Subcommittee:

I am pleased to be here today to discuss the governmentwide problem of improper payments in federal programs and activities and agencies' efforts to address key requirements of the Improper Payments Information Act of 2002 (IPIA)[1] and Section 831 of the National Defense Authorization Act for Fiscal Year 2002, commonly known as the Recovery Auditing Act.[2] Since fiscal year 2000, we have issued a number of reports and testimonies aimed at raising the level of attention given to improper payments. Our work over the past several years has demonstrated that improper payments are a long-standing, widespread, and significant problem in the federal government. IPIA has increased visibility over improper payments[3] by requiring executive agency heads, based on guidance from the Office of Management and Budget (OMB),[4] to identify programs and activities susceptible to significant improper payments,[5] estimate amounts improperly paid, and report on the amounts of improper payments and their actions to reduce them. Similarly, the Recovery Auditing Act provides an impetus for applicable agencies to systematically identify and recover contract overpayments. This act requires, among others things, that all executive branch agencies entering into contracts with a total value exceeding $500 million in a fiscal year to have cost-effective programs for identifying errors in paying contractors and for recovering amounts erroneously paid. As the steward of taxpayer dollars, the federal government is accountable for how its agencies and grantees spend hundreds of billions of taxpayer dollars and is responsible for safeguarding those funds against improper payments as well as having

[1]Pub. L. No. 107-300, 116 Stat. 2350 (Nov. 26, 2002).

[2]Section 831 of the National Defense Authorization Act for Fiscal Year 2002, Pub. L. No. 107-107, div. A, title VIII, § 831, 115 Stat. 1012, 1186 (Dec. 28, 2001) (codified at 31 U.S.C. §§ 3561-3567).

[3]IPIA defines improper payments as any payment that should not have been made or that was made in an incorrect amount (including overpayments and underpayments) under statutory, contractual, administrative, or other legally applicable requirements. It includes any payment to an ineligible recipient, any payment for an ineligible service, any duplicate payment, payments for services not received, and any payment that does not account for credit for applicable discounts.

[4]OMB Memorandum M-06-23, "Issuance of Appendix C to OMB Circular No. A-123" (Aug. 10, 2006).

[5]OMB's guidance defines significant improper payments as those in any particular program that exceed both 2.5 percent of program payments and $10 million annually.

mechanisms in place to recoup those funds when improper payments occur.

OMB has played a key role in the oversight of the governmentwide improper payments problem. In 2005, OMB established Eliminating Improper Payments as a new program-specific initiative under the President's Management Agenda (PMA). This separate PMA program initiative helps to ensure that agency managers are held accountable for meeting the goals of IPIA and are, therefore, dedicating the necessary attention and resources to meeting IPIA requirements. OMB continues its commitment to identify all improper payments governmentwide by working with agencies to establish corrective action plans to address their root causes. OMB also annually reports[6] on agencies' efforts to address IPIA and Recovery Auditing Act requirements.

Today, my testimony will focus on three key areas:

- trends in agencies' reporting under IPIA for fiscal years 2004 through 2006,
- challenges in reporting improper payment information and improving internal control, and
- agencies' reporting of recovery auditing efforts to recoup improper payments.

This testimony is based on our previous reports on agencies' efforts to implement IPIA requirements for fiscal years 2005 and 2004[7] and our current review of available fiscal year 2006 improper payment information reported by 36 of the 38 federal agencies that the Department of the Treasury (Treasury) determined to be significant to the U.S. government's consolidated financial statements. (See app. I for a list of the 38 agencies.) The remaining 2 federal government corporations have a different year-end reporting date and had not issued their annual reports as of the end of our fieldwork. We reviewed improper payment information reported in the 36 agencies' fiscal year 2006 performance and accountability reports (PAR) or annual reports. We also reviewed OMB guidance on

[6]Office of Management and Budget, *Improving the Accuracy and Integrity of Federal Payments*, (Washington, D.C.: Jan. 31, 2007).

[7]GAO, *Improper Payments: Agencies' Fiscal Year 2005 Reporting under the Improper Payments Information Act Remains Incomplete*, GAO-07-92 (Washington, D.C.: Nov. 14, 2006) and *Financial Management: Challenges in Meeting Requirements of the Improper Payments Information Act*, GAO-05-417 (Washington, D.C.: Mar. 31, 2005).

implementation of IPIA and the Recovery Auditing Act and its annual report on agencies' efforts to identify and reduce improper payments. In addition, we reviewed GAO reports and agency Office of Inspector General (OIG) management challenges reports to identify internal control weaknesses and program integrity issues for agency programs reporting improper payment estimates for fiscal year 2006. We did not independently validate the data that agencies reported in their PARs or annual reports or the data that OMB reported. However, we are providing agency-reported data as descriptive information that will inform interested parties about the magnitude of reported governmentwide improper payments and amounts recouped through recovery audits and other improper payment-related information. We believe the data to be sufficiently reliable for this purpose. We provided information on the major findings discussed in this statement to OMB. OMB provided technical comments that we have incorporated as appropriate. We conducted our work in March 2007 in accordance with generally accepted government auditing standards. Details on our scope and methodology related to fiscal year 2005 and 2004 findings can be found in our prior reports.[8]

Significant Trends in IPIA Reporting

I would now like to focus on agencies' efforts to address select IPIA reporting requirements during the first 3 years of IPIA implementation, fiscal years 2004 through 2006. Generally, agencies must perform four key steps to address the improper payments reporting requirements—(1) perform a risk assessment, (2) estimate improper payments for risk-susceptible programs and activities, (3) implement a plan to reduce improper payments for programs with estimates exceeding $10 million, and (4) annually report improper payment estimates and actions to reduce them. OMB requires the results of these steps to be reported in the agencies' PARs, in the Management Discussion and Analysis section and as a separate appendix, for each fiscal year ending on or after September 30, 2004. Today, I will touch on progress made and challenges that remain in these areas.

Risk Assessments

Our past and current reviews of agencies' reported risk assessments have raised questions regarding their adequacy. For fiscal years 2004 through 2006, we found that some agencies still had not instituted systematic methods of reviewing all programs and activities or had not identified all

[8]GAO-07-92 and GAO-05-417.

programs susceptible to significant improper payments. We also reported that certain agencies' risk assessments appear questionable. Conducting a risk assessment is an essential part of agencies' efforts to comply with IPIA. Risk assessment is a key step in helping to gain a reasonable level of assurance that programs are operating as intended and that they are achieving their expected outcomes. Done properly, it entails a comprehensive review and analysis of program operations to determine if risks exist, what those risks are, and the potential or actual effect of those risks on program operations. The information developed during a risk assessment forms the foundation or basis upon which management can determine the nature and type of corrective actions needed. It also gives management baseline information for measuring progress in reducing improper payments.

- For the first year of reporting under IPIA, we reported in March 2005,[9] that of the 29 agencies reviewed, 23 had completed risk assessments for all programs and activities for fiscal year 2004. However, for 3 of these, agencies' auditors raised noncompliance issues with the risk assessments. For example, agency auditors for the Department of Justice (DOJ) and the National Aeronautics and Space Administration (NASA) reported that the risk assessments did not consider all payment types or programs. The auditor for the Department of Homeland Security (DHS) reported that the agency did not institute a systematic method of reviewing all programs and identifying those it believed were susceptible to significant erroneous payments.

- Regarding the second year of IPIA reporting, we reported in November 2006,[10] that the same number of agencies, 23, had performed risk assessments of all of their programs and activities based on our review of 35 agency PARs or annual reports for fiscal year 2005. Similar to the first year of IPIA reporting, we noted that auditors for DOJ and DHS again raised noncompliance issues regarding the adequacy of the agencies' risk assessments. We noted other risk assessment deficiencies as well. For example, the Department of Agriculture (USDA) OIG reported[11] that the agency's risk assessments were not adequate to estimate the agency's susceptibility to improper payments

[9]GAO-05-417.

[10]GAO-07-92.

[11]Department of Agriculture, Office of Inspector General, Memorandum for the Secretary, "Management Challenges," September 2, 2005.

because the guidance from the USDA's Office of the Chief Financial Officer (OCFO) was not sufficiently prescriptive and detailed to translate into meaningful results. As such, the OIG recommended that the USDA OCFO strengthen guidance over its IPIA risk assessments to provide reasonable assurance that the requirements of the act are met. Further, the OIG stated that USDA should identify risk factors that are discrete to the program being assessed and consider information from all sources, such as audit reports.

- For fiscal year 2006, the third year of IPIA reporting, we found that 30 of the 36 agencies had reported performing some type of assessment to identify programs and activities susceptible to significant improper payments. The remaining 6 agencies either did not report improper payments information in their PARs or annual reports, or did not report assessing for risk of improper payments for all of their programs and activities. Of the 30, 18 agencies reported reviewing all programs and activities as part of the risk assessment process, while the remaining 12 agencies provided enough details that indicated some level of review was performed. For example, 1 agency reported that it had evaluated its major programs based on its developed risk criteria. Although the major programs made up a significant portion of the agency's outlays, the agency did not report that it had assessed the remaining programs and activities. We also found instances where an agency's description of the risk assessment performed contradicted its assertion that all programs and activities had been reviewed. For example, 1 agency reported in its PAR that it had assessed all programs and activities, but also reported in the same PAR that assessments for two activities had not been conducted. Another agency reported that it had assessed all of its payment programs, but later stated in its PAR that its risk assessment only covered certain types of programs.

Similar to the previous years, agency auditors continued to find inadequacies in agencies' risk assessments for fiscal year 2006. The DHS auditor reported that the agency did not perform a risk assessment for all programs and activities. Further, the NASA auditor reported that the agency had potentially violated certain requirements of IPIA as NASA had been unable to provide the auditor with sufficient documentation to support performance of an annual review of all programs and activities that the agency administers.

Other agencies reported improving and refining their risk assessment methodologies for fiscal year 2006. For example, USDA's Farm Service Agency reported that it made improvements to its risk assessments and as a result, four additional programs were determined to be susceptible to

significant improper payments. Two other agencies reported redefining their programs to conduct their risk assessments. DOJ reported that it addressed its noncompliance with IPIA by performing risk assessments in its U.S. Marshals Service component. Other agencies identified plans for improving future risk assessments. For example, the Office of Personnel Management (OPM) reported that it will assess in fiscal year 2007 whether any agency payment streams, other than its former OMB Circular No. A-11 programs,[12] are susceptible to significant improper payments. The Department of Defense reported that it is developing a program to review its intergovernmental payments and payments for afloat and deployed forces. NASA reported that it plans to perform a risk assessment of the agency's commercial and noncommercial disbursement activities.

Finally, we noted that the number of agencies conducting risk assessments may decrease in future reporting, because OMB's revised IPIA implementing guidance allows agencies to perform risk assessments every 3 years for those agency programs not deemed susceptible to significant improper payments. Prior to issuing its revised implementing guidance, OMB discussed the proposed changes with us. We advised OMB that the provision to perform risk assessments every 3 years for those programs not deemed risk-susceptible was inconsistent with the IPIA requirement for agencies to review all programs and activities annually. In its fiscal year 2006 PAR, the General Services Administration (GSA) reported that because it does not have any programs or activities susceptible to significant improper payments, GSA will perform the next risk assessment in fiscal year 2008. Additionally, several programs included in OMB's former Circular No. A-11, reported that OMB had granted them a waiver from improper payments reporting because they did not have programs susceptible to significant improper payments. These programs included the Environmental Protection Agency's Clean and Drinking Water State Revolving Funds, the National Science Foundation's Research and Education Grants and Cooperative Agreements, and the Department of Veterans Affairs (VA) Insurance programs. OMB's previous implementing guidance required agencies to annually estimate improper payments for

[12]Prior to the governmentwide IPIA reporting requirements beginning with fiscal year 2004, former section 57 of OMB Circular No. A-11 required certain agencies to submit similar information, including estimated improper payment target rates, target rates for future reductions in these payments, the types and causes of these payments, and variances from targets and goals established. In addition, these agencies were to provide a description and assessment of the current methods for measuring the rate of improper payments and the quality of data resulting from these methods.

their programs that were included in former Circular No. A-11, regardless of amount.

Improper Payment Dollar and Error Rate Estimates

Since fiscal year 2004, agencies have made progress in reporting improper payment information. For example, the number of programs reporting improper payment estimates for fiscal year 2004 totaled 41, as compared to 60 programs reporting for fiscal year 2006, a net increase of 19 programs.[13] The total improper payments dollar estimate was $45 billion in fiscal year 2004, $38 billion in fiscal year 2005, and about $42 billion[14] in fiscal year 2006. (See app. II for further details.)

We have previously testified[15] before this subcommittee regarding the decrease in the total improper payment estimate from $45 billion in fiscal year 2004 to $38 billion in fiscal year 2005. Specifically, we reported that the $7 billion decrease was primarily attributable to a decrease in the Medicare estimate that resulted from increased efforts to educate health care providers on the importance of responding to requests for medical records to perform detailed statistical reviews. Also, the Department of Health and Human Services (HHS) extended the time that providers have for responding to documentation requests from 55 days to 90 days. We further reported that these changes primarily affected HHS's processes related to its efforts to perform detailed statistical reviews for the purposes of calculating an annual improper payment estimate for the Medicare program. While this represents a refinement, it may not reflect improved accountability over program dollars given that GAO continues to designate the Medicare program as a high-risk area. Specifically, in our January 2007 report,[16] we reported that further action must be taken to refine Medicare's payment methods and collection of data used as a basis

[13]The net increase represents newly reported programs for applicable years as well as programs that may have reported in one year but not in a subsequent fiscal year.

[14]For fiscal year 2006, OMB reported total improper payments of about $41 billion, a difference of $1 billion. The difference is primarily attributable to OMB excluding improper payment estimates for the Tennessee Valley Authority and agency-reported improper payment estimates related to commercial or vendor payments because, according to OMB, those estimates are reported in agencies' recovery auditing amounts. Rounding differences also exist.

[15]GAO, *Improper Payments: Incomplete Reporting under the Improper Payments Information Act Masks the Extent of the Problem*, GAO-07-254T (Washington, D.C.: Dec. 5, 2006).

[16]GAO, *High-Risk Series: An Update*, GAO-07-310 (Washington, D.C.: January 2007).

for setting payment rates and address program integrity weaknesses, among others. Also, HHS's OIG continued to report the integrity of Medicare payments as a top management challenge for fiscal year 2006.

For fiscal year 2006, the total improper payment estimate increased to about $42 billion from the reported $38 billion for fiscal year 2005. The increase in improper payments was primarily attributable to 15 newly reported programs or activities totaling about $2.4 billion, and a $1.6 billion increase in USDA's Marketing Assistance Loan program due to improvements in how it measured its improper payments. In addition, several programs experienced increases in their improper payment estimates as a result of lax upfront eligibility controls to facilitate rapid benefit delivery to victims devastated by Hurricane Katrina. According to OMB, the programs most directly affected included the Federal Emergency Management Agency's Individuals and Households program (IHP), Department of Labor's (Labor) Disaster Unemployment Insurance (UI) program, and the Small Business Administration's Disaster Assistance Loan program. For example, Labor identified more than $100 million in improper payments related to Hurricane Katrina for the Disaster UI program. To respond to the challenges of the Gulf Coast hurricanes, on August 29, 2006, the President signed Executive Order 13411, Improving Assistance for Disaster Victims, which established a task force on disaster coordination responsible for recommending specific actions to improve the delivery of federal disaster assistance while strengthening controls designed to prevent improper payments and other forms of fraud, waste, and abuse.

Mr. Chairman, I commend agencies' efforts to decrease improper payment error rates. For example, from our review of agency programs initially reporting error rates in the first year of IPIA implementation, fiscal year 2004, we noted that of the 32 agency programs with changes in their error rates, 18 program error rates, or 56 percent, had declined when compared to fiscal year 2006. However, it should be noted that in this still-early stage of IPIA implementation, a decrease in the reported error rate may not signal improved accountability just as an increase may not necessarily indicate a greater number of control weaknesses. In some cases, these fluctuations may be attributed to changes in the estimating methodology used. For example, USDA's Marketing Assistance Loan program did not report an estimate in fiscal year 2004 and reported a small estimate for fiscal year 2005. However, with improvements in how it measures improper payments, this program estimated an error rate of 20.3 percent for fiscal year 2006. The Marketing Assistance Loan program is now in a greatly improved position to identify the root causes of these errors and

ultimately improve the integrity of its payments—the primary goal of IPIA reporting.

Table 1 highlights improper payment error rates for the 8 major programs that accounted for 86 percent of the $42 billion total improper payment estimate for fiscal year 2006.

Table 1: Reported Improper Payment Error Rates for Major Programs for Fiscal Years 2004 through 2006

		FY 2004		FY 2005		FY 2006	
Agency	**Program**	**Error rate (percent)**	**Estimate (dollars in billions)**	**Error rate (percent)**	**Estimate (dollars in billions)**	**Error rate (percent)**	**Estimate (dollars in billions)**
Health and Human Services	Medicare (Fee-for-Service component)	10.1	$21.7	5.2	$12.1	4.4	$10.8
Department of the Treasury	Earned Income Tax Credit	24.5	9.7	25.5	10.5	25.5	10.7
Department of Labor	Unemployment Insurance	10.3	3.9	10.1	3.3	10.7	3.4
Social Security Administration	Old Age, Survivors, and Disability Insurance	0.3	1.7	0.7	3.7	0.6	3.3
Social Security Administration	Supplemental Security Income Program	7.3	2.6	7.7	2.9	7.8	3.0
Department of Agriculture	Food Stamp Program	6.6	1.6	5.9	1.4	5.8	1.6
Department of Agriculture	Marketing Assistance Loan Program	0.0	0.0	0.7	0.5	20.3	1.6
Housing and Urban Development	Public Housing/Rental Assistance	6.9	1.7	5.6	1.5	5.4	1.5
	Total		**$42.9**		**$35.9**		**$35.9**
	Estimate for all programs		45.4		38.4		41.6
	Major programs as a percent of total for all programs		94 percent		93 percent		86 percent

Sources: GAO analysis of agencies' fiscal years 2004 to 2006 PARs and OMB

Noncompliance Issues with IPIA Continue

Although they are not specifically required to do so by the act, some agency auditors have reported on noncompliance issues related to implementation of IPIA since the first year of IPIA reporting. For example, for fiscal years 2004 and 2005, we reported[17] that agency auditors had

[17]GAO-05-417 and GAO-07-92, respectively.

identified instances of noncompliance, such as the lack of a systematic method for reviewing all programs and risk assessments that did not consider all payment types or programs. For fiscal year 2006, agency auditors reported instances of noncompliance such as an agency still being in its early stages of IPIA implementation or not yet having reported for all risk-susceptible programs.

We found that the level of noncompliance and types of issues raised varied over the first 3 years of IPIA reporting. From our review of the agency auditors' description of the noncompliance, we classified the findings into three categories—full noncompliance, partial noncompliance, and potential noncompliance. We noted that agency auditors reported problems related to agencies' risk assessments, the definition of programs for IPIA purposes, sampling methodologies, lack of reporting for all risk-susceptible programs, and supporting documentation, as shown in table 2. Fully addressing these matters should lead to inuproved reporting under IPIA. Although IPIA does not include a separate reporting requirement for auditors to assess agencies' compliance, we noted that those that included this assessment provided a valuable independent validation of agencies' efforts to implement the act.

Table 2: Noncompliance Issues Reported by Some Agency Auditors for Fiscal Years 2004 through 2006

Category of noncompliance	Fiscal year 2004	Fiscal year 2005	Fiscal year 2006	Type of noncompliance issue
Full noncompliance	3	2	1	Defining programs and activities, risk assessment, sampling, early stages of IPIA implementation
Partial noncompliance	1	1	4	Not estimating for all risk-susceptible programs, risk assessment, sampling
Potential noncompliance	0	0	1	Documentation does not support work reportedly performed
Total	**4**	**3**	**6**	

Source: GAO analysis

From our analysis, we noted that four agencies[18] had reported noncompliance issues for at least 2 of the 3 IPIA reporting years. For example, agency auditors for DHS have reported noncompliance issues for

[18]The four agencies include HHS, DHS, DOJ, and NASA.

the first 3 years of IPIA reporting. As mentioned earlier in this testimony, the first 2 years of noncompliance were primarily caused by inadequate risk assessments. For fiscal year 2006, DHS auditors reported that the agency had not fully complied with IPIA due to several inadequacies related to sampling methodologies, trained staff, and monitoring of results to ensure testing was completed for all required programs. DHS auditors recommended that the agency follow OMB guidance for fiscal year 2007, including completing the necessary susceptibility assessments, testing for all material programs, and instituting sampling techniques to allow for statistical projection of improper payments testing results.

Challenges Continue in Reporting Improper Payment Information and Improving Internal Control

While showing progress, agencies' fiscal year 2006 reporting under IPIA does not yet reflect the full scope of improper payments across executive branch agencies. Major challenges remain in meeting the goals of the act and ultimately improving the integrity of payments. Specifically, some agencies have not yet reported for all risk-susceptible programs, and certain methodologies used to estimate improper payments do not result in reliable estimates. Also, we noted that management challenges related to agencies' internal control weaknesses continue to plague programs susceptible to significant improper payments.

Improper Payments Estimate Excludes Several Large Risk-Susceptible Programs

The fiscal year 2006 total improper payment estimate of about $42 billion did not include any amounts for 13 risk-susceptible programs having fiscal year 2006 outlays totaling about $329 billion. The Medicaid program represents the largest program that has not yet reported, with reported outlays of about $183 billion. OMB had specifically required 9 of these programs, including the Medicaid program to report selected improper payment information for several years before IPIA reporting requirements became effective. After passage of IPIA, OMB's implementing guidance required that these programs continue to report improper payment information under IPIA. See table 3 for more detailed information.

Table 3: Risk-Susceptible Programs That Did Not Report Improper Payment Estimates and Target Dates for Estimates

Agency/program	Fiscal year 2006 outlays (dollars in billions)	Target date for improper payment estimate	Previously required to estimate
Department of Agriculture—National School Lunch and School Breakfast Programs (previously School Programs)	$6.5	2007	X
Federal Communications Commission—High Cost Support Program	3.8	2007	
Federal Communications Commission—Universal Service Fund's Schools and Libraries	1.7	2007	
Small Business Administration—504 Certified Development Companies	4.3	2007	X
Department of Transportation—Airport Improvement Program	3.8	2007	X
Department of Transportation—Capital Investments	3.1	2007	X
Department of Transportation—Formula Grants	1.9	2007	X
Department of Health and Human Services—Child Care and Development Fund	4.9	2008[a]	X
Department of Health and Human Services—Medicaid	182.9	2008	X
Department of Health and Human Services—State Children's Insurance Program	5.8	2008	X
Department of Health and Human Services—Temporary Assistance for Needy Families	17.4	2008[a]	X
Department of Health and Human Services—Medicare Advantage	55.4	Did not report a target date	
Department of Health and Human Services—Medicare Prescription Drug Benefit	37.4	Did not report a target date	
Total	**$328.9**		**9**

Sources: OMB and cited agencies' fiscal year 2006 PARs.

[a]Although not reported in HHS's fiscal year 2006 PAR, according to OMB, both the Child Care and Development Fund and Temporary Assistance for Needy Families programs anticipate reporting a component error measurement in HHS's fiscal year 2008 PAR

Of these 13 programs, 11 reported that they would be able to estimate and report on improper payments in the next 2 fiscal years, but could not do so for fiscal year 2006. The remaining 2 programs were silent about when they would report estimates in the future. As a result, improper payment reporting of these programs susceptible to risk remain unknown.
OMB reported that some of the agencies were unable to determine the rate or amount of improper payments because of measurement challenges or time and resource constraints, which OMB expects to be resolved in future reporting years. For example, since fiscal year 2002, HHS has conducted pilots at the state level to further its progress toward reporting a national improper payments estimate for its Medicaid program. Each state is responsible for designing and overseeing its own Medicaid program within the federal government structure. This type of program structure presents challenges for implementing a methodology to estimate improper payments as HHS must work with states to obtain applicable documentation used in the calculation. An additional challenge that HHS and other agencies with state-administered programs say they face is the ability to hold states accountable for meeting targets to reduce and recover improper payments in the absence of specific statutory authority. In April 2006, we reported[19] on the need for federal and state coordination to report national improper payment estimates on federal programs as state-administered programs and other nonfederal entities receive over $400 billion annually in federal funds. Thus, federal agencies and states share a responsibility for the prudent use of these funds.

Certain Methodologies Used to Estimate Improper Payments Do Not Result in Accurate Estimates

We have previously noted that agencies employed different sampling methodologies to estimate improper payments, including statistical sampling, nonstatistical sampling, or a combination of the two. OMB's implementing guidance requires that agencies generally use a statistical sample to estimate improper payments. Agencies may also use an alternative sampling approach provided they obtain OMB approval prior to implementation. The advantage of using statistical sampling is that sample results can be generalized to the entire population from which the sample was taken. Based on our review of fiscal year 2006 reporting, we found seven agencies that did not use statistical sampling to estimate improper payments for nine programs totaling about $202 million, with program

[19]GAO, *Improper Payments: Federal and State Coordination Needed to Report National Improper Payment Estimates on Federal Programs*, GAO-06-347 (Washington, D.C. Apr. 14, 2006).

outlays exceeding $88 billion. Given that total outlays for these nine risk-susceptible programs exceeded $88 billion for fiscal year 2006, the improper payment estimate for these programs would likely have been much greater had statistically valid methods been used.

For example, Labor analyzed fiscal year 2004 audits done under the Single Audit Act,[20] as amended, to identify questioned costs for its Workforce Investment Act[21] program, which, in turn, were used as a proxy for reporting its improper payment estimate. Specifically, the improper payment rate was determined by calculating the projected questioned costs and dividing this total amount by the corresponding outlays. Using this methodology, Labor reported a $6.4 million improper payment estimate for fiscal year 2006. We do not believe this is a reasonable proxy for improper payment levels because single audits, by themselves, may lack the level of detail necessary for achieving IPIA compliance. Specifically, single audits generally focus on the largest dollars in an auditee's portfolio. Thus, all programs identified as susceptible to improper payments at the federal level may not receive extensive coverage under a single audit. Consequently, both the depth and level of detail of single audit results are, generally, insufficient to identify improper payments, estimate improper payments, or both. We noted that Labor's OIG reported the use of single audits as a major management challenge because serious deficiencies in single audits, including inadequate sampling methodologies have been reported, thus making them unreliable for purposes of estimating improper payments.

We also found that five agencies used a combination of statistical and nonstatistical sampling methods to estimate improper payments totaling about $11.6 billion for ten programs. For example, VA reported that improper payment estimates for its Compensation and Pension programs are based on statistical sampling of its quality assurance program together with actual amounts of debt incurred that are referred to the VA Debt Management Center. In another example, the Railroad Retirement Board (RRB) reported that improper payment estimates for its Retirement and

[20]31 U.S.C. §§ 7501-7507. Under the Single Audit Act, as amended, and implementing guidance, independent auditors audit state and local governments and nonprofit organizations that expend $500,000 or more in federal awards to assess, among other things, compliance with laws, regulations, and the provisions of contracts or grant agreements material to the entities' major federal programs.

[21]Pub. L. No. 105-220, 112 Stat. 936 (Aug. 7, 1998).

Survivors Benefits program and Railroad Unemployment Insurance Benefits program were based on a statistical sample of railroad retirement awards and unemployment and sickness insurance claims as well as special studies and audits that were not entirely statistically based. In its fiscal year 2006 PAR, RRB reported that in May 2005, its general counsel issued a legal opinion that since the levels of improper payments did not exceed OMB's designated thresholds—exceeding $10 million and 2.5 percent of program payments—the agency was not required to conduct statistical sampling. We noted that both of these programs were required to report improper payment information for several years before IPIA reporting requirements became effective. After passage of IPIA, OMB's implementing guidance required that these programs continue to report improper payment information under IPIA, including using statistical sampling to estimate improper payments.

In addition, we noted instances where agencies estimated improper payments for only one component of the risk-susceptible program. For example, HHS's Medicare program is the largest of the programs constituting the total improper payment estimate, with an estimate of $10.8 billion for fiscal year 2006. However, this estimate represents payment errors only for its fee-for-service program component. HHS has not yet begun to estimate improper payments for its managed care component (also known as Medicare Advantage), with outlays totaling about $55 billion, or 14 percent of Medicare program outlays. HHS's auditor, an independent public accounting firm that audited its financial statements for fiscal year 2006, identified Medicare's managed care benefits payment cycle as a reportable condition in its report on internal controls. The auditor found that HHS lacks a comprehensive control environment in which the risk of inaccurate payments is not sufficiently mitigated. Specifically, HHS had inadequate procedures to review and process managed care payments, lacked documentation and procedures to determine eligibility of new providers, and provided inadequate oversight of managed care organizations. In its fiscal year 2006 PAR, HHS reported that a methodology to estimate improper payments for the Medicare Advantage program was in the initial stage of development. During fiscal year 2007, HHS plans to perform a comprehensive risk assessment for the Medicare Advantage program to determine potential areas vulnerable to payment errors. HHS anticipates reporting on the measurement project and select findings in its fiscal year 2008 PAR. However, HHS has not yet provided a target date for reporting an improper payment estimate for its Medicare Advantage program.

Improved Internal Control Is Key to Resolving Improper Payments

Agency OIGs reported management challenges in the annual PARs related to agencies' internal control weaknesses that continue to plague programs susceptible to significant improper payments. In accordance with OMB Circular No. A-136, OIGs are required to highlight issues that the OIGs consider to be the most serious management and performance challenges facing agencies. Management challenges involving internal control have a direct effect on program integrity and improper payment issues, and thus a review of the OIGs' statements on management challenges can be instructive in this regard. Generally, improper payments result from a lack of or an inadequate system of internal control, but some result from program design issues.

Internal control is a major part of managing an organization. It comprises the plans, methods, and procedures used to meet missions, goals, and objectives and supports performance-based management. Internal control also serves as the first line of defense in safeguarding assets and preventing and detecting errors and fraud. Our *Standards for Internal Control in the Federal Government* provide a road map for entities to establish control for all aspects of their operations and a basis against which entities' control structures can be evaluated.[22] Also, our executive guide on strategies to manage improper payments focuses on internal control standards as they relate to reducing improper payments.[23]

We found that over half of the programs reporting improper payment estimates also had reported management challenges that could increase the risk of improper payments, including challenges related to internal controls. For example, in the Department of Education's (Education) fiscal year 2006 PAR, the Education OIG reported that recent audits, inspections, and investigations continue to uncover problems with program control and oversight of program participants, placing billions of taxpayer dollars at risk of waste, fraud, abuse, and noncompliance. The OIG concluded that only by improving effective oversight of its operations and demanding accountability by its managers, staff, contractors, and grantees can the agency be an effective steward of the billions of taxpayer dollars supporting its programs and operations. Education's OIG also reported that identifying and correcting improper payments remains a

[22]GAO, *Standards for Internal Control in the Federal Government*, GAO/AIMD-00-21.3.1 (Washington, D.C.: November 1999).

[23]GAO, *Strategies to Manage Improper Payments: Learning From Public and Private Sector Organizations*, GAO-02-69G (Washington, D.C.: October 2001).

challenge for the agency due to ineffective oversight and monitoring of its policies, programs, and participants.

Another example involved an agency's systems used to detect fraudulent activity. Specifically, Treasury's OIG reported that some tax credits, such as the Earned Income Tax Credit, provide opportunities for abuse in income tax claims. In past years, the Internal Revenue Service (IRS) used its Web-based Electronic Fraud Detection System (EFDS) to search for signs of fraud at the time that tax returns are filed to help eliminate the issuing of questionable refunds. For its 2005 processing year,[24] IRS stopped over $412 million in improper payments. However, IRS was unable to utilize EFDS for the 2006 processing year[25] because the contractor it had hired to update the fraud detection program could not produce a working program within the established timeframe. Because IRS believed that the contractor would deliver the updated program, it had not developed a contingency plan nor taken any action to return to the old system. As a result, the Treasury OIG reported that more than $300 million in fraudulent refunds may have been issued in 2006. We identified this issue as a material weakness during our audit of IRS's fiscal years 2005 and 2006 financial statements.[26]

Agencies' Reporting of Recovery Auditing Information

Section 831 of the National Defense Authorization Act for Fiscal Year 2002 provides an impetus for applicable agencies to systematically identify and recover contract overpayments. The act requires that agencies that enter into contracts with a total value in excess of $500 million in a fiscal year carry out a cost-effective program for identifying and recovering amounts erroneously paid to contractors. The law authorizes federal agencies to retain recovered funds to cover in-house administrative costs as well as to pay contractors, such as collection agencies. Any residual recoveries, net of these program costs, shall be credited back to the original appropriation from which the improper payment was made, subject to restrictions as described in the legislation.

[24]A processing year is the calendar year in which tax returns and related data are processed.

[25]During processing year 2006, IRS processed primarily 2005 tax returns.

[26]GAO, *Financial Audit: IRS's Fiscal Years 2006 and 2005 Financial Statements*, GAO-07-136 (Washington, D.C.: Nov. 9, 2006).

Recovery auditing is a method that agencies can use to recoup detected improper payments. Recovery auditing is a detective control to help determine whether contractor costs were proper. Specifically, it focuses on the identification of erroneous invoices, discounts offered but not received, improper late penalty payments, incorrect shipping costs, and multiple payments for single invoices. Recovery auditing can be conducted in-house or contracted out to recovery audit firms. The techniques used in recovery auditing offer the opportunity for identifying weaknesses in agency internal controls, which can be modified or upgraded to be more effective in preventing improper payments before they occur for subsequent contract outlays.

I would like to emphasize that effective internal control calls for a sound, ongoing invoice review and approval process as the first line of defense in preventing unallowable contract costs. Given the large volume and complexity of federal payments and historically low recovery rates for certain programs, it is much more efficient and effective to pay bills and provide benefits properly in the first place. Prevention is always preferred to detection and collection. Aside from minimizing overpayments, preventing improper payments increases public confidence in the administration of benefit programs and avoids the difficulties associated with the "pay and chase" aspects of recovering improper payments. Without strong preventive controls, agencies' internal control activities over payments to contractors will not be effective in reducing the risk of improper payments.

Beginning with fiscal year 2004, OMB required that applicable agencies publicly report on their recovery auditing efforts as part of their PAR reporting of improper payment information. Agencies are required to discuss any contract types excluded from review and justification for doing so. Agencies are also required to report, in table format, various amounts related to contracts subject to review and actually reviewed, contract amounts identified for recovery and actually recovered, and prior year amounts.

From fiscal year 2004 to 2006, we noted that the number of agencies reporting recovery auditing information and the dollar amounts identified for recovery and actually recovered had increased, as shown in table 4.

Table 4: Improper Payment Amounts Identified and Recovered for Fiscal Years 2004 to 2006

		Fiscal year 2004		Fiscal year 2005		Fiscal year 2006	
	Department or agency	Agency-reported amount identified for recovery	Agency-reported amount recovered	Agency-reported amount identified for recovery	Agency-reported amount recovered	Agency-reported amount identified for recovery	Agency-reported amount recovered
1	Agency for International Development	did not report	did not report	$5,900,000	$5,782,000	$17,100,000	$17,090,000
2	Department of Agriculture	$2,000	$2,000	333,000	189,000	379,000	538,000[a]
3	Department of Commerce	did not report	did not report	96,354	84,551	96,000	96,000
4	Department of Defense	6,300,000	6,300,000	473,000,000	418,500,000	195,300,000	137,900,000
5	Department of Education	269,000	79,000	274,367	112,506	did not report	did not report
6	Department of Energy	6,000,000	6,000,000	10,600,000	9,500,000	11,900,000	10,300,000
7	Environmental Protection Agency	did not report	did not report	130,000	130,000	1,102,000	0[b]
8	General Services Administration	14,409,000	11,117,000	26,638,654	8,317,187	46,721,742	45,917,920
9	Department of Health and Human Services	did not report	did not report	2,100,000	14,430	1,600,000[c]	40,000[c]
10	Department of Homeland Security	did not report	did not report	2,191,000	1,207,000	502,000,000[c]	6,016,000[c]
11	Department of Housing and Urban Development	227,000	40,000	reported not cost beneficial	reported not cost beneficial	reported not cost beneficial	reported not cost beneficial
12	Department of the Interior	231,000	231,000	1,548,620	195,479	4,407,345	505,743
13	Department of Justice	973,000	780,000	1,044,320	765,086	1,851,709	1,734,421
14	Department of Labor	did not report	did not report	reported not cost beneficial	reported not cost beneficial	reported not cost beneficial	reported not cost beneficial
15	National Aeronautics and Space Administration	did not report	did not report	617,442	617,442	256,255	139,420
16	Social Security Administration	5,000	5,000	317,000	50,000	178,000	178,000
17	Department of State	did not report	did not report	5,350,000	5,190,000	2,397,200	2,276,700
18	Tennessee Valley Authority	did not report	did not report	909,573	443,763	6,793,581[d]	1,202,651

	Department or agency	Fiscal year 2004 Agency-reported amount identified for recovery	Fiscal year 2004 Agency-reported amount recovered	Fiscal year 2005 Agency-reported amount identified for recovery	Fiscal year 2005 Agency-reported amount recovered	Fiscal year 2006 Agency-reported amount identified for recovery	Fiscal year 2006 Agency-reported amount recovered
19	Department of Transportation	216,000	216,000	2,663,984	2,663,984	6,450,993	45,109
20	Department of the Treasury	855,000	669,000	428,977	364,680	2,305,424	1,442,708
21	Department of Veterans Affairs	29,500,000	27,300,000	23,001,137	12,957,264	39,155,454	30,378,423
	Total	**$58,987,000**	**$52,739,000**	**$557,144,428**	**$467,084,372**	**$839,994,703**	**$255,801,095**

Sources: OMB and agencies' fiscal year 2005 and 2006 PARs.

[a]According to USDA, amount recovered in fiscal year 2006 include some recoveries identified in fiscal year 2005.

[b]Agency did not report an amount recovered in its PAR. According to OMB, only four improper payments were identified and dollars were not statistically significant.

[c]We obtained this amount from OMB.

[d]This amount represents the agency-reported amount of $1,208,498 and an additional $5,585,083 identified from Tennessee Valley Authority's (TVA) OIG contract compliance audits, which is also included in the annual report. TVA noted that there is a partial overlap between these two amounts, but could not identify the overlapped amount.

We are pleased that progress has been made over the past 3 fiscal years to identify amounts for recovery and those amounts actually recovered. We also noted that the rate of recovery of contract overpayments for fiscal year 2006, about 30 percent, had substantially decreased from the prior year reported recovery rate of 84 percent. In our November 2006 report,[27] we raised questions regarding the overall high recovery rate of 84 percent and found discrepancies, such as the contract costs identified for recovery were considerably lower than the corresponding OIG amount identified from that year's audit reviews. We determined that the discrepancies significantly decreased the overall recovery rate from 84 percent to 22 percent. Although we have not performed a detailed review of the agencies' recovery rates for fiscal year 2006, the reported overall recovery rate of 30 percent may provide a more realistic view of agencies' recovery audit efforts.

[27]GAO-07-92.

From our review, we noted that 12 agencies reported recovering about $53 million for fiscal year 2004 compared to 18 agencies that reported recovering about $256 million for fiscal year 2006. In addition to the 18 agencies, we found that 3 agencies—Education, the Department of Housing and Urban Development (HUD), and Labor—did not report recovery auditing information for fiscal year 2006. Education reported that it reviewed all of its vendor payments from fiscal years 1998 to 2005 and found that potential recoveries were minimal. During fiscal year 2007, Education plans to review fiscal year 2006 contract payments. Education also noted that its purchase card and travel card programs are subject to monthly reviews and reconciliations to identify potential misuse or abuse. HUD and Labor reported that based on their recovery audit results, a recovery auditing program was not cost-beneficial or necessary, similar to what they reported for fiscal year 2005. Specifically, in fiscal year 2006, HUD reported that its recovery audit contractor had determined that procedures and systems in place provide strong controls for processing contract payments. Labor reported that from its statistical sample of 50 transactions, no improper payments were found, and therefore recovery audit efforts were not necessary. In addition, we noted that of the 18 agencies reporting for fiscal year 2006, 3 agencies had conducted in-house recovery audits, 8 agencies reported they contracted out their recovery audit services, another 6 agencies reported using both in-house and recovery audit contractors to perform recovery auditing, and the remaining 1 agency was silent.

Concluding Observations

In closing, we recognize that measuring improper payments and designing and implementing actions to reduce them are not simple tasks and will not be easily accomplished. Further, while internal control should be maintained as the front-line defense against improper payments, recovery auditing holds promise as a cost-effective means of identifying contractor overpayments.

Given today's budgetary pressures and the American public's increasing demands for accountability over taxpayer funds, oversight hearings such as this one today and the continuing leadership of OMB under the PMA, help keep agencies focused on the goals of IPIA and being accountable for results. Preventing, identifying, and recovering improper payments in that order are what is needed across government. Fulfilling the requirements of IPIA will require sustained attention to implementation and oversight to monitor whether desired results are being achieved.

Mr. Chairman, this concludes my statement. I would be pleased to respond to any questions that you or other members of the subcommittee may have.

Contact and Acknowledgments

For more information regarding this testimony, please contact McCoy Williams, Director, Financial Management and Assurance, at (202) 512-9095 or by e-mail at williamsm1@gao.gov. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this testimony. Individuals making key contributions to this testimony included Carla Lewis, Assistant Director; Francine DelVecchio; Christina Quattrociocchi; Heather Rasmussen; Donell Ries; and Viny Talwar.

Appendix I: Agencies and Related Programs Included in Our Review of Fiscal Year 2006 Performance and Accountability Reports and Annual Reports

	Department or agency		Program or activity
1	Agency for International Development	1	Cash Transfers
		2	Cooperative Agreements, Grants, and Contracts
2	Department of Agriculture	3	Child and Adult Care Food Program
		4	Conservation Reserve Program
		5	Direct and Counter-Cyclical Payments
		6	Disaster Programs
		7	Farm Security and Rural Investment
		8	Federal Crop Insurance Corporation
		9	Food Stamp Program
		10	Loan Deficiency Payments
		11	Marketing Assistance Loan Program
		12	Milk Income Loss Contract Program
		13	National School Lunch and School Breakfast Programs (previously School Programs)
		14	Noninsured Assistance Program
		15	Rental Assistance Program
		16	Wildland Fire Suppression Management
		17	Women, Infants, and Children
3	Department of Commerce	18	All programs and activities
4	Department of Defense	19	Civilian Pay
		20	Commercial Pay
		21	Military Health Benefits
		22	Military Pay
		23	Military Retirement Fund
		24	Travel Pay
5	Department of Education	25	Student Financial Assistance—Federal Family Education Loan
		26	Student Financial Assistance—Pell Grants
		27	Title I
6	Department of Energy	28	Payment programs
7	Environmental Protection Agency	29	Clean Water State Revolving Funds
		30	Drinking Water State Revolving Funds

	Department or agency		Program or activity
8	Export-Import Bank of the United States	31	All programs and activities
9	Farm Credit System Insurance Corporation[a]	32	All programs and activities
10	Federal Communications Commission	33	High Cost Support Program
		34	Universal Service Fund's Schools and Libraries
11	Federal Deposit Insurance Corporation	35	All programs and activities
12	Federal Trade Commission	36	All programs and activities
13	General Services Administration	37	All programs and activities
14	Department of Health and Human Services	38	Child Care and Development Fund
		39	Foster Care—Title IV-E
		40	Head Start
		41	Medicaid
		42	Medicare Advantage
		43	Medicare Fee-for-Service
		44	Medicare Prescription Drug Benefit
		45	State Children's Insurance Program
		46	Temporary Assistance for Needy Families
15	Department of Homeland Security	47	Individuals and Households Program
		48	Vendor Payments
16	Department of Housing and Urban Development	49	Community Development Block Grant
		50	Federal Housing Administration's Single Family Acquired Asset Management System
		51	Low Income Public Housing
		52	Public Housing Capital Fund
		53	Section 8—Project Based
		54	Section 8—Tenant Based
17	Department of the Interior	55	All programs and activities
18	Department of Justice	56	All programs and activities
19	Department of Labor	57	Federal Employees' Compensation Act
		58	Unemployment Insurance
		59	Workforce Investment Act
20	National Aeronautics and Space Administration	60	All programs and activities

	Department or agency		Program or activity
21	National Archives and Records Administration	61	All programs and activities
22	National Credit Union Administration*	62	All programs and activities
23	National Science Foundation	63	Research and Education Grants and Cooperative Agreements
24	National Transportation Safety Board	64	All programs and activities
25	Nuclear Regulatory Commission	65	All programs and activities
26	Office of Personnel Management	66	Federal Employees Group Life Insurance
		67	Federal Employees Health Benefits Program
		68	Retirement Program (Civil Service Retirement System and Federal Employees Retirement System)
27	Pension Benefit Guaranty Corporation	69	All programs and activities
28	U.S. Postal Service	70	All programs and activities
29	Railroad Retirement Board	71	Railroad Unemployment Insurance Benefits
		72	Retirement and Survivors Benefits
30	Securities and Exchange Commission	73	All programs and activities
31	Small Business Administration	74	504 Certified Development Companies
		75	7(a) Business Loan Program
		76	Disaster Assistance
		77	Small Business Investment Companies
32	Smithsonian Institution	78	All programs and activities
33	Social Security Administration	79	Old Age and Survivors' Insurance
		80	Disability Insurance
		81	Supplemental Security Income Program
34	Department of State	82	International Information Program—U.S. Speaker Specialist Program
		83	International Narcotic and Law Enforcement Affairs—Narcotics Program
		84	Structures and Equipment
		85	Vendor payments
35	Tennessee Valley Authority	86	Payment programs
36	Department of Transportation	87	Airport Improvement Program
		88	Federal Transit—Capital Investment Grants

	Department or agency		Program or activity
		89	Federal Transit—Formula Grants
		90	Highway Planning and Construction
37	Department of the Treasury	91	Earned Income Tax Credit
38	Department of Veterans Affairs	92	Compensation
		93	Dependency and Indemnity Compensation
		94	Education programs
		95	Insurance programs
		96	Loan Guaranty
		97	Pension
		98	Vocational Rehabilitation

Sources: GAO's analysis of cited agencies' fiscal year 2006 performance and accountability reports and annual reports

*Agency PAR or annual report was not available as of the end of fieldwork.

Appendix II: Improper Payment Estimates Reported in Agency Fiscal Year 2005 and 2006 Performance and Accountability Reports or Annual Reports

	Department or agency		Program or activity	2005 Total estimate (dollars in millions)	2005 Error rate (percent)	2006 Total estimate (dollars in millions)	2006 Error rate (percent)
1	Agency for International Development	1	Cash Transfers	0.9[a]	0.1[a]	7.0	0.8
		2	Cooperative Agreements, Grants, and Contracts	0.2[a]	0.0[a,b]	15.1	0.2
2	Department of Agriculture	3	Child and Adult Care Food Program	0.0[c]	0.0[c]	16.0	1.8
		4	Conservation Reserve Program	0.0[c]	0.0[c]	64.0	3.5
		5	Direct and Counter-Cyclical Payments	0.0[c]	0.0[c]	424.0	5.0
		6	Disaster Programs	0.0[c]	0.0[c]	291.0	12.3
		7	Farm Security and Rural Investment	16.0	1.6	3.0	0.2
		8	Federal Crop Insurance Corporation	28.0	0.9	62.0	1.9
		9	Food Stamp Program	1,432.0	5.9	1,645.0	5.8
		10	Loan Deficiency Payments	5.0	1.0	443.0	9.3
		11	Marketing Assistance Loan Program (previously Commodity Loan Programs)	45.0	0.7	1,611.0	20.3
		12	Milk Income Loss Contract Program	0.2	0.1	0.0[c]	0.0[c]
		13	National School Lunch and School Breakfast Programs (previously School Programs)[d]	0.0	0.0	0.0	0.0
		14	Noninsured Assistance Program	0.0[c]	0.0[c]	25.0	22.9
		15	Rental Assistance Program	27.0	3.2	22.0	3.5
		16	Wildland Fire Suppression Management	18.0[e]	3.7[e]	7.0	2.5
		17	Women, Infants, and Children	0.0[c]	0.0[c]	21.0	0.6
3	Department of Commerce	18	All programs and activities[e]	0.0	0.0	0.0	0.0
4	Department of Defense	19	Civilian Pay	0.0[c]	0.0[c]	62.8	0.1
		20	Commercial Pay	0.0[c]	0.0[c]	550.0	0.2
		21	Military Health Benefits	87.8[e]	1.2[e]	140.0	2.0
		22	Military Pay	432.0	0.6	65.9	0.1
		23	Military Retirement Fund	49.3	0.1	48.8	0.1

	Department or agency		Program or activity	2005 Total estimate (dollars in millions)	2005 Error rate (percent)	2006 Total estimate (dollars in millions)	2006 Error rate (percent)
		24	Travel Pay	0.0[c]	0.0[c]	8.0	1.0
5	Department of Education	25	Student Financial Assistance—Federal Family Education Loan	190.0[a]	2.2[a]	401.0	2.2
		26	Student Financial Assistance—Pell Grants	444.0[a]	3.5[a]	422.0	3.5
		27	Title I	149.0	1.2	25.2	0.2
6	Department of Energy	28	Payment programs	14.5	0.1	18.4	0.1
7	Environmental Protection Agency	29	Clean Water State Revolving Funds	3.0[e]	0.1[e]	3.5	0.2
		30	Drinking Water State Revolving Funds	0.0[f]	0.0[f]	0.0[f]	0.0[f]
8	Export-Import Bank of the United States[g]	31	All programs and activities	0.0	0.0	0.0	0.0
9	Farm Credit System Insurance Corporation	32	All programs and activities	0.0[g]	0.0[g]	0.0[h]	0.0[h]
10	Federal Communications Commission	33	High Cost Support Program[d]	0.0	0.0	0.0	0.0
		34	Universal Service Fund's Schools and Libraries[d]	0.0	0.0	0.0	0.0
11	Federal Deposit Insurance Corporation[g]	35	All programs and activities	0.0	0.0	0.0	0.0
12	Federal Trade Commission	36	All programs and activities	0.0[f]	0.0[f]	0.0[e]	0.0[e]
13	General Services Administration	37	All programs and activities[e]	0.0	0.0	0.0	0.0
14	Department of Health and Human Services	38	Child Care and Development Fund[d]	0.0	0.0	0.0	0.0
		39	Foster Care—Title IV-E	152.0[a]	8.6[a]	134.0	7.7
		40	Head Start	109.0[a]	1.6	210.0	3.1
		41	Medicaid[d]	0.0	0.0	0.0	0.0
		42	Medicare Advantage[d]	0.0	0.0	0.0	0.0
		43	Medicare Fee-for-Service	12,100.0	5.2	10,800.0	4.4
		44	Medicare Prescription Drug Benefit[d]	0.0	0.0	0.0	0.0
		45	State Children's Insurance Program[d]	0.0	0.0	0.0	0.0

	Department or agency		Program or activity	2005 Total estimate (dollars in millions)	2005 Error rate (percent)	2006 Total estimate (dollars in millions)	2006 Error rate (percent)
		46	Temporary Assistance for Needy Families[d]	0.0	0.0	0.0	0.0
15	Department of Homeland Security	47	Individuals and Households Program	397.0[a]	8.6[a]	334.0	8.6
		48	Vendor payments	494.0[a]	7.4[a]	502.0	7.4
16	Department of Housing and Urban Development	49	Community Development Block Grant (Entitlement Grants, States/Small Cities)	8.0[e]	0.2[e]	4.4	0.1
		50	Federal Housing Administration's Single Family Acquired Asset Management System	2.2	0.6	0.0[f]	0.0[f]
		51	Low Income Public Housing	326.0	5.6	378.5	1.4
		52	Public Housing Capital Fund	133.5	5.1	0.0[f]	0.0[f]
		53	Section 8—Project Based	324.0	0.0[f]	362.6	1.3
		54	Section 8—Tenant Based	551.0	0.0[f]	723.2	2.7
17	Department of the Interior	55	All programs and activities[c]	0.0	0.0	0.0	0.0
18	Department of Justice	56	All programs and activities[a]	0.0	0.0	0.0	0.0
19	Department of Labor	57	Federal Employees' Compensation Act	3.3	0.1	0.3	0.0[b]
		58	Unemployment Insurance	3,267.0	10.1	3,376.0	10.7
		59	Workforce Investment Act	7.8[a]	0.2	6.4	0.2
20	National Aeronautics and Space Administration	60	All programs and activities[c]	0.0	0.0	0.0	0.0
21	National Archives and Records Administration	61	All programs and activities	0.0[f]	0.0[f]	0.0[b]	0.0[b]
22	National Credit Union Administration	62	All programs and activities	0.0[g]	0.0[g]	0.0[h]	0.0[h]
23	National Science Foundation	63	Research and Education Grants and Cooperative Agreements	1.1	0.0[b]	0.0[f]	0.0[f]
24	National Transportation Safety Board	64	All programs and activities	0.0[f]	0.0[f]	0.0[g]	0.0[g]
25	Nuclear Regulatory Commission	65	All programs and activities[c]	0.0	0.0	0.0	0.0

	Department or agency		Program or activity	2005 Total estimate (dollars in millions)	2005 Error rate (percent)	2006 Total estimate (dollars in millions)	2006 Error rate (percent)
26	Office of Personnel Management	66	Federal Employees Group Life Insurance	3.4[a]	0.3[a]	0.8	0.1
		67	Federal Employees Health Benefits Program	196.7[a]	0.7[a]	62.5	0.2
		68	Retirement Program (Civil Service Retirement System and Federal Employees Retirement System)	153.0[a]	0.3[a]	253.5	0.4
27	Pension Benefit Guaranty Corporation	69	All programs and activities	0.0[c]	0.0[c]	0.0[c]	0.0[c]
28	U.S. Postal Service[g]	70	All programs and activities	0.0	0.0	0.0	0.0
29	Railroad Retirement Board	71	Railroad Unemployment Insurance Benefits	2.6[a]	2.3[a]	2.7	2.3
		72	Retirement and Survivors Benefits	151.8[a]	1.7[a]	157.0	1.7
30	Securities and Exchange Commission	73	All programs and activities[e]	0.0	0.0	0.0	0.0
31	Small Business Administration	74	504 Certified Development Companies[d]	0.0	0.0	0.0	0.0
		75	7(a) Business Loan Program	8.7[a]	1.4[a]	10.2	1.6
		76	Disaster Assistance	1.6	0.1	89.4	0.8
		77	Small Business Investment Companies	125.0[a]	4.7[a]	0.0[c]	0.0[c]
32	Smithsonian Institution[g]	78	All programs and activities	0.0	0.0	0.0	0.0
33	Social Security Administration	79	Old Age and Survivors' Insurance	3,681.0	0.7	3,280.0	0.6
		80	Disability Insurance	0.0[f]	0.0[f]	0.0[f]	0.0[f]
		81	Supplemental Security Income Program	2,910.0	7.7	3,028.0	7.8
34	Department of State	82	International Information Program—U.S. Speaker and Specialist Program	1.9	81.2	6.7[a]	23.8
		83	International Narcotic and Law Enforcement Affairs—Narcotics Program	0.6	0.0[b]	12.4[k]	4.0
		84	Structures and Equipment	0.2	0.0[b]	0.0[j]	0.0[j]
		85	Vendor payments	0.4	0.0[b]	0.0[j]	0.0[j]
35	Tennessee Valley Authority	86	Payment programs	36.3	0.5	7.5	0.1

	Department or agency		Program or activity	2005 Total estimate (dollars in millions)	2005 Error rate (percent)	2006 Total estimate (dollars in millions)	2006 Error rate (percent)
36	Department of Transportation	87	Airport Improvement Program	0.0[f]	0.0[f]	0.0[c]	0.0[d]
		88	Federal Transit—Capital Investment Grants	0.0[f]	0.0[f]	0.0[d]	0.0[c]
		89	Federal Transit—Formula Grants	0.0[f]	0.0[f]	0.0[d]	0.0[d]
		90	Highway Planning and Construction	0.0[f]	0.0[f]	30.2	0.2
37	Department of the Treasury	91	Earned Income Tax Credit	10,500.0	25.5	10,700.0	25.5
38	Department of Veterans Affairs	92	Compensation	306.0[e]	1.1	324.6	1.0
		93	Dependency and Indemnity Compensation	0.0[f]	0.0[f]	0.0[f]	0.0[f]
		94	Education programs	32.3[a]	1.2[a]	67.2	2.2
		95	Insurance programs	0.3	0.0[b]	0.0[f]	0.0[f]
		96	Loan Guaranty	3.5[a]	0.3[a]	0.9	0.1
		97	Pension	370.9[a]	10.9[a]	370.6	10.7
		98	Vocational Rehabilitation	6.2[a]	1.1[a]	6.0	1.0
	Total			**$39,310.2**		**$41,643.3**	

Sources: GAO prior report and analysis of cited agencies' fiscal year 2006 PARs or annual reports

[a]Fiscal year 2005 estimates or error rates were updated to the revised estimates reported in the fiscal year 2006 PARs or annual reports.

[b]Agency reported error rate was less than one percent or reported the error rate rounded to zero for purposes of this testimony.

[c]Agency did not report an annual improper payment estimate or error rate.

[d]See table 3 of this testimony.

[e]Agency reported that it had no programs or activities susceptible to significant improper payments.

[f]Agency combined with the program above.

[g]Agency did not address improper payments or IPIA in its PAR or annual report for fiscal year 2005, fiscal year 2006, or both.

[h]Agency PAR or annual report was not available as of the end of fieldwork.

[i]Fiscal year 2006 was the first year this agency was included in our scope of review.

[j]Agency reported program no longer susceptible to significant improper payments

[k]We obtained this amount from OMB.

[l]Agency reported that the annual improper payment amount or error rate was zero.

Prepared Statement of John W. Cox

Chief Financial Officer
U.S. Department of Housing and Urban Development

Hearing before the
Subcommittee on Federal Financial Management, Government Information, Federal Services and International Security

Committee on Homeland Security and Governmental Affairs
United States Senate

March 29, 2007

Chairman Carper, Senator Coburn and distinguished members of the Committee, my name is John Cox, the Chief Financial Officer for HUD. Thank you for inviting me to appear before this Committee today to speak about the results of HUD's efforts to reduce improper payments.

The Department has aggressively complied with the Improper Payments Information Act of 2002, and was the first agency to achieve green status on the President's Management Agenda initiative for Eliminating Improper Payments. I would like to go over a few of the Department's accomplishments since my office last testified before this committee on this topic in September 2005:

- We are in the process of updating our fourth annual improper payment risk assessment. Our most recent completed annual improper payment risk assessment covered the $58.8 billion in payments made by the Department in Fiscal Year 2005, and no new high risk program activities were identified. Over the past three years, the results of HUD's annual risk assessments called for the measurement of improper payment levels in eleven major program areas with the risk potential to exceed the $10 million high-risk program threshold. Those eleven programs constitute about 65 percent of the Department's total annual payment activity. Five of the eleven programs measured exceeded the $10 million improper payment threshold to require corrective action planning and annual measurement, reporting, and follow-up efforts to reduce improper payment levels.

- We completed and verified corrective actions to reduce improper payments to an acceptable level in two of the five programs originally determined to be at-risk of significant improper payment levels – payments under the Single Family Acquired Asset Management System and the Public Housing Capital Fund.

- We exceeded our internal goals for reducing improper payment levels for HUD's three remaining at-risk program areas -- the Public Housing, Tenant-Based Assistance and Project-Based Assistance Programs – which are collectively referred to as HUD's rental housing assistance programs. In 2000, HUD established a baseline estimate of $3.2 billion in gross annual improper rental assistance payments, inclusive of $2 billion in net annual overpayments, attributed to subsidy determination errors and underreporting of tenant income upon which the subsidies are based. HUD's initial goal was to reduce that $2 billion net annual overpayment estimate 50 percent by the end of FY 2005. As shown in the following table, HUD exceeded that goal by reducing net annual overpayments by 69 percent.

Reductions in Improper Rental Housing Assistance Payments Due to Subsidy Determination and Income Reporting Errors

Period	Over Payments*	Under Payments	Net Over-Payments	Gross Improper Payments
2000	$2,594	$622	$1,972	$3,216
2005	$943	$341	$602	$1,284
$ Reduction	$1,651	$281	$1,370	$1,932
% Reduction	64%	45%	69%	60%

* - Amounts shown in millions

This reduction – and the underlying internal control improvements -- was one of the key reasons HUD's rental housing assistance program area was removed from the GAO high-risk list in January 2007.

The reductions in housing subsidy determination errors resulted from HUD efforts to work with its housing industry partners at public housing agencies and multifamily housing projects through enhanced program guidance, training, oversight, and enforcement. The reduction of erroneous payments due to tenant under-reporting of income resulted from: improved income verification efforts by housing program administrators; increased voluntary compliance by tenants due to promotion of the issue; HUD's initiation of improved computer matching processes for upfront verification of tenant income; and an improved methodology for reviewing income discrepancies identified through computer matching to better determine actual cases of under-reported income impacting subsidy levels.

While the total gross level of improper payments in the rental housing assistance programs remained relatively constant between FY 2004 and FY 2005, the percentage of total payments that were improper dropped from 5.6 percent to 5.4 percent, exceeding HUD's goal of 5.6 percent. HUD paid over $27.2 billion in rental housing assistance in FY 2005, representing over 46 percent of all HUD payments.

In FY 2006, HUD implemented its new Enterprise Income Verification System for use by Public Housing Agency program administrators in conducting improved verifications of tenant income during the annual recertification process. I want to thank our agency partners at the Department of Health and Human Services and the Social Security Administration for their assistance. The new web-based, secure verification system will be expanded to the Multifamily Housing Project-Based Assistance Programs during the current fiscal year. This improved computer matching capability for verifying income has the potential to eliminate the majority of the remaining estimated improper rental housing assistance payments. This system is not only faster and more efficient, but just as importantly, it affords more privacy to tenants by eliminating the paper income verification letter that was formerly mailed to the assisted tenant's employer for completion and returned to the Public Housing Agency or other HUD program administrator for income verification. HUD's long-range strategic goal is to reduce improper rental assistance payments to less than 2.5 percent of total payments by the end

of FY 2008. That would be quite an accomplishment, given the high degree of complexity of the housing subsidy determinations and the decentralized nature of the program administration.

In conclusion, Mr. Chairman, I want to thank the employees of HUD, and our agency and industry partners, for working together to tackle the tough issue of improper rental housing assistance payments. These efforts not only reduced improper payments, allowing more funds to be available for HUD's mission, but we proved that working together we could correct long-standing issues. Utilizing enhanced technology and continued partnership with agency and industry partners will allow the Department to meet its goal of further reducing improper payments.

I am pleased to answer any questions you may have.

Statement by

David Norquist

Chief Financial Officer

Department of Homeland Security

Before the

U.S. Senate Committee on Homeland Security and Governmental Affairs

Subcommittee on Federal Financial Management, Government Information, Federal Services, and International Security

Hearing on

Eliminating and Recovering Improper Payments

March 29, 2007

Opening Statement

Thank you Chairman Carper, Senator Coburn, and Members of the Subcommittee for allowing me this opportunity to testify before you regarding the Department of Homeland Security's (DHS) efforts to reduce improper payments. I also want to thank you for Senate Resolution 94. Your statement of support and recognition of the DHS workforce is greatly appreciated. Secretary Chertoff and I are committed to strengthening the processes needed to implement the Recovery Auditing Act of 2001 and the Improper Payments Information Act of 2002 (IPIA).

Department-wide Improper Payments Information Act Testing

In Fiscal Year (FY) 2005, the Department's improper payment testing and reporting was limited, however each year we continue to make improvements. In FY 2006, we improved our IPIA process by executing statistically valid sample test plans. Based on this test work, DHS identified two high risk programs at the Federal Emergency Management Agency (FEMA): 1) Individuals & Households Program (IHP) (i.e., payments to individuals) and 2) Vendor Payments (i.e., payments to contractors). We also determined that many programs at other components are not at high risk. For example, in FY 2006 we conducted statistically valid sample testing[1] at:

- Four programs totaling $2.4 billion in payments at U.S. Customs and Border Protection;
- Four programs totaling $1.5 billion in payments at U.S. Immigration and Customs Enforcement and cross serviced components;
- Two programs totaling $2.0 billion in payments at Transportation Security Administration;
- One program totaling $0.8 billion in payments at U.S. Coast Guard;
- One program totaling $0.1 billion in payments at U.S. Secret Service;
- Three programs totaling $0.1 billion in payments at Federal Law Enforcement Training Center; and
- The Department's centralized purchase card program totaling $0.4 billion in payments.

In FY 2007, we will expand the scope and quality of our testing. First, our IPIA process was strengthened to include more front end checks for consistency with Treasury payment data. Second, all DHS components will conduct IPIA risk assessments to identify programs susceptible to improper payments, in accordance with Office of Management and Budget (OMB) guidance provided by Appendix C to A-123. In addition, major DHS components will test the design of key controls for payment management processes. We also have a much clearer understanding of which components and types of programs present the greatest challenge.

[1] These high volume programs issued greater than $100 million in FY 2006 payments, excluding payroll, intragovernmental and travel.

To ensure the long-term effectiveness of the Department's efforts to reduce improper payments, in our FY 2008 Budget we requested additional resources to enhance risk assessment procedures and conduct oversight and review of component test plans.

DHS High Risk Programs

In the wake of Hurricane Katrina, FEMA conducted testing that identified the following Disaster Relief Fund (DRF) programs as being at high risk for improper payments: 1) Individuals & Households Program (IHP) (i.e., payments to individuals) and 2) Vendor Payments (i.e., payments to contractors). The testing was designed to: determine if improper payments occurred; assess the root causes for improper payments; and develop corrective action plans to mitigate the risk of future occurrences of erroneous payments.

Individuals & Households Program (IHP)

FEMA selected a statistical sample of 815 IHP payment transactions representing 276 individual applicants within the period September 1, 2005, through March 1, 2006. The sample of IHP payments included Rental Assistance, Lodging Expense Reimbursement (LER), Expedited Assistance (EA), Repair and Replacement Assistance, and Other Needs Assistance (ONA) for Hurricane Katrina victims. The IPIA IHP testing approach was developed to determine if IHP payments were in compliance with applicable laws and regulations.

FEMA IHP testing resulted in an estimate of improper payments totaling approximately $450 million or 8.56 percent of $5.25 billion in total payments. The estimate was based on a statistically valid sample. FEMA's key findings included the following:

- Lack of identity verification controls over phone registrations for assistance.
- Limited IT systems capabilities during a catastrophic disaster.
- Limited controls to prevent duplicate payments.
- Timeliness of detective controls surrounding post-payment activities.
- Inadequate training of emergency new hires and enforcement of policies and procedures.

To address these findings FEMA initiated corrective action plans to:

- Validate social security numbers during phone registration.
- Increased IT systems capabilities to handle high volume during a catastrophic disaster.
- Prevent duplicate applications.
- Enhanced post-payments reviews.
- Enhance emergency new hire training programs for all call centers.

Vendor Payments

FEMA selected a statistical sample of 184 vendor payments made during the period September 1, 2005 through March 1, 2006. The sample of payments included transportation, rent, contractual services, supplies, and equipment to support Katrina disaster relief efforts. The IPIA Vendor Payments testing approach was developed to determine if Vendor Payments were in compliance with applicable laws and regulations. Vendor Payments testing resulted in an estimate of improper payments totaling approximately $319 million of $4.29 billion in total payments. The estimate was based on a statistically valid sample performed in conformance with IPIA guidance. Key findings included the following:

- Inadequate supporting documentation,
- Contractual deficiencies, and
- Unsupported freight amounts.

To address these findings FEMA initiated corrective action plans to:

- Review roles and responsibilities for invoice reviewers and approvers to ensure clarity.
- Enhance training and guidance for invoice processors on expectations including formalizing timelines for invoice approval and strengthening the delegation of signature authority process.
- Develop a vendor payment quality assurance program.
- Review contract language for consistency across similar goods and services regarding product substitution, freight charges and price variances.

FEMA's Path Forward

FEMA has taken steps to strengthen compliance with the IPIA and to implement OMB guidance. FEMA's IPIA Program will continue to identify and reduce the likelihood of improper payments through the following steps:

- **IPIA Assessment -** Conducting a second round of IPIA testing on Katrina IHP payments made between March and November of 2006 to evaluate the improvement from restoring and improving payment controls.
- **IPIA Risk Assessment -** Perform a risk assessment of all FEMA programs to identify programs that are susceptible to a high level of improper payments. This work will be the basis for determining additional programs that may need to be tested for improper payments.

Conclusion

DHS has made progress on IPIA, and we are on track to make more progress this year. We will continue to work closely with Director Paulison of FEMA to strengthen their core capabilities and capacity to manage payments. We will also continue to work closely with OMB to ensure continued progress in eliminating and recovering improper payments. I appreciate the support we have had from the Congress and this subcommittee. Thank you for your leadership and your continued support of the Department of Homeland Security. I would be happy to answer any questions you may have.

TESTIMONY OF
TIMOTHY B. HILL
DIRECTOR
OFFICE OF FINANCIAL MANAGEMENT
IN THE
CENTERS FOR MEDICARE & MEDICAID SERVICES
ON
MEDICARE AND MEDICAID IMPROPER PAYMENTS
BEFORE THE
SENATE HOMELAND SECURITY AND GOVERNMENTAL AFFAIRS
SUBCOMMITTEE ON FEDERAL FINANCIAL MANAGEMENT, GOVERNMENT INFORMATION AND INTERNATIONAL SECURITY

MARCH 29, 2007

Chairman Carper, Senator Coburn, distinguished Subcommittee members, thank you for inviting me here to discuss the Centers for Medicare & Medicaid Services (CMS) initiatives to reduce improper payments in Medicare, Medicaid, and the State Children's Health Insurance Program (SCHIP). At CMS, we continue to be a government-wide leader in engaging in activities that identify, reduce and recover improper payments in our programs.

Today, I would like to give you some background on Medicare, Medicaid and SCHIP and then discuss the types of payment errors we are finding and our proposed actions for reducing the occurrence of errors. I will also provide you with information about how CMS succeeded in lowering the Medicare Fee for Service (FFS) error rate for Fiscal Year (FY) 2006 and our status in measuring improper payments in the Medicaid program and SCHIP. I will discuss briefly some of the challenges we face complying with the Improper Payments Information Act of 2002 (IPIA). It is important to note that because my testimony focuses on our efforts to identify

incorrect or erroneous payments and not on CMS fraud and abuse efforts, the improper payments I will be discussing are generally not due to bad actors but rather other types of errors.

Background on Medicare, Medicaid and SCHIP

Medicare is a Federal health insurance program that provides medical insurance to 44 million people. About 37 million individuals are entitled to Medicare because they are age 65 or older, and about 7 million beneficiaries who are under age 65 are entitled because of disability. Those under age 65 generally begin to get Medicare when they have been entitled to Social Security disability cash benefits for 24 months. Total gross Medicare benefits for 2007 are estimated to be nearly $426 billion.

The majority of Medicare spending is FFS Medicare, with hospital and physician services currently representing the largest shares of this spending. The FFS component of Medicare also covers a wide range of other items and services, including home health care, ambulance services, medical equipment, and preventive services. This FFS component of Medicare is administered by CMS through contracts with private companies that process claims for Medicare benefits. During 2007, CMS estimates that Medicare contractors will process well over one billion claims (1.2 billion) from providers, physicians, and suppliers for items and services that Medicare covers. Specifically, CMS administers the claims processing and payment systems for Medicare through contracts with Carriers, Fiscal Intermediaries (FIs), and Durable Medical Equipment Medicare Administrative Contractors (DME MACs).[1] These entities in addition to Quality

[1] CMS currently is in the process of implementing Medicare Contracting Reform, which will consolidate existing contracts and contractor functions. Once fully implemented, all contractors will be referred to as Medicare Administrative Contractors (MACs).

Improvement Organizations (QIOs) review claims submitted by providers to ensure payment is made only for medically necessary services covered by Medicare for eligible individuals.

Medicaid is a partnership between the Federal government and the states. While the Federal government sets broad guidelines and provides financial matching payments to the states, each state is responsible for overseeing its Medicaid program, and each state essentially designs and runs its own program within the Federal structure. The Federal government pays the States a portion of their costs through a statutorily determined matching rate called the Federal Medical Assistance Percentage, or FMAP, that currently ranges between 50 and 76 percent. In FY 2007, total Medicaid expenditures – those that include both Federal and State contributions – are estimated to be approximately $336 billion.

In addition to Medicaid, CMS also administers SCHIP. Program benefits became available October 1, 1997, with $40 billion in Federal matching funds available over the succeeding 10 years to help States expand health care coverage to uninsured children. SCHIP is a state-administered program and each State sets its own guidelines regarding eligibility and services. Total SCHIP expenditures, including both Federal and State contributions, are estimated to be $8.2 billion for FY 2007. Total enrollment for both Medicaid and SCHIP for FY 2007 is estimated to be approximately 53.4 million.

CMS IPIA Compliance

Given the staggering size of these programs' expenditures, even small amounts of payment error can represent a significant impact to both Federal and State treasuries and taxpayers. For this

reason, CMS, as part of a sound financial management strategy, has a relatively long history of using improper payment calculations as a tool to preserve the fiscal integrity of Medicare, Medicaid and SCHIP. CMS uses improper payments calculations to identify the amount of money that has been inappropriately paid, identify and study the causes of the inappropriate payments, and focus on strengthening internal controls to stop the improper payments from continuing. However, the variation in financing and administration among Medicare, Medicaid and SCHIP requires distinct approaches to applying these financial management tools.

Medicare IPIA Compliance

In 1996, the Department of Health and Human Services' (DHHS) Office of Inspector General (OIG) began estimating improper payments in the Medicare FFS program as part of the Chief Financial Officer's Audit. The OIG produced FFS error rates from FY 1996 to FY 2002. Beginning in FY 2003, CMS, working with the OIG, implemented a much more robust process – the Comprehensive Error Rate Testing (CERT) program – to assess and measure improper payments in the Medicare FFS program. The CERT program not only produces a national paid claims error rate, but also very specific improper payment rates. These include:

- Contractor-specific improper payment rates – which measure the accuracy of our claims processors;
- Provider-type specific improper payment rates – which measure how well the providers who care for our beneficiaries are preparing and submitting claims to the program; and
- Other management related information - which provides insight into payment errors by region and reason.

Thus, in 2002 when the IPIA was enacted, CMS needed to make only minor changes to our ongoing processes for FFS Medicare to come into compliance with the Office of Management and Budget (OMB) guidance on the IPIA. In fact, CMS has calculated additional improper payment rates for FFS Medicare, as discussed earlier. This enhanced scrutiny reflects the Agency's increased commitment to use more detailed data and analysis to eliminate improper payments.

Calculating improper payment rates is only one step in the process. Remediation is the key part of CMS IPIA compliance activities. CMS, through its contractors, including the Carriers, FIs, DME MACs and QIOs use the error rates to identify where problems exist and target improvement efforts. The cornerstone of these efforts is our annual Error Rate Reduction Plan (ERRP), which includes agency level strategies to clarify CMS policies and implement new initiatives to reduce FFS Medicare improper payments. In the past, ERRPs have included plans to conduct special pilot studies (i.e., electronic medical record submission pilot) and specific education-related initiatives. CMS also directs Carriers, DME MACs, and FIs to develop local efforts to lower the FFS Medicare error rate by targeting provider education and claim review efforts to those services with the highest improper payments. The type and nature of the errors we see in the program all lend themselves to different types of corrective actions to mediate them.

For example, a primary cause of Medicare payment errors in the past has been providers not submitting the medical record documentation needed to verify the appropriateness of payment in response to our requests for documentation. Many providers were concerned that submitting medical records to a CMS contractor would be in violation of the Health Insurance Portability

and Accountability Act (HIPAA) regulations. However, the HIPAA Privacy Rule permits disclosure of protected health information to carry out treatment, payment or health care operations. Thus, we expanded our education efforts to ensure that providers understand that responding to our requests does not violate HIPAA.

Another significant cause of errors has been providers not submitting the appropriate types of medical record documentation to support the types of services billed to the Medicare program. CMS implemented a number of corrective actions to reduce these types of errors, including education and more intensive efforts to locate and contact providers. These corrective actions have resulted in an 83 percent decrease in documentation errors since 2004.

CMS also uses contractor-specific error rates to evaluate the performance of the contractors that process Medicare claims. While our previous contracting authority limited CMS's ability to take action against contractors with high error rates, implementation of Medicare Contracting Reform (MCR) enacted by the MMA is changing the contracting process and the contractor incentive structure. One key outcome of this initiative is the ability to use incentives to get our contractors to eliminate improper payments. In 2004, CMS conducted a study to evaluate whether the Agency could reduce improper payments by using award fees as incentives for contractors to lower their paid claims and provider compliance error rates. The outcome of that pilot was positive and CMS plans to use award fees as incentives in the future to reduce improper payments as part of MCR.

We believe our efforts in Medicare have been a success. In November 2006, HHS reported a Medicare FFS paid claims error rate of 4.4 percent for FY 2006, a significant decrease from the 5.2 percent reported in 2005, and significantly lower than the 10.1 percent rate reported in FY

2004. We have far exceeded our expectations, having reduced the error rate beyond the 2006 goal of 5.1 percent. With continued monitoring and error reducing efforts we aim to achieve our future targets of 4.3 percent in 2007, 4.2 percent in 2008, and 4.1 percent in 2009.

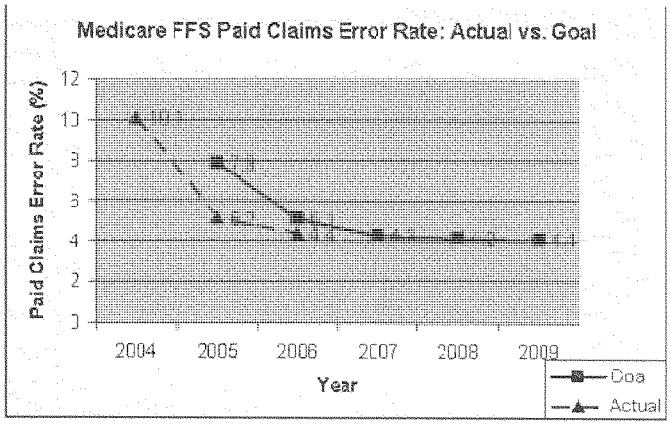

Figure 1:

Medicaid and SCHIP IPIA Compliance

Since I last appeared before the Subcommittee, CMS has made a great deal of progress in its efforts to successfully implement the Medicaid and SCHIP payment error rate measurement (PERM) program quickly and effectively, and we are on track to finalize the establishment of the PERM program. To that end CMS fully expects to implement the State corrective action process, whereby States will analyze root error causes that contribute to improper payments and develop corrective actions to address error causes which should ultimately reduce improper payments over time.

In response to States' expressed desire to provide input beyond the rulemaking process, CMS is working to improve communications with the States. We are establishing a PERM Technical Advisory Group that will consist of CMS and State representatives and will have monthly conference calls to discuss high level policy decisions and other conceptual ways to reduce State cost and burden. CMS believes that these steps will provide States the opportunity to have more direct involvement with CMS to offer suggestions and recommendations for reducing State cost and burden.

To help ensure compliance, CMS expects to:

- Continue efforts to achieve greater program efficieney;
- Reduce improper payments in Medicaid and SCHIP through States' corrective actions;
- Have States initiate recovery of erroneously paid Federal funds in these programs as identified through the PERM program; and
- Report a national program error rate in the PAR for each fiscal year measured. However, due to unexpected challenges facing the FY 2006 measurement (e.g., inaccurate State data), CMS will report a preliminary Medicaid component error rate in the FY 2007 PAR.

As the PERM program matures, CMS will identify areas in improper payment measurement that can be improved upon to make the program more efficient, to reduce cost and burden, and to help ensure accurate program error rates. Through experience, lessons learned, and State partnership, CMS is committed to advancing the efficiency and accuracy of the PERM program as it evolves.

PERM was implemented to measure the FY 2006 Medicaid FFS error rate for the FY 2007 PAR. For FY 2007, we expect to measure improper payments in the FFS, managed care and eligibility components of Medicaid and SCHIP to be reported in the FY 2008 PAR. Therefore, we expect Medicaid and SCHIP to be fully compliant with IPIA by 2008. CMS has and will continue to work closely with OMB to ensure that the PERM program meets the requirements of the IPIA and subsequent OMB guidance.

Fraud, Waste and Abuse

CMS' actions to safeguard Federal funds are not just limited to the error rate programs described in this testimony. Program and fiscal integrity oversight is an integral part of CMS' financial management strategy and a high priority is placed on detecting and preventing improper or fraudulent payments. To that end, CMS has made significant changes to its program integrity activities in the past year. These changes include the creation of new divisions within CMS to focus on data analysis to identify problem areas through trend analysis of claims data.

CMS has taken several specific actions to ensure that Federal dollars are being properly spent and fraudulent billings are stopped when they are detected. Our Los Angeles (LA), California and Miami, Florida satellite offices continue to be successful in helping to curtail fraudulent spending in those high risk areas. We are also planning to open a satellite office in New York in Spring 2007. Through the combined efforts of the CMS LA satellite office, the Program Safeguard Contractors (PSC) and the claims processing contractors operating in California, CMS has collectively identified over $2.1 billion in improper payments in Calendar Years 2005 thru

2006. This includes the denial of claims based upon fraud indicators and the collection of overpayments for claims reviewed after payment has occurred which have been identified as potentially fraudulent or highly suspect.

The goal of the satellite offices is to work collaboratively with our partners to test creative and innovative approaches to detect, investigate and prosecute fraud against the Medicare Trust Fund. A recent example of this is the Los Angeles tax project. The LA office is conducting a unique pilot program with the District Attorney (DA) of LA County to try and more effectively deal with the crisis of health care fraud through the prosecution of health care providers (both non-filers and low-filers) for state income tax evasion. Relying on an elaborate communications network, the LA project provides partners with a new tool for dealing with health care providers suspected of committing insurance fraud within California and it is expected to be successful in other states in which there is a state income tax.

The LA Project works. As of February, 2007, five cases have been filed under the LA project, and three convictions have resulted in prison sentences. The direct result to the Medicare program is that "bad" providers are identified and prosecuted, and providers are convicted of felony charges. Felony convictions may be used by the Medicare and Medicaid programs to revoke the billing privileges of the Medicare provider. Subsequently, the provider may be removed from the program. In addition, when restitution is ordered and collected from the provider, Medicare will receive remuneration.

Because of the success of the project in LA county, the DA of LA County and CMS are partnering to expand the program both to other areas of California and nationally. Specifically, CMS is currently working with the California Franchise Tax Board and the State of California to implement the project statewide. In addition, we are in beginning discussions with the state of New York tax authorities and prosecutors. Preliminary discussions concerning Federal expansion have begun with representatives from the Internal Revenue Service.

In 2004, CMS's Miami Satellite Office launched a joint initiative with the Department of Justice (DOJ), the OIG, the Federal Bureau of Investigation, the Florida Medicare Carrier and the Florida Part A & B Medicare PSC, and the State of Florida (Department of Health, Agency for Health Care Administration, Medicaid Fraud Control Unit, and Office of Drug Control) to address widespread Infusion Fraud in South Florida. Under the typical scam, for-profit clinics and doctors are recruiting and paying kickbacks to HIV/AIDS patients to receive unnecessary or non-rendered infusion services billed at medically unbelievable frequencies and dosages. Some incorporate identity theft into the scam as well, billing for infusions and injections to bogus patients, using stolen beneficiary Medicare numbers and physician Provider Identification Numbers along with forged signatures on reassignment of benefits forms. Combinations of corrective actions like prepayment edits (beneficiary-specific, provider-specific, provider-type, dollar thresholds and medically unbelievable dosages), payment suspensions, joint federal/state site visits, provider enrollment onsite and activity checks, enrollment revocations and deactivations, data analysis and complaint investigations and prosecutions and plea agreements have resulted in savings to the Medicare Trust Fund in excess of $1.8 Billion.

When instances of fraud or abuse are detected through any of these oversight mechanisms, CMS refers those cases to law enforcement. CMS has actively partnered with its law enforcement partners at the DOJ and OIG to aggressively pursue enforcement actions against those providers and suppliers that are found to be deliberately defrauding the Federal health care programs.

CMS is making improvements to its data analysis efforts. To achieve this we are collecting vulnerability data from many of our partners, including Medicare contractors, and using a variety of data analysis tools to review Medicare claims data. Much of our work will focus on addressing vulnerabilities early in their lifecycle and those that have high, estimated dollar impact to the Medicare program. Our program integrity efforts will focus on the top 10 vulnerabilities identified through our data analysis and developing corrective actions to address these identified vulnerabilities. This enhanced focus on data will enable our program integrity efforts to be more proactive rather than reactive, thus enabling us to focus more activities on actually preventing fraud rather than simply mitigating it.

Recovery Audit Contractors

Section 306 of the Medicare Prescription Drug Improvement and Modernization Act of 2003 (MMA) gave CMS additional authority to pilot a new contracting authority designed to detect improper payments. This MMA provision directs the Secretary to demonstrate the use of Recovery Audit Contractors (RACs) in identifying Medicare underpayments and overpayments, and collecting Medicare overpayments. The demonstration is being conducted in California, Florida and New York and has been a great success. In March, 2005 CMS awarded contracts to 5 different companies with extensive experience performing recovery auditing services in private

industry and/or Medicaid. To date these five contractors have identified over $400 million in potential overpayments, and have so far collected $144 million. The overpayments were identified through a careful review of individual Medicare claims to determine if the claims were medically necessary, correctly coded and conformed to Medicare payment policy.

It is clear from the demonstration results thus far how effective recovery auditing can be. Based on this effectiveness, the Tax Relief and Health Care Act of 2006 mandated the use of recovery audit contractors in all states by 2010. We have developed an expansion plan which will allow us to begin using recovery audit contractors in all states in FY 2008. CMS' implementation plan will have recovery audit contractors reviewing targeted Part A and B claim types in FY 2008 and all Part A and B claim types by 2010. This incremental approach will allow CMS to work closely with the national and state health care associations to assure that health care providers have up to date information regarding the expansion process.

We have learned a great deal during the demonstration and as important as the recovery of improper payments is, CMS sees the RAC program as an important tool in reducing and eliminating future improper payments. In order to do this, CMS is analyzing all RAC findings internally and externally through an independent evaluation contractor to determine what actions CMS, Medicare providers and claims processors can take to improve payment accuracy and eliminate improper payments. These actions will include the installation of new or improved edits in the claim payment systems, industry wide and/or provider-specific education and clarifications to coverage and payment policies.

As mentioned previously, we have an aggressive timetable in place to expand the program and meet the mandated target of 2010. Based on the results of the demonstration, we expect the expansion will be successful and that recovery auditing will become an important tool in our efforts to eliminate improper Medicare payments.

Conclusion

CMS is strongly committed to protecting taxpayer dollars and ensuring the sound financial management of the Medicare, Medicaid, and SCHIP programs. As evidenced by the testimony today, the Agency has taken significant actions to meet IPIA standards in Medicare and is taking a number of proactive steps to become IPIA compliant in Medicaid and SCHIP. The Agency has developed a comprehensive strategy that will strengthen Federal oversight of State financial practices. We have made a great deal of progress, and we look forward to continuing to work cooperatively with you. CMS and the Administration fully support this Subcommittee's efforts to improve the fiscal health of the Medicare, Medicaid, and SCHIP programs. I look forward to answering any questions you might have.

Hold for Release
Until Presented by Witness
March 29, 2007

Statement of

Terry Bowie
Deputy Chief Financial Officer
National Aeronautics and Space Administration

before the

Subcommittee on Federal Financial Management, Government Information, Federal Services, and International Security
Committee on Homeland Security and Governmental Affairs

United States Senate

Chairman Carper, Senator Coburn, and Members of the Subcommittee, thank you for the opportunity to appear today to discuss NASA's progress in identifying, eliminating, and recovering improper payments. NASA is committed to ensuring that taxpayer resources are used appropriately and, therefore, that the Agency makes proper payments. In my testimony today, I will outline the steps NASA has taken to address improper payments, including complying with the Improper Payments Information Act (IPIA) of 2002.

I would like to begin by explaining the composition of NASA's contracts and how that affects our payments. Contractors support the execution of many of NASA's research and development (R&D) programs. The variable and often unpredictable nature of this complex R&D work leads NASA to use cost versus fixed-price contracts. While both contract types are used in various NASA programs, cost contracts represent approximately 88 percent of payments made, and fixed-price contracts represent the remaining 12 percent. NASA has implemented a multi-pronged approach to oversee the integrity of the payments for its R&D programs and associated contracts.

Effective contract process controls represent one element of our approach and are the cornerstone of NASA's efforts to ensure proper payments. Once contract work is underway, NASA adheres to financial management procedures and internal controls that help to ensure that proper payments are made from the initial disbursement of funds. As an important second element of our approach, the Defense Contract Audit Agency (DCAA) reviews cost contracts and our contractors' adherence to accounting and control requirements. For cost contracts, the DCAA also conducts contract close-out audits that

may identify any questionable costs. Any questionable costs are reviewed by the NASA contracting officer for resolution, if necessary.

As a third element, complementary to our program integrity activities, the Agency has taken the additional step of establishing an Acquisition Integrity Program (AIP) aimed at strengthening acquisition oversight and management. AIP was formally launched in December 2006 by NASA's Deputy Administrator, Shana Dale, and tasked with ensuring that transparency, accountability, and integrity remain paramount touchstones in all aspects of the NASA acquisition process. This commitment to preserve resources is a collaborative effort among the Offices of the Inspector General, the Chief Financial Officer, General Counsel, and Procurement. The AIP seeks to maximize remedies that return funds to Agency accounts for use in required areas, identify irresponsible contractors for suspension or debarment, and improve the understanding and effectiveness of procurement processes.

Finally, in accordance with the IPIA of 2002 and consistent with Office of Management and Budget (OMB) guidance, NASA seeks to continually strengthen its program integrity activities and assess its risk assessment approach and recovery audit processes.

NASA, as well as other agencies, is required to complete an improper payments risk assessment. For its FY 2006 risk assessment, NASA used the results of the prior year's recovery audit. Through that process, NASA reviewed approximately $57 billion of cost and fixed-price contract payments across all programs dating back to 1997. Based on the results of that assessment, NASA found the total value of improper payments that had not already been identified and reported in prior years to be $256,255. This formed the basis for the amount reported in the FY 2006 Performance and Accountability Report (PAR). In that document, NASA reported that the Agency's assessed risk and actual results for the past three years have shown NASA's improper payments to be less than the benchmark 2.5 percent of program payments and less than $10 million.

There have been several observations regarding Questioned Costs and their relationship to the improper payment figures reported in NASA's PAR. Questioned Costs are not analogous to improper payments. Rather, they are costs that NASA's Office of Inspector General (OIG) found had no supporting documentation at the time of audit, or that they recommend be further reviewed by NASA management to determine validity, or questioned whether they were expended for an unnecessary purpose. Therefore, since there are more categories of possible Questioned Costs than exist with improper payments and since these audit Questioned Cost are not always sustained, it is likely, and is in fact typically the case, that the OIG would report a higher figure for Questioned Costs than the amount that is reported as improper payments.

For FY 2007, NASA's risk assessment approach incorporates lessons learned from the results of prior year audit recovery activities and incorporates OMB Memorandum M-06-03, Issuance of Appendix C to OMB Circular A-123, August 10, 2006 instructions. This risk assessment addresses disbursement activities on a program basis for both cost and

fixed-price contracts. A statistically valid sample of payment transactions will be obtained and tested, after which, NASA will report the results.

With respect to a recovery audit program, as I noted earlier in my testimony, NASA performed a comprehensive recovery audit in FY 2006. NASA is implementing improvements in our FY 2007 recovery audit. And, consistent with OMB guidance, the Agency has chosen to exclude cost contracts from the scope of its recovery audit activities. Cost contracts establish a cost ceiling that cannot be exceeded without NASA's approval. The contractor then bills NASA based on the effort expended. Payments under cost contracts may be interim, provisional or otherwise subject to further adjustment in accordance with the terms of the contract. These contracts are already subjected to on-going reviews. Further, the DCAA conducts interim and final audits of these contracts. At contract closeout, all prior interim payments made under these cost contracts are accounted for and reconciled. Including these contracts in a recovery audit program would result in duplicative audits of contractor records and, to date, has not yielded monetary benefits or proven to be cost beneficial for external review based on contingent recovery fees.

Based on lessons learned over the past few years, the Agency is revising contractor requirements in its Request for Proposal for audit recovery services.

We have taken steps to bring our program into compliance with OMB's guidelines for implementing the Improper Payments Information Act of 2002. As a result, I am confident in the results of our assessments. We will continue to adopt lessons learned from future recovery audits to ensure that we are making the most of those efforts.

In closing, NASA is fully committed to ensuring that Agency payments are properly made and that the Agency fully complies with the Improper Payments Information Act of 2002.

Mr. Chairman, I would be pleased to respond to any questions you or the other Members of the Subcommittee may have.

Statement of Mr. Lee White
Executive Vice President
PRG-Schultz International, Inc.

Presented to a Hearing of the Subcommittee
On Federal Financial Management, Government
Information and International Security
Committee on Homeland Security
And Governmental Affairs
U.S. Senate

Entitled "Eliminating and Recovering Improper Payments"

March 29, 2007

Chairman Carper, Senator Coburn and distinguished members of the Subcommittee.

Thank you for the invitation to testify today on recovering improper payments. My name is Lee White, Executive Vice-President, PRG-Schultz International.

We are very aware of and apprcciate this Subcommittee's work as steadfast overseers of the public trust and your efforts to take on the difficult task of ensuring strong stewardship of our Government's finances.

As the largest recovery audit company experienced in assisting corporations and government tackle improper payments, we are honored to make a contribution to assist you in ensuring that all means possible are brought to bear on this critical issue.

PRG is a recovery audit company and part of an industry that has graduated over the years from auditors collecting boxes of invoices, contracts and purchase orders to massive data centers containing multiple, integrated, proprietary applications, databases, and dedicated specialists. We are contingency auditors—that is, we keep a portion of money that we find and the overpayments that we identify would typically go unrecovered.

Recovery audits are an accepted part of American business. We audit many of the Fortune 100 companies. Corporate giants and mid-sized companies have embraced a process that has yielded billions of dollars in savings for their consumers and shareholders. Our company alone audits one trillion dollars in transactions or seven percent of the Gross Domestic Product and we recover nearly one billion dollars a year. Simply put, our corporate clients believe that the juice is worth the squeeze. They have fully embraced the process as a best practice that helps them recover lost funds, identify internal control weaknesses, and improve processes. With each of our clients we regularly provide advice on how to improve their processes to avoid future overpayments.

We do this with a process that sifts through mountains of data. We thrive in large-scale and complex environments. Proprietary algorithms kick out discrepancies and we drill into those discrepancies to find and validate overpayments or underpayments. Hallmarks of our approach are privacy and security of data which are fully compartmentalized and only used for the purpose intended.

Claims are fully researched and validated before they are submitted for collection. The government must sign off on each claim and payment requests are prepared by us and issued by government officials. We then work with the vendor to gain authorization to either recoup the funds from the future payments or have the vendor issue a check as

repayment of the overpayment. Because many relationships are repeat business, we frequently don't have to collect checks. Rather, return of overpayments takes the form of a credit on future purchases.

As you would expect, we also find that once vendors know that they are going to be subjected to a recovery audit, they improve their processes to ensure that they are not over billing.

Recovery auditing in government represents potentially the best of all worlds—private sector business principles and practices coupled with state-of-the art technology projected on government enterprises. It is a formula for success that can readily be achieved with the support of Congress, OMB, and the agencies.

We realize that contingency recovery audits are not a panacea for the improper payment problem but can be a useful and effective tool in the arsenal to ensure government and taxpayers are not paying for goods and services they don't receive. Employing professional recovery auditors can allow agencies to free-up audit and IG resources to go after improper payments that are not conducive to the contingency recovery audit model.

The Office of Management and Budget has made tremendous strides in taking on this issue and the Administration is increasingly strengthening its emphasis on the problem. Recovery audits can help further this effort. As with our most successful corporate clients, government has all of the fundamental ingredients to provide a ripe environment for success. These include massive and robust data bases, large and complex spending and central management of programs.

We have entered into contracts with GSA, HHS, and the Departments of Justice, Transportation, Interior, State, Agriculture and Defense. To date, we estimate that contingency recovery auditors government-wide have returned over $600 million to the Government. However, we could have done much better. We have been successful when the agencies wanted the money and where they were willing to provide us with access to the data that we needed to do our job. Where this cooperation is lacking, we do not have good results.

Several Federal Agencies have yet to fully embrace the concept. An example of an agency where the program is started but yet to realize its full potential is the Department of Defense. Here, expenditures for goods and services exceed $160 billion a year. Defense has taken a big first step with the issuance of a Directive and we hope that they will see fit to follow through with aggressive recovery implementation in all of their

entities for most of their spend categories. Other agencies have initiated internal recovery audits while still others have not undertaken recovery audits at all.

Wherever Government deploys the practice, success occurs in the same environment that engenders success in the private sector: (1) where we have willing partners who are incentivized to save money; (2) where we have large scale enterprises with complex systems; (3) where there is readily available data and supporting documentation; (4) where there is a forward looking mindset and motivation for continuous improvement.

Our experience is that providing real incentives will create the impetus to make the program work. Hard working Federal public servants have a lot on their plate. As such, they gravitate to those programs that will realize the biggest bang for their buck within their agency. If we want them to take the improper payment program head-on, agencies need to be incentivized.

Further on the matter of incentives, the 2001 Defense Authorization Act that mandated recovery audits in Government allowed auditors to be paid a portion of the money recovered. However, it only allows agencies to keep their portion of the funds collected if it was appropriated and recovered in the same fiscal year. If the appropriation had expired, funds would go to general receipts of the Treasury and agencies were only allowed to keep funds to cover expenses actually incurred in conducting the recovery audit programs.

A successful government recovery audit program is best exemplified at CMS. Here, recovery auditors already have identified over $400 million in savings while operating only in three states without yet hitting full-stride. This results from a couple of key factors. Both the ingredients listed above for a successful government recovery audit program and legislation that allows CMS to keep savings for the Trust Fund exist because they operate under a statute that was enacted separately from the program established in the Fiscal Year 2002 Defense Act. CMS officials are willing partners prepared to remove any impediments to a successful program.

Once incentives are established, we would hope that the three remaining issues that impede fully successful government recoveries will be resolved. These are:

- Access to data. We have contracted with agencies and have moved forward vigorously only to run into obstacles to obtaining even rudimentary electronic and hard copy information that we need to do our job.
- Recovering valid claims. Another major issue arises when we identify claims and the agency does not follow through with the contractor to collect the money, frequently without explanation as to why the claim is not settled.
- Resolving claim disputes. There currently is no formal mechanism for escalating claims and ownership of the claim resolution issue. Overpayments often are identified only to lay dormant due to inaction by the Government with no follow-through.

We need to reward success. Today's culture needs to be changed from the existing mind-set where agency officials may be reluctant to implement recovery audit programs because it might make them look bad to tomorrows program of rewarding them for protecting the public trust by having an effective program. Our corporate clients use us to audit their payments for errors not because they are poorly managed, after all their aggregate payment accuracy rate of 99.9 percent is very impressive. Just the opposite: They use us to audit their payments for errors because they are well managed. Because they are well managed, they realize that finding and correcting that last one-tenth of a percent is worth millions of dollars in annual cost savings. Further, our best corporate clients realize that by using outside recovery audit contractors, they are not only able to identify and correct past errors, they are also able to improve their payment processes. They understand that over time, while errors can never be eliminated entirely, they reduce their number of errors that will occur in the future by assuring they don't happen in the first place. Recovery auditing will be more successful in government if the agencies audited benefit rather than are harmed by error corrections, and we encourage policy that supports this objective.

Another key area that warrants consideration is the process of getting the recovery audits started. Once contracts are awarded, we have to re-invent the wheel with each agency having to establish its own parameters for a successful program. And, as is the case with large agencies such as Department of Defense, each organization within Defense has to establish implementation procedures that take time to develop and often are different

from the last agency that implemented the process. The implementation process would be greatly expedited if Government developed a defined program structure that agencies could use to implement the audits. This would provide a guide to address issues such as data access and claims processing that continually arise with the award of each contract.

While contingency auditors bear nearly all of the start-up costs to recover overpayments, the Government has some costs associated with gathering data and issuing claims. Agencies normally do not budget for these expenditures and cooperation with the recovery contracts means diversion of some resources. We recommend that some money be set aside to lay the groundwork for the audits and, once the process is jump-started, on-going recoveries can pay back costs incurred and provide the resources needed to proceed with further recoveries.

We know that the committee is very interested in accurate reporting of the scope of the improper payment problem in government. Along these lines, we believe that employing recovery audits in the agencies goes hand-in-hand with the implementation of the Improper Payments Information Act. Running payments through the recovery audit process will yield a wealth of information to improve reporting and payment accuracy.

A further area of great potential is grants made to local jurisdictions for various programs such as those issued by the Departments of Homeland Security, Justice, and Transportation. Naturally, as with all outlays, the best way to limit abuse in this area is to

strengthen and enforce the criteria on awarding grants in the first place. But when grants are made and abused, there are restrictions of the Single Audit Act that preclude a review of grants at the local level. The wide dispersion of thousands of grants may be more suited to fee-for-service work as it may not lend itself to large scale, electronic data-centric contingency audits. Also, in order to employ contingency recovery auditors in the pursuit of grant overpayments, there needs to be a mechanism for contingency auditors to be paid a share of the recoveries.

Based on our corporate experience and our analysis of government estimates that emanate from the data reported by agencies as part of the Improper Payments Information Act enacted in November 2002, our recoveries to date are only the tip of the iceberg. We can do better. Because we normally go back three years, we estimate that the recoverable audit base for all agencies is $2.46 trillion. With error rates at one-half of one percent to five percent, depending upon the spend category, we estimate the potential savings for the taxpayer in the first full year of auditing the entire base would be between $60 billion to $90 billion with a reduced amount in ensuing years.

We have the experience, we have the technology, and we have the willingness to put a huge dent in the Government's improper payment problem. Often, despite their best efforts, agencies undertake their own internal recovery audit programs internally. We think the private sector can do it better. First, it is all we do and we are good at it. Second, we are third-party who can take an objective look at the problem and remedy it.

However, we believe that commercial recovery audits will work for some programs and not for others. We are good at recovering funds from businesses and organizations that overcharge the Government for goods and services. Government should take the lead role in recovering funds from individuals and beneficiaries such as underpayments for taxes and things like food stamps, earned income tax credits and social security payments.

Our recommendations for improving the process include:

- Require agencies as part of the Improper Payments Information Act to report on their contracted contingency recovery audit programs, efforts they have made to remove impediments to a successful program, and instances where overpayments have been identified but not collected. Sifting data through the recovery audit process can help the Government yield more reliable reporting data and generate funds at the same time.
- Establish a joint industry and government OMB-led task force comprised of key agency officials and recovery audit industry experts to firmly establish the scale of overpayments conducive to recovery audits such as purchases, leases, IT expenditures, telecommunications, and health care. This task force would develop recommendations and a road map for removing any impediments. Also, encourage the Office of Management and Budget to work with agencies

to remove impediments to successful recovery audits by mandating that ready access be provided to data.

- Institutionalize the recovery audit processes as a part of the traditional internal government erroneous payment identification techniques. With our corporate clients, our processes become an integral part of their overall procurement and financial management systems. The process works in the background with these systems sorting through data and yielding savings on a continual basis. It becomes an accepted way of doing business. Implementation can be facilitated by a government-wide template for agency implementation that includes procedures for data access, collections, security clearances and dispute escalation. This set of consistent protocols would greatly facilitate proliferation of the recovery audit process. Using pre-negotiated contract vehicles with a menu of recovery audit services can further expedite the process and therefore agencies can issue task orders based on pre-negotiated terms.
- Develop a contract vehicle for a Government-wide disbursement audit for all centralized payment facilities. Purchases of commodities are a natural early target. Disbursement overpayment recoveries would be withheld from future vendor remittances from the Treasury and would result in sizable and immediate savings to taxpayers.
- Build on the success realized by CMS in employing recovery auditors for Medicare payments and extend the process into Medicaid by using Federal

funding to provide incentives for states to implement an effective recovery audit program.

- Allow agencies to keep a portion of the funds recovered. One mechanism would be to create a "Government Efficiency Fund" wherein recovered money would be made available for Government efficiency initiatives that are reported to Congress annually. Remove restrictions of the Paperwork Reduction Act that impede the issuance of documentation requests and demand letters to suppliers of goods and services to the Government.
- Examine the Single Audit Act to facilitate recovery audits for programs such as grants to states by Federal Agencies that are currently prohibited from secondary audits under that Act. The provisions of the Act would be waived where these programs demonstrate an intolerable level of erroneous payments.

In conclusion Mr. Chairman, recovery auditing is a tried and tested method which, if properly implemented, can greatly assist the Government in taking on this massive issue. The recovery audit industry has the tools and experience while the scale and complexity of government creates a significant opportunity greater than even that of the private sector. Removal of the last remaining impediments through a working partnership with industry will yield great returns to the taxpayer.

Thank you Mr. Chairman. I'm prepared to answer any questions you may have.

EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF MANAGEMENT AND BUDGET
WASHINGTON, D.C. 20503

THE CONTROLLER

The Honorable Tom Coburn, M.D.
Ranking Member, Subcommittee on Federal
Financial Management, Government
Information, Federal Services,
and International Security
Committee on Homeland Security
and Governmental Affairs
United States Senate
Washington, DC 20510

Dear Senator Coburn:

Thank you for the recent opportunity to testify before the Subcommittee on the Administration's efforts to implement the Improper Payments Information Act of 2002 (IPIA). Your ongoing attention to the identification and elimination of improper payments has been a critical factor in the Administration's success to date. As we approach the challenges that still remain, I look forward to our continued collaboration on finding cost-effective solutions for improving the accuracy and integrity of Federal payments.

To this end, I am writing to seek further clarification regarding a concern expressed by the Subcommittee at the March 29, 2007 hearing. Specifically, the Subcommittee raised a question about whether the definition of improper payments found in the Office of Management and Budget (OMB) Circular A-123, Appendix C is resulting in one or more "high risk" programs being incorrectly excluded from IPIA reporting activities.

Under OMB's current definition of programs that are risk susceptible to significant improper payments (i.e., "high risk" programs), Federal agencies have deemed 65% of all Federal outlays ($1.7 trillion out of $2.7 trillion) as subject to IPIA reporting requirements. Therefore, to identify any additional programs that warrant IPIA coverage, we must examine the remaining $1 trillion in outlays. Of the $1 trillion in outlays not currently reported by Federal agencies under the IPIA, approximately:

e) $227 billion (23%) is net interest on the public debt, where the IPIA is not applicable;
f) $415 billion (41%) is contract payments, where improper payments are currently being reviewed and reported under the Recovery Audit Act;
g) $227 billion (23%) is civilian compensation (non-DOD) and benefits that have not been identified as high risk by any civilian agency; and,
h) $131 billion (13%) is all other programs, many of which have small outlay totals, and thus are unlikely to meet the IPIA threshold of exceeding $10 million in improper payments annually. This amount also represents programs that have been risk assessed on an annual basis and were not found to be susceptible to improper payments.

Based on this breakdown, we believe that Federal agencies are currently capturing all appropriate program outlays for IPIA reporting. We remain concerned that adding new, lower risk programs to our current reporting universe will cause Federal agencies to divert scarce resources from areas with a significant return on investment (i.e., working to address the $1.7 trillion in outlays currently being tracked under the IPIA) to areas with no or negative return on the investment. Still, we remain open to your input on programs that should be added to our current IPIA reporting totals. As the Deputy Director for Management, Clay Johnson, committed to you during his hearing on December 5, 2006, OMB will happy to look into any specific program that falls outside of OMB's definition of "significant erroneous payments" if requested by Congress or GAO.

I have enclosed my responses to the Questions for the Record provided on April 18, 2007. And again, I look forward to our continuing partnership on this issue and welcome the opportunity to discuss new ideas and approaches for building on the foundation of success that has been put in place since the IPIA was enacted.

Sincerely,

Linda M. Combs
Controller

Enclosures

Identical Letter Sent to The Honorable Thomas R. Carper

Post-Hearing Questions for the Record
Submitted to Linda Combs
From Senator Thomas R. Carper

"Eliminating and Recovering Improper Payments"

March 29, 2007

1. You mentioned in response to one of my questions during the hearing that you expect partial improper payments reporting for the Child Care and Development Fund, the Medicare Advantage program, and the Medicare Prescription Drug Benefit Program by FY 2008. What portions of these programs will be reporting by that time and what portions will not be? Also, when do you expect to have Temporary Assistance for Needy Families reporting?

OMB response:

As I stated in my testimony, all of the programs currently deemed high risk that have not yet reported an error measurement have a timeline in place for reporting. Table 3 in the Appendix of OMB's report, Improving the Accuracy and Integrity of Federal Payments, identifies the programs and the fiscal year we anticipate the agencies reporting an error measurement.

The Department of Health and Human Services (HHS) will report an error rate for the eligibility component of the Child Care and Development Fund (CCDF) program in its fiscal year (FY) 2008 Performance and Accountability Report (PAR). HHS has determined that the eligibility component is the most critical area to measure because if an applicant is incorrectly deemed eligible (or eligible for the wrong subsidy), all payments based on approval of this application would be improper.

HHS will report the first component of error measurement for the Medicare Advantage program in its FY 2007 PAR. HHS will report on the systems ability to accurately calculate Medicare Advantage payments. HHS will continue to examine which, if any, additional components of the payment process within the CCDF and Medicare Advantage programs pose significant risk of improper payments and therefore should be added to the error measurement in future years.

HHS is currently performing a risk assessment on the Medicare Prescription Drug Benefit program. The size and complexity of this new program requires that a comprehensive risk assessment be completed, and then the risk points identified be weighed and prioritized to determine which component(s) should be measured and reported in the FY 2008 PAR.

The Temporary Assistance for Needy Families (TANF) program will report error rates from three States in the FY 2007 PAR. In the FY 2008 PAR HHS will report a statistically valid national error estimate.

2. The first step agencies must take under the Improper Payments Information Act, as you know, is to perform risk assessments on all of their programs and activities to determine which ones are susceptible to "significant improper payments." There are a number of agencies that, for some reason, have still not taken this first step, at least with respect to some of their programs and activities. I'm disappointed that any agency – now three years after the first year of improper payments reporting – would still prove incapable of performing a risk assessment. How far away are we from having all agencies, at the very least, performing improper payments risk assessments on a regular basis?

OMB response:

Under OMB's current definition of programs that are risk susceptible to significant improper payments (i.e., "high risk" programs), Federal agencies have deemed 65% of all Federal outlays ($1.7 trillion out of $2.7 trillion) as subject to IPIA reporting requirements. Therefore, to identify any additional programs that warrant IPIA coverage, we must examine the remaining $1 trillion in outlays. Of the $1 trillion in outlays not currently reported nor on a timeline for reporting by Federal agencies under the IPIA, approximately:

a) $227 billion (23%) is net interest on the public debt, where the IPIA is not applicable;
b) $415 billion (41%) is contract payments, where improper payments are currently being reviewed and reported under the Recovery Audit Act;
c) $227 billion (23%) is civilian compensation (non-DOD) and benefits that have not been identified as high risk by any civilian agency; and,
d) $131 billion (13%) is all other programs, many of which have small outlay totals, and thus are unlikely to meet the IPIA threshold of exceeding $10 million in improper payments annually. This amount also represents programs that have been risk assessed on an annual basis and were not found to be susceptible to improper payments.

We will continue to encourage agencies and the Inspector General community to verify the accuracy and completeness of agency risk assessments and revisit them when necessary. Good risk assessments are critical to meeting the objectives of identifying and eliminating improper payments. The U.S. Department of Agriculture (USDA) re-assessment and reclassification of several programs within the Farm Service Agency as high-risk is a good example of how this process is working.

3. It's clear that agencies use a wide variety of methods to perform the risk assessments required under the Improper Payments Information Act. I'm certain that some methods are more effective than others. What does OMB do to ensure that agencies' risk assessments meet minimum standards?

OMB response:

OMB, as part of the President's Management Agenda (PMA), meets with agencies throughout the year to discuss their ongoing efforts to identify, measure, and reduce improper payments. During these discussions, we assess the actions that agencies are taking to conduct these risk assessments to ensure that they are comprehensive. We also review agency PARs to ensure that agency review and reporting is comprehensive.

As noted in Response #2 above, agencies have deemed $1.7 trillion or 65% of all Federal outlays as risk susceptible to improper payments. In fact, if we consider only those outlays that are directly applicable to the IPIA (i.e., factoring out net interest and payments being tracked under the Recovery Audit Act), Federal agencies have deemed more than 82% of outlays as risk susceptible to improper payments. We believe these results indicate that agency risk assessments are rigorous and effective.

4. At one point in his written testimony, Mr. Williams discusses a change OMB made in the implementing guidance for the Improper Payments Information Act that allows agencies to perform the risk assessments called for in the Act only every three years for those programs and activities that have not been deemed at risk for improper payments. Mr. Williams expresses concern – and it's a concern I share – that this revision is inconsistent with the Act. As enacted, the Improper Payments Information Act requires that agencies perform risk assessments every year for all of their programs and activities.

   Take a minute or two to explain, then, if you could, the rationale behind the change that was made in the implementing guidance. Were the risk assessments proving too costly or too burdensome in some way? How are you making sure that nothing is slipping under the cracks in the years between risk assessments?

OMB response:

In OMB's latest improper payment implementing guidance, *Appendix C to Circular A-123, Management's Responsibility for Internal Control*, we retained - with appropriate fine-tuning -- the annual review that all agencies must conduct, for all of their programs and activities, under the Improper Payments Information Act of 2002 (IPIA). As the IPIA states, the purpose of the annual review is for each agency to identify those programs and activities "that may be susceptible to significant improper payments" (IPIA, Section 2(a)). As explained below, OMB has revised this guidance to agencies based on the experience gained in recent years to increase the effectiveness of the Federal Government improper payments' activities when identifying those programs and activities that may be susceptible to significant improper payments, and in taking action to reduce and eliminate improper payments. Under the revised guidance, an agency must still conduct an annual review of all of its programs and activities, but the nature of the review will differ depending on the relative risk of the program, as informed by prior experience.

The IPIA was enacted on November 26, 2002, and the statute directed OMB to issue implementing guidance within six months. OMB issued the guidance on May 21, 2003, in OMB Memorandum M-03-13. In this initial guidance, OMB required agencies to review annually all the programs and activities that they administer and to identify those that may be susceptible to significant improper payments.

During the first few years of reporting, agencies requested that OMB consider alternative approaches for those measured programs that reduced and reported consecutive years of low erroneous payment levels (i.e., less than $10 million). Agencies felt that once erroneous payments were reduced to below $10 million (which is the agency-reporting threshold under IPIA Section 2(c)), it would be more cost-effective to focus their limited resources on identifying, measuring, and correcting errors in the higher risk programs rather than continuing to perform the same level of risk assessment on all programs, including those with demonstrated low error rates.

OMB considered this agency feedback and agency efforts in assessing, reporting, and reducing improper payments. Based on the agency input and OMB's review of the experience the Executive Branch had gained in implementing the IPIA, OMB reached the conclusion that the initial May 2003 guidance did not provide the optimal approach for how an agency should annually review all of its programs and activities. Instead, OMB concluded that, in limited circumstances, there were more cost-effective ways for an agency to review, the payment risk of a program or activity each year.

Accordingly, OMB updated its guidance on August 10, 2006; the revised guidance is found in Appendix C to Circular A-123. The revised guidance allows agencies to conduct a streamlined review (risk assessment) each year for those programs and activities with a proven track record of reporting low erroneous payment rates, which the revised guidance defines as two consecutive years of reporting improper payments that are less than $10 million. Under this alternative review, an agency -- for these demonstrated low-risk programs and activities -- is required to determine whether any legislative or programmatic changes, significant funding increases, or other changes have occurred that would have a substantial program impact. If no such changes are identified, then the agency in its next annual review will conduct another alternative risk assessment. However, if the alternative review does identify any such changes, then the revised OMB guidance requires the agency, in its next annual review, to conduct a full risk assessment for that program or activity.

OMB believes that this risk-management approach of tailoring the annual review, under which agency resources are targeted to the areas of greatest risk, furthers the primary objectives of the IPIA, which are to identify those programs and activities that "may be susceptible to significant improper payments" and to take effective action to reduce the improper payments in those program and activities.

5. Mr. Williams also expresses some concern in his written testimony about some agencies not using appropriate sampling methods to develop their improper payments estimates. If this is true, I assume the data we get from these agencies

is not truly a realistic picture of the improper payments problems they face. What is your understanding of what the Improper Payments Information Act requires with respect to sampling methods and how does OMB ensure that agencies are doing what they need to do in this area?

OMB response:

OMB believes that Federal agencies can achieve the greatest return on investment for the taxpayer by ensuring that improper payments are eliminated in high risk programs or components of high risk programs rather than diverting resources to track lower risk areas. Federal agencies have expressed concerns that, in some limited cases, obtaining an estimate that meets "traditional" statistical requirements would be cost prohibitive. They have further expressed the position that, in the best interest of the taxpayer, they could expend fewer resources and develop an error measurement that would ultimately provide valid and reliable information that will lead to better practices and improved payment accuracy.

As a result, OMB has allowed a limited number of agencies to deviate from traditional statistical methods. For example, in the Title IV-E Foster Care program improper payment estimates are obtained as part of the normal regulatory review performed rather than an additional sampling process that would require additional time and money.

6. Mr. Williams points out in his written testimony that more than half of the programs reporting improper payments estimates are also reporting serious management and internal control problems that could contribute to waste, fraud, and abuse. In fact, most agencies, according to a report released recently by GAO, have been found to be not in compliance with at least one aspect of the Federal Financial Management Improvement Act – the 1996 legislation laying out the basic financial management system standards for the federal government. I assume that, as long as these problems persist, agencies will have a difficult time actually eliminating the improper payments they're reporting.

   How, then, is OMB helping agencies make progress in addressing the management and internal control weaknesses that lead to improper payments? How do you work with agencies on a one–on-one basis to address any issues that may be specific to them?

   In addition, have you given any thought to requiring that at least some agencies be required to receive an auditor's opinion on their internal controls on a regular basis as the Department of Homeland Security is required to do?

OMB response:

OMB has been working closely with agencies over the past few years to improve agency results in the areas you have identified. Specifically, since 2001:

- Auditor material weaknesses have decreased from 62 to 41
- Agencies found to be in compliance with FFMIA have increased to 12
- Agencies have improved in identifying, measuring, and reducing improper payments.

The President's Management Agenda (PMA) has been an invaluable tool in holding agencies accountable for improving these, as well as other, key financial management requirements. Going forward, our plan is to (1) continue to use the PMA and our quarterly assessment process to hold agencies accountable for achieving key results (e.g., reducing internal control weaknesses, operating systems that comply with financial requirements, reducing improper payments); and (2) continue to work with agencies to identify the root causes of the improper payments and ways to eliminate these problems.

We are also working with the agencies to inventory the causes of payment errors in the 8 programs that make up approximately 90% of all improper payments to focus on the solutions that will bring about the greatest return on investment.

In OMB's revised Circular A-123, Management's Responsibility for Internal Control, OMB may, at its discretion, require the agency to obtain an independent audit opinion of their internal control over financial reporting as part of their financial statement audit if an agency cannot meet the deadlines outlined in the approved corrective action plan. FY 2006 was the first year of reporting under the revised guidance and the process has benefited the agencies in a number of ways including the reporting of previously unidentified internal control weaknesses. At this time, OMB has not identified a need to require any agency to receive a separate auditor's opinion on their internal controls.

7. This subcommittee and the full committee have held a number of hearings over the years on the vast amount of money that has been wasted through improper payments following major disasters such as Hurricane Katrina and the big hurricanes we've seen in Florida. I understand that the Individual and Household Assistance program at FEMA, the Unemployment Insurance program at the Department of Labor, and the Disaster Loan program at the Small Business Administration all saw an increase in improper payments following Katrina. Those increases are reflected, I believe, in the government-wide improper payments estimate OMB submitted at the end of FY 2006.

   What steps have been taken since Katrina to help agencies better prevent disaster-related improper payments next time? The improper payments report OMB issued at the end of January mentions a task force formed by the President this past August that is charged, among other things, with finding a way to prevent fraud, waste, and abuse in federal disaster assistance. What progress has this group made so far?

7

OMB response:

A multi-agency President's Task Force on Disaster Assistance Coordination was established by Executive Order 13441 on August 29, 2006. The Task Force recently completed Phase 1 of their efforts, a collaborative effort among more than fifteen departments and agencies to develop an aggressive but achievable plan to improve the promptness and efficiency with which eligible disaster victims obtain access to and receive Federal disaster assistance. The Disaster Assistance Improvement Plan that this group will provide to the President will outline (1) a coordinated, actionable strategy for implementing a consolidated and unified disaster assistance application, and (2) a system for supporting the application process.

Phase 2, which will be the implementation of the strategy, will address many of the 'lessons learned' from a program integrity perspective. The Executive Order specifically requires that we "strengthen controls designed to prevent improper payments and other forms of fraud, waste, and abuse." We intend to ensure that the solution that is implemented meets this objective.

8. According to information my staff was able to obtain from CRS, 18 agencies across the federal government are subject to the Improper Payments Information Act. Twenty agencies, meanwhile, are required to perform recovery audits due to the fact that they have contracts outstanding of $500 million or more. I understand that this leaves us with five agencies – US-AID, the FCC, OPM, the Railroad Retirement Board, and the Small Business Administration – that are reporting improper payments but are not required to perform recovery audits.

   Also, the recovery audits that are occurring in those agencies that perform them only apply, as I understand it, to overpayments made to contractors.

   I wanted to put this information all into the record to make the point that we're probably not making as much use of recovery auditing as we could be. We have agencies that we know are making significant improper payments that are not required to perform recovery audits – or at least not required to report on their efforts. Then we limit the recovery auditing program only to those overpayments made to contractors.

   Would it be useful to expand the number of agencies required to perform recovery auditing? Would it be useful to subject a broader range of agency payments to these audits too?

OMB response:

All agencies that award $500 million or more in annual contracts are subject to recovery auditing requirements.

Recovery auditing is defined as a review of contract payments (only) by either an internal or external auditor. When external auditors are used, they are contracted with on a contingency fee basis.

The use of recovery auditing for beneficiary or any other non-contract payments does not lend themselves to contingency fee-based contracts in most instances. Even the use of private collection agencies, because they are also paid on a contingency fee basis, may not prove useful when thought of in terms of social security benefit recoupment or other means-test benefits recovery.

Contract review through recovery auditing involves a specific type of improper vendor payment, i.e. an overpayment, duplicate payment, and payment for services not rendered. And most specifically, recovery auditing is not performed on cost type contracts.

Cost-type contracts are subject to other types of monitoring, not recovery auditing. For the most part, the contract close out process is used to reconcile invoices, payments, deliveries, and other types of contract transactions to ensure the government only paid for what it received and at the correct price.

I agree that we may need a revised approach for assessing and reporting improper contract payments. I will be happy to work with you on a proposed solution.

9. I understand that CMS has been running a relatively successful recovery auditing program under Medicare. That program is due to expand from three states today to all 50 states by 2010. And I'm told that the auditing being performed under the program goes beyond contractor payments and involves payments to providers. What can the success of this program and its expansion nationwide tell us about the usefulness of expanding the use of recovery auditing in other programs, especially Medicaid?

OMB response:

The Recovery Auditing Contractor (RAC) program is an important tool in reducing and eliminating improper payments in the Medicare program. It shows what is possible when the government establishes the right incentives and looks for new opportunities to leverage private sector solutions in the improper payments initiative. The payment reviews under this arrangement apply to claims billed by Medicare providers and suppliers. For example, in my discussion with State representatives, they have raised the possibility of having incentives similar to recovery auditing to retain a percentage of improper payments identified. However, this usage has come up against certain challenges wherein Federal regulations require improper payments discovered by a State

to be refunded to the Federal agency within 60 days. This would discourage States from using the recovery auditing model as they would not have the funds to make these repayments before the recoveries had actually been received.

Through the CFO Council, we will explore the CMS successes and identify other areas where we could replicate this approach. I look forward to reporting back to you on what we find and seeing how Congress may be able to help.

Questions For the Record
Hearing: "*Eliminating and Recovering Improper Payments*"
Senator Tom Coburn, M.D.
Senate Subcommittee on Federal Financial Management, Government Information, Federal Services, and International Security

To: Linda Combs, Controller, Office of Management and Budget (OMB)

1. In FY 2006, $184 billion in federal outlays that were previously not reported as risk susceptible have now fallen in the risk susceptible category. Which agencies and programs have fallen into the new risk susceptible reporting? Has any corrective action plans been implemented to reduce improper payments for the new risk susceptible programs?

OMB response:

The chart below identifies the programs that were either added to the high risk outlay total or reported a measurement beginning with the FY 2006 Performance and Accountability Reports (PAR):

(dollars in millions)		
Department of Agriculture		
Direct and Counter-Cyclical Loans		8,546
Farm Disaster Programs		2,365
Non-Insured Assistance Program		109
Department of Defense		
Civilian Pay		62,800
Travel Pay		800
Health & Human Services		
Medicare Managed Care		55,365
Medicare Prescription Drug Benefit		37,426
Department of Homeland Security		
FEMA's Individuals & Households Program	$	3,902
Housing and Urban Development		
Community Development Block Grants*		4,832
Department of State		
International Narcotics & Law Enforcement Program	$	313
International Information Program		28
U.S. Agency for International Development		
Cash Transfers	$	851
Cooperative Agreements, Grants & Contracts		6,846
TOTAL OUTLAYS ADDED TO HIGH RISK AMOUNT IN FY 2006	**$**	**184,183**

*HUD reported three years (2003-2005) of measurements in the FY 2006 PAR that fell below the minimum threshold.

Corrective action plans are in place or are being developed for these programs. Of note, for the U.S. Department of Agriculture (USDA) programs, the majority of payment errors identified were the result of poor file documentation, and not actual payment errors. USDA immediately implemented corrective actions, and anticipates improper payments to decrease significantly when reported in FY 2007.

Additionally, the Medicare Advantage and Prescription Drug Benefit programs are both undergoing extensive risk assessments this year to both validate areas of known risk within the payment process and determine additional sources of risk. The Medicare Advantage and the Prescription Drug Benefit programs will be reporting component error measurements in the FY 2008 PAR.

2. OMB recently revised guidance for implementing the Improper Payments Information Act of 2002 (IPIA) to allow agencies to perform risk assessments every 3 years for those programs not deemed susceptible to significant improper payments. What statute or regulation did OMB cite as the authority to deviate from the annual review required by law?

OMB Response:

In OMB's latest improper payment implementing guidance, *Appendix C to Circular A-123, Management's Responsibility for Internal Control*, we retained - with appropriate fine-tuning -- the annual review that all agencies must conduct, for all of their programs and activities, under the Improper Payments Information Act of 2002 (IPIA). As the IPIA states, the purpose of the annual review is for each agency to identify those programs and activities "that may be susceptible to significant improper payments" (IPIA, Section 2(a)). As explained below, OMB has revised this guidance to agencies based on the experience gained in recent years to increase the effectiveness of the Federal Government improper payments' activities when identifying those programs and activities that may be susceptible to significant improper payments, and in taking action to reduce and eliminate improper payments. Under the revised guidance, an agency must still conduct an annual review of all of its programs and activities, but the nature of the review will differ depending on the relative risk of the program as informed by prior experience.

The IPIA was enacted on November 26, 2002, and the statute directed OMB to issue implementing guidance within six months. OMB issued the guidance on May 21, 2003, in OMB Memorandum M-03-13. In this initial guidance, OMB required agencies to review annually all the programs and activities that they administer and to identify those that may be susceptible to significant improper payments.

During the first few years of reporting, agencies requested that OMB consider alternative approaches for those measured programs that reduced and reported consecutive years of low erroneous payment levels (i.e., less than $10 million). Agencies felt that once erroneous payments were reduced to below $10 million (which is the agency-reporting threshold under IPIA Section 2(c)), it would be more cost-effective to focus their limited resources on

identifying, measuring, and correcting errors in the higher risk programs rather than continuing to perform the same level of risk assessment on all programs, including those with demonstrated low error rates.

OMB considered this agency feedback and agency efforts in assessing, reporting, and reducing improper payments. Based on the agency input and OMB's review of the experience the Executive Branch had gained in implementing the IPIA, OMB reached the conclusion that the initial May 2003 guidance did not provide the optimal approach for how an agency should annually review all of its programs and activities. Instead, OMB concluded that, in limited circumstances, there were more cost-effective ways for an agency to review the payment risk of a program or activity each year.

Accordingly, OMB updated its guidance on August 10, 2006; the revised guidance is found in Appendix C to Circular A-123. The revised guidance allows agencies to conduct each year a streamlined review (risk assessment) for those programs and activities with a proven track record of reporting low erroneous payment rates, which the revised guidance defines as two consecutive years of reporting improper payments that are less than $10 million. Under this alternative review, an agency -- for these demonstrated low-risk programs and activities -- is required to determine whether any legislative or programmatic changes, significant funding increases, or other changes have occurred that would have a substantial program impact. If no such changes are identified, then the agency in its next annual review will conduct another alternative risk assessment. However, if the alternative review does identify any such changes, then the revised OMB guidance requires the agency, in its next annual review, to conduct a full risk assessment for that program or activity.

OMB believes that this risk-management approach of tailoring the annual review, under which agency resources are targeted to the areas of greatest risk, furthers the primary objectives of the IPIA, which are to identify those programs and activities that "may be susceptible to significant improper payments" and to take effective action to reduce the improper payments in those program and activities.

3. During the improper payments hearing, OMB stated that in FY 2008, 100 percent of risk susceptible dollars will report an error measurement. What is the data to support this conclusion? Do you have guarantees in writing or other documentation that would ensure that all agencies and programs will provide an error measurement?

OMB response:

All agencies subject to IPIA report annually in their PARs on programs not yet reporting improper payments and include a timeline to begin reporting an error measurement. In addition, OMB monitors progress for 15 CFO Act agencies (at the highest risk of improper payments) through the President's Management Agenda (PMA) scorecard on Eliminating Improper Payments. This process allows OMB to track progress and specific deliverables on a quarterly basis.

4. Section 831 of the National Defense Authorization Act of 2001 allows agencies to keep their portion from a recovery audit only if it was appropriated and recovered in the same fiscal year. If the appropriation had expired, funds would go to general receipts of the

Treasury and agencies were only allowed to keep funds to cover expenses incurred in conducting the recovery audit programs. Do you believe this provision potentially dissuades agencies from performing recovery audits addressing earlier fiscal years, as perhaps they may not stand to benefit from recapturing funds? Are there any other incentives for agencies to conduct recovery audits? Are there any agencies or programs for which you are not promoting aggressive use of recovery audits?

OMB response:

It is possible that this requirement might dissuade certain agencies from performing recovery audits. In fact, when the law was first enacted and OMB guidance first published (in January 2003 as M-03-7), a portion of the funds recouped by the agencies was to be used for management improvements (i.e., program integrity). These management improvements could have included using some of the recoveries to pay for additional program integrity efforts. However, because legal interpretation precludes the use of funds from closed appropriations, this did not occur.

The primary incentive for conducting recovery audits outside of recovering the funds, is finding out the reasons that these payment errors occurred. If an agency uses a private sector recovery auditing firm, this firm should routinely brief the agency management on how improvements to its internal controls can reduce payment errors.

5. What independent validation process, if any, does OMB perform before granting waivers to agencies for IPIA reporting? What procedures will be taken to independently verify that agencies do not have significant improper payments in the years that they are not required to report?

OMB response:

Please refer to the response to Question #2 above.

6. What role can OMB play to encourage states to assist federal agencies in reporting improper payment estimates for state-administered programs?

OMB response:

Because IPIA is a Federal requirement, there is not always a clear delineation of what role the State is required to play in measuring and reporting payment errors for State-administered programs. OMB has begun a series of dialogues with Federal and State representatives to address this and find potential solutions. Ultimately, we hope to have a better understanding from State stakeholders on the optimal approach a Federal agency can take in: (a) developing, vetting, and implementing a clear and coordinated IPIA implementation plan with the States; and (b) establishing incentives that help ensure effective State participation.

To date, we have identified some best practices in these areas. For example, the Departments of Health and Human Services and USDA have utilized a notice and comment rulemaking process to establish a measurement approach in State-administered programs such as Medicaid, State Children's Health Insurance Program, Child Care Development Fund, and National School

Lunch/Breakfast. In addition, the Department of Labor (DOL) has promoted the use of the National Directory of New Hires (NDNH) by the states to quickly detect and reduce improper UI payments. DOL worked with the Department of Health and Human Services to help States access the NDNH; sponsored a pilot program to encourage implementation; conducted an evaluation of the pilot program; and provided technical assistance and $6.75 million to the states to aid in implementation nationwide.

Another example is the Food Stamp program where USDA employs a combination of rewards and admonitions that facilitate more aggressive approaches to program integrity at the State level. Based on the many years of testing and results, this arrangement has a documented record of positive results.

The issue of State involvement is an area where the Congress, and in particular this Subcommittee, has been and will continue to be very helpful. We appreciate the Senate's interest in including language to newly authorized bills that stresses the importance of program integrity. We also invite your leadership in assisting in the enactment of the other program-specific reforms included in the President's FY 2008 Budget. The President's FY 2008 Budget contains a series of reforms that are needed to ensure greater program integrity and payment accuracy. These proposals include:

- UI Overpayment Recoveries – provides tools and resources as financial incentives to both prevent and more aggressively pursue benefit overpayments and more delinquent employer taxies. If enacted, the proposal is projected to save $3.6 billion over ten years.
- EITC and Child Tax Credit – clarifies tax code definitions to reduce filing complexity. If enacted, the proposals would save $487 million in the first year and $6.7 billion over ten years.
- OASDI – provides SSA with the tools to conduct improved enforcement of certain statutory provisions and to eliminate the more complicated formulas currently used when calculating certain benefit offsets. If enacted, these two proposals would save $4 million in the first year and $3.6 billion over ten years.
- Medicare – provides CMS with resources to identify and reduce improper payments in the Medicare prescription drug benefit and Medicare Advantage programs. If enacted, this discretionary cap adjustment proposal would save $330 million in the first year.

Responses to Questions from McCoy Williams

United States Government Accountability Office
Washington, DC 20548

May 30, 2007

The Honorable Thomas R. Carper
Chairman, Subcommittee on Federal Financial Management, Government Information, Federal Services, and International Security
Committee on Homeland Security and Governmental Affairs
United States Senate

Subject: *Improper Payments: Responses to Posthearing Questions Related to Agencies' Progress in Addressing Improper Payment and Recovery Auditing Requirements*

Dear Mr. Chairman:

On March 29, 2007, we testified[1] before your subcommittee at a hearing entitled, "Eliminating and Recovering Improper Payments." At the hearing, we discussed federal agencies' progress in addressing key requirements of the Improper Payments Information Act of 2002 (IPIA)[2] and Section 831 of the National Defense Authorization Act for Fiscal Year 2002, commonly known as the Recovery Auditing Act.[3] Our review and testimony focused on (1) trends in agencies' reporting under IPIA from fiscal years 2004 through 2006, (2) challenges in reporting improper payment information and improving internal control, and (3) agencies' reporting of recovery auditing efforts.

This letter responds to your April 18, 2007, request to provide answers to follow-up questions relating to our March 29, 2007, testimony. The responses are based on work associated with previously issued GAO products (see Related GAO Products at the end of this report) and data reported in agencies' performance and accountability reports (PAR). Your questions, along with our responses, follow.

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[1]GAO, *Improper Payments: Agencies' Efforts to Address Improper Payment and Recovery Auditing Requirements Continue*, GAO-07-635T (Washington, D.C.: Mar. 29, 2007).

[2]Pub. L. No. 107-300, 116 Stat. 2350 (Nov. 26, 2002).

[3]National Defense Authorization Act for Fiscal Year 2002, Pub. L. No. 107-107, div. A, title VIII, § 831, 115 Stat. 1012, 1186 (Dec. 28, 2001) (codified at 31 U.S.C. §§ 3561-3567).

1. *In your written testimony, you state that over half of the programs reporting improper payment estimates also had reported management challenges, including internal control issues that may have a direct impact on improper payment issues. Could you provide us with an example of how internal control issues increase the risk that agencies will make improper payments? What guidelines are available or where can agencies go to learn how to manage improper payments and implement strong internal controls?*

Internal control is a major part of managing an organization. It comprises the plans, methods, and procedures used to meet missions, goals, and objectives that support performance-based management. Internal control serves as the first line of defense in safeguarding assets and preventing and detecting errors and fraud. Strong systems of internal control provide reasonable assurance that programs are operating as intended and are achieving expected outcomes. Generally, improper payments result from a lack of or an inadequate system of internal controls, but some result from program design issues.

For fiscal year 2006, agency auditors reported numerous internal control weaknesses that could increase the risk of improper payments. For example, at the National Science Foundation (NSF), agency auditors identified two reportable conditions during their examination of the effectiveness of NSF's internal control over financial reporting. These reportable conditions related to oversight of grants and cooperative agreements and monitoring of contracts. For the first reportable condition, auditors found that NSF's monitoring process to ensure that expenditures were allowable, allocable, and reasonable under the terms of the grant award or agreement lacked oversight reviews for 286, or about 84 percent, of high-risk awards,[4] totaling approximately $2.7 billion for fiscal year 2006. As such, NSF could not ensure that federal funds were properly spent on allowable costs benefiting NSF's research activities. The auditors recommended, among other things, that NSF management expand the coverage of review for its high-risk awards.

Regarding the second reportable condition, the auditors reported that NSF did not have a comprehensive, risk-based system, including detailed policies and procedures, in place to oversee and monitor its contract awards totaling about $550 million for fiscal year 2006. This lack of appropriate contract oversight was evident during the auditor's review of NSF's largest contractor responsible for acquiring, maintaining, and performing a physical inventory of NSF's property, plant, and equipment (PP&E). The auditors reported that NSF did not perform any independent verification of the PP&E amounts reported by the contractor, and did not maintain copies of source documentation supporting the amounts included in the financial statements. The auditors recommended that NSF develop a more comprehensive, risk-based, internal management monitoring program to ensure that contractors use NSF funds

[4]NSF procedures require that awards are assessed as high, medium, or low risk based on objective factors. The procedures also require that institutions with high-risk awards receive a more detailed level of review such as site visits on a cyclical basis every 4 or 5 years.

consistent with the objectives of the contract, and that funds are protected from waste, fraud, or mismanagement.

There are two key resources available to agencies for implementing strong internal control and managing improper payments. First, our Standards for Internal Control in the Federal Government[5] provides an overall framework for entities to establish control for all aspects of their operations and a basis against which entities' control structures can be evaluated. Specifically, internal control provides reasonable assurance that an organization's objectives are achieved through (1) effective and efficient operations, (2) reliable financial reporting, and (3) compliance with laws and regulations.

Second, our executive guide[6] on strategies to manage improper payments focuses on internal control standards as they relate to reducing improper payments. The five components of internal control—control environment, risk assessment, control activities, information and communication, and monitoring—are defined in the executive guide in relation to improper payments as follows:

- Control environment—creating a culture of accountability by establishing a positive and supportive attitude toward improvement and the achievement of established program outcomes.
- Risk assessment—analyzing program operations to determine if risks exist and the nature and extent of the risks identified.
- Control activities—taking actions to address identified risk areas and help ensure that management's decisions and plans are carried out and program objectives are met.
- Information and communication—using and sharing relevant, reliable, and timely financial and nonfinancial information in managing activities related to improper payments.
- Monitoring—tracking improvement initiatives over time, and identifying additional actions needed to further improve program efficiency and effectiveness.

2. *In your written testimony, you note that the Improper Payments Information Act does not include a requirement for auditors to assess agencies' compliance with the Act. Would there be any value in making this a requirement of agency auditors?*

As we stated in our testimony, IPIA does not include a separate reporting requirement for auditors to assess agencies' compliance with the act. However, where agencies' auditors have elected to test specific compliance with IPIA, their

[5]GAO, *Standards for Internal Control in the Federal Government,* GAO/AIMD-00-21.3.1 (Washington, D.C.: November 1999).

[6]GAO, *Strategies to Manage Improper Payments: Learning From Public and Private Sector Organizations,* GAO-02-69G (Washington, D.C.: October 2001).

assessments have provided a valuable independent validation of agencies' efforts to implement the act. For example, we found that for the selected agencies we reviewed, some agencies' auditors reported problems relating to agencies' risk assessments, the definition of programs for IPIA purposes, sampling methodologies, lack of reporting for all risk-susceptible programs, and supporting documentation.

Identification of any deficiencies in implementing IPIA helps agencies determine if risks exist, what those risks are, and the potential or actual effect of those risks on program operations. Independent assessments of these estimates would also enhance an agency's ability to identify sound performance measures, monitor progress against those measures, and help establish performance and results expectations. Finally, independent assessments of agencies' improper payments estimates would enable agencies and others with oversight and monitoring responsibilities to measure progress over time and determine whether further action is needed to minimize future improper payments.

3. *You have stated that certain methodologies used to estimate improper payments did not result in accurate estimates. Could you please explain what this means? What needs to be done to help ensure that amounts reported by agencies are accurate?*

As we reported in our testimony, the $42 billion total improper payment estimate reported by agencies for fiscal year 2006 may not reflect the full magnitude of total improper payments. We noted that agencies employed different sampling methodologies to estimate improper payments, including statistical sampling, nonstatistical sampling, or a combination of the two.[7] The advantage of using statistical sampling is that sample results can be generalized to the entire population from which the sample was taken. Thus, a properly designed statistical sampling methodology provides a more accurate representation of the extent to which improper payments exist within a given program or activity. On the other hand, results of a nongeneralizable, or judgmental, sample may not be extrapolated beyond the sample transactions tested. For fiscal year 2006, we found that seven agencies did not use statistical sampling to estimate improper payments for nine programs totaling about $202 million, with program outlays exceeding $88 billion. Because the results of nongeneralizable sample selections cannot be extrapolated beyond the sampled items, the improper payment estimate for these programs would likely have been much greater had statistically valid methods been used.

Agency statisticians should be engaged throughout the sampling process, from design of the sampling methodology to evaluation of the results. This is consistent with OMB's revised IPIA implementation guidance,[8] which provides general steps that

[7]The Office of Management and Budget's (OMB) implementing guidance requires that agencies generally use a statistical sample to estimate improper payments. Agencies may also use an alternative sampling approach provided they obtain OMB approval prior to implementation.

[8]OMB Memorandum M-06-23, "Issuance of Appendix C to OMB Circular No. A-123" (Aug. 10, 2006).

agencies should follow to obtain a statistically valid improper payment estimate. Specifically, OMB guidance emphasizes that most agencies will need to consult with a statistician to design an appropriate sample that considers payment universes with divergent dollar amounts, types of payments, or both, and samples that involve multiple stages of selection or stratification. Further, additional oversight of agencies' sampling methodologies could help ensure that amounts reported by agencies are accurate and, in turn, enable agencies to measure progress over time and determine whether further action is needed to minimize future improper payments.

4. *As you know, the Improper Payments Information Act requires agencies, with respect to any program or activity with estimated improper payments of more than $10 million, file a report along with their improper payments estimates that includes at least four things:*

   a. *a discussion of the causes of improper payments identified, actions taken to correct those causes, and results of the actions taken to address those causes;*
   b. *a statement of whether the agency has the information systems and other infrastructure it needs in order to reduce improper payments to minimal cost-effective levels;*
   c. *if the agency does not have such systems and infrastructure, a description of the resources the agency has requested in its budget submission to obtain the necessary information systems and infrastructure; and*
   d. *a description of the steps the agency has taken to ensure that agency managers (including the agency head) are held accountable for reducing improper payments.*

   Do you think these are the right things we should be asking agencies to report on? What, if anything, would you add or take away from the reporting requirements under the Act?

The current IPIA reporting requirements increase the visibility over the governmentwide improper payments problem and transparency of agencies' efforts to address improper payments in their programs. Improper payments are a significant problem in the federal government and information on actions taken, and the results of those actions, is a critical element in the overall process of reducing improper payments. Prior to implementation of IPIA, we issued several reports[9] on governmentwide improper payments. Our reviews showed that the type and amount of improper payment information reported were inconsistent across federal agencies, with few agencies publicly reporting the amounts of their improper payments or other information such as:

- barriers to identifying or reducing improper payments,
- targets and goals set for improvement, and
- progress in identifying, minimizing, and recovering improper payments.

[9]See the Related GAO Products list at the end of this report.

The act's reporting requirements coincide with our recommendations made prior to IPIA implementation that agencies take actions to estimate, reduce, and publicly report improper payments. Our prior recommendations and OMB's IPIA implementing guidance also provided that agencies (1) assign responsibility to a senior official for establishing policies and procedures for assessing agency and program risks of improper payments, and (2) establish improper payment goals or targets and measure performance against those goals to determine progress made and areas needing additional improvements.

However, two additional areas that could provide enhanced transparency in agencies' improper payment reporting include (1) a reporting requirement concerning improper payment estimates by type of error and (2) information on agencies' efforts to recover improper payments in their risk-susceptible programs and activities. Currently, we found that only a few agencies report improper payment estimates by type of error or provide information on the recovery of improper payments made to program beneficiaries or grantees. Existing guidance to report recovery auditing information solely focuses on contract overpayments made to vendors in accordance with the Recovery Auditing Act. Agencies should consider performing cost-benefit analyses of a recovery auditing program before implementation to provide a baseline to help ensure that the cost of those activities to the organization is not greater than the potential benefit and then measure results periodically.

Requiring the reporting of improper payment estimates by type of error would assist in the identification of the source and progress made to reduce those errors. For example, the Department of Housing and Urban Development (HUD) reports three types of error rates for its public housing/rental assistance programs—errors due to administrator subsidy determinations, tenant underreporting of income, and gross billing errors. With this level of detail, HUD has the information available to readily measure its progress in reducing improper payments related to these types of errors, and thus is in a better position to target corrective actions. Other agencies categorized errors as to cause, but did not report an estimate for each category. For example, the Department of Transportation categorized its errors into various types—such as data entry errors, unallowable charges, and materials received not in accordance with contract terms—but did not report an estimate for each category. We also realize that agencies may use other reporting methods to provide a detailed breakout of their improper payment estimates. Although not included as part of its PAR reporting, the Department of Health and Human Services (HHS) reports improper payment estimates for its Medicare Fee-for-Service program by type of error, individual contractor, and geographical region and makes this information publicly available on its Web site.[10]

Another area that agencies could be required to report on as part of their IPIA reporting includes the results of their efforts to recover improper payments in their risk-susceptible programs and activities. Generally, agencies' recovery auditing

[10]See the Comprehensive Error Rate Testing (CERT) reports at www.cms.hhs.gov/CERT/.

efforts target contract overpayments as required by the Recovery Auditing Act. These requirements are only applicable for agencies that enter into contracts with a total value in excess of $500 million in a given fiscal year. Agencies currently have no requirement under IPIA to report on any recovery efforts for improper payments made to program beneficiaries or grantees. Reporting this type of information would provide additional accountability mechanisms for agencies to recover taxpayer funds and provide Congress additional insight on challenges agencies face in recovering improperly paid funds.

5. *As you know, there has been significant debate over OMB's definition of the phrase "significant improper payments." How this phrase is defined is important because it determines which programs and activities—all of which likely have some level of improper payment—actually report the payment errors they make. Do you think there is some way to define "significant improper payments" that gives us more transparency without imposing an unacceptable administrative burden on OMB and the agencies?*

We reported[11] in November 2006 that OMB's implementation of IPIA's general criteria to identify risk-susceptible programs limits the disclosure and transparency of governmentwide improper payments. This limitation does not further the objectives of IPIA, as programs that do not meet OMB's criteria of exceeding $10 million and 2.5 percent of program payments are excluded from agencies' improper payment reporting. For example, one agency identified three programs with estimated improper payments exceeding $10 million, but because the estimates did not exceed 2.5 percent of program outlays, they were not included in the governmentwide improper payments total. In that report, we recommended that Congress consider amending existing IPIA provisions to define specific criteria, such as a minimum dollar threshold, agencies should use to identify which programs and activities are susceptible to significant improper payments.

In response[12] to posthearing questions related to our December 5, 2006, testimony,[13] we included suggested language for amending IPIA for better transparency and disclosure of improper payments reporting. The suggested language would amend IPIA to define, for purposes of identifying what programs or activities are susceptible to improper payments, the term "significant" to mean "annual improper payments under a program or activity that exceed $10 million." This amendment would be consistent with the threshold currently identified in IPIA that requires additional reporting for those agencies with estimates of more than $10 million.

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[11]GAO, *Improper Payments: Agencies' Fiscal Year 2005 Reporting under the Improper Payments Information Act Remains Incomplete*, GAO-07-92 (Washington, D.C.: Nov. 14, 2006).

[12]GAO, *Improper Payments: Posthearing Responses on a December 5, 2006, Hearing to Assess the Improper Payments Information Act of 2002*, GAO-07-533R (Washington, D.C.: Feb. 27, 2007).

[13]GAO, *Improper Payments: Incomplete Reporting under the Improper Payments Information Act Masks the Extent of the Problem*, GAO-07-254T (Washington, D.C.: Dec. 5, 2006).

6. *As you know, current recovery audit requirements only apply to overpayments made to agencies' contractors. I suspect that there are a number of other areas, however, that would benefit from this kind of audit work. Do you think it would be appropriate and useful for Congress to require that a broader range of agency payments be subjected to recovery auditing?*

Subjecting a broader range of agency payments to recovery auditing or collection procedures may provide useful information to Congress as part of its decision-making and oversight responsibilities. Currently, IPIA does not include a reporting requirement on agencies' efforts to recover improper payments made to program beneficiaries or grantees. However, existing legislation, such as the Debt Collection Improvement Act of 1996 (DCIA)[14] and program-specific legislation, provides mechanisms that agencies can utilize to recoup improper payments.

For example, the Social Security Administration (SSA) reported in its fiscal year 2006 PAR that it had collected $2.3 billion in program debt. SSA's internal collection techniques include benefit withholding and billing to recipients with subsequent follow-up. In addition, SSA uses external collection techniques authorized by DCIA including the Treasury Offset Program,[15] credit bureau reporting, and administrative wage garnishment[16] to recoup improper payments. DCIA requires that agencies refer eligible debts that an agency has been unable to collect and remain delinquent more than 180 days to the Department of the Treasury for payment offset or for cross-servicing. Cross-servicing involves such actions as locating debtors, issuing demand letters, and referring debts to private collection agencies.

In another example, HHS under section 306 of the Medicare Prescription Drug, Improvement, and Modernization Act of 2003,[17] was given authority to conduct a project to demonstrate the use of recovery audit contractors in identifying improper payments and recouping overpayments for Medicare in the Medicare Fee-for-Service program. HHS reported in its fiscal year 2006 PAR that it initiated this 3-year project in March 2005 in the three states with the highest Medicare utilization rates. HHS reported that it provided the recovery audit contractors about $167 billion of claims submitted between fiscal years 2002 and 2005 for review. Of the $167 billion, HHS reported that it is working on recovering $224 million in claims payments determined to be improper.

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[14]Pub. L. No. 104-134, 110 Stat. 1321, 1321-358 (April 26, 1996).

[15]This program includes the offset of certain benefit payments, vendor payments, and tax refunds.

[16]This is a process in which a federal agency orders an employer to withhold amounts each payday from an employee who owes a debt to the agency. In turn, the employer pays the withheld amount to the agency.

[17]Pub. L. No. 108-173, 117 Stat. 2066, 2256 (Dec. 8, 2003).

As we previously reported and testified before this subcommittee,[18] recovery auditing is a method that agencies can use to recoup detected improper payments. While we support the use of recovery auditing and annual reporting of this information, effective internal control serves as the first line of defense in safeguarding assets and preventing and detecting errors and fraud. Given the large volume and complexity of federal payments and historically low recovery rates for certain programs, it is much more efficient to pay bills and provide benefits properly in the first place. Aside from minimizing overpayments, preventing improper payments increases public confidence in the administration of benefit programs and avoids the difficulties associated with the "pay and chase" aspects of recovering improper payments. Without strong preventive controls, agencies' internal control activities over disbursements will not be effective in reducing the risk of improper payments.

7. *You note in your written testimony that 18 agencies have reported on their recovery audit efforts and have used a variety of methods to do that auditing work. Some conducted in-house recovery audits, others contracted out their recovery audit services, and still others used both in-house and private sector auditors. Do you have any sense of whether contractor or in-house recovery is more effective?*

Beginning with fiscal year 2004, OMB required that applicable agencies publicly report on their recovery auditing efforts as part of the PAR reporting of improper payment information. As we reported in our March 2007 testimony, the number of agencies reporting recovery auditing information, including the dollar amounts identified for recovery and actually recovered, had increased from fiscal year 2004 to 2006. We also reported that agencies conducted in-house recovery audits, contracted out their recovery audit services, or used a combination of the two methods. However, we have not analyzed the relative effectiveness of the different types of methods agencies used to recover overpayments.

[18]GAO-07-92 and GAO-07-635T.

Questions For the Record

Hearing: *"Eliminating and Recovering Improper Payments"*

Senator Tom Coburn, M.D.

Senate Subcommittee on Federal Financial Management, Government Information, Federal Services, and International Security

To: John Cox, Chief Financial Officer, Department of Housing and Urban Development (HUD);
Jim Martin, Deputy Chief Financial Officer, Department of Housing and Urban Development (HUD)

1. HUD's Community Development Block Grant (CDBG) program, with spending totaling $5.4 billion, reported a 0.1 percent error rate. On June 29, 2006 this subcommittee conducted a hearing specifically highlighting the lack of transparency for spending in the program – particularly after the money is handed to the communities. Given that communities are not generally able to consistently and reliably report how all their CDBG funds are spent, how can you be sure of any definite error rate, and especially so low a rate?

Prior to enactment of the Improper Payments Information Act (IPIA), the Office of Management and Budget requested agency input on improper payments in select programs, including the CDBG Entitlement and State/Small Cities Programs, through Section 57 of OMB Circular No. A-11. HUD's original Section 57 assessment and initial annual risk assessments under the IPIA found the CDBG program to be at low risk of improper payments, not warranting reporting. However, OMB subsequently revised its guidance to clarify that agencies should report on the former Section 57 programs until they can document a minimum of two consecutive years of improper payments that are less than $10 million annually, as the basis for a request for OMB relief from annual reporting. In compliance with this requirement, HUD developed and applied a systematic method to document that the CDBG program has not had a significant improper payment level for the past three consecutive years.

HUD reviewed improper payment activity in the CDBG program for the period FY 2003-FY 2005, as identified through risk-based monitoring efforts under the Grants Management Process (GMP). Grantees were ranked according to Departmental risk criteria and selected for on-site monitoring based on their ranking. Field offices performed on-site monitoring of higher risk grantees and identified improper payments as part of their reviews. Improper payments data was compiled by the field offices and entered into the GMP system. CPD headquarters staff analyzed the data and extrapolated to the annual funds disbursed for fiscal years 2003 to 2005 to determine the total estimated annual CDBG improper payment level for the three-year period, as follows:

CDBG Improper Payments Based on GMP System for FY 2003 through FY 2005

Fiscal Year	Total CDBG Dollar Amount Monitored	Total CDBG Program Dollars Disbursed	Improper Payments Detected on Monitoring	Improper Payments Extrapolated to the Population
2003	$2,075,218,153	$4,923,710,000	$2,025,487	$4,805,717
2004	$1,906,042,598	$4,869,633,000	$3,116,223	$7,961,450
2005	$1,780,311,308	$4,832,286,000	$1,616,704	$4,388,208

HUD considers the extrapolated annual amount of improper payments to be on the high side since it is based on higher risk CDBG recipients. Those higher risk grantees would be expected to have a higher amount of improper payments than grantees of lesser risk. The extrapolation procedures described above do not take this into account when projecting the total to the entire grantee population including low risk grantees. Had the monitoring efforts included an equal number of high, moderate and low risk grantees as would be expected in a statistical sample, HUD expects the amount of improper payments discovered would be less. Despite this, the estimated amount of improper payments remained below the reporting threshold. CDBG funds are awarded to and administered by units of state and local government that generally have adequate financial management systems and practices that reduce the risk of improper payments.

2. In 2005, The Public Housing Capital Fund made $133.5 million in improper payments with an error rate of 5.1 percent, thus meeting both of the IPIA thresholds that mandates a corrective plan and annual reporting. Yet, in 2006 HUD did not report an estimate or a corrective action plan for the Public Housing Capital Fund as dictated by the Improper Payments Information Act because the Department claimed the Fund is no longer susceptible to improper payments. Please describe in detail the corrective actions implemented in the Public Housing Capital Fund that led to the significant decrease in error rate and dollar amount.

HUD completed the statistical sample testing for the Public Housing Capital Fund Program and estimated that the total gross improper payments for the program in FY 2003 were $133.5 million or 5.1 percent of the $2.6 billion in total payments covered by the sample testing. The gross improper payment estimate includes $118.1 million in estimated overpayments and $15.4 million in estimated underpayments. The total estimated gross improper payments amount consists of the following two categories of substantive causes of error and two categories of error associated with incomplete sample testing due to time and cost constraints on the testing:

Estimates of Improper Payments Based on Substantive Causes

- $13.9 million estimated for contract retainage amounts that are paid in advance of the need for payment in violation of HUD's cash management policies, and
- $11,000 in estimated other payments without proper supporting documentation.

Estimates of Improper Payments Due to Incomplete Sample Testing

- $96.8 million estimated for payments associated with large, complex monthly funding drawdown/reconciliation processes for which sample testing was not yet completed after allowing six months to provide adequate supporting documentation, and
- $22.7 million estimated for other payments for which sample testing was not completed after HUD's decision to end sample testing after six months because the general level and causes of errors was believed to be known based on completed testing.

Almost all of the improper payment issues discovered during HUD's sample testing related to the largest Capital Fund grant recipient, the New York City Housing Authority. Thus the Department concluded that a program-wide problem did not exist. The New York City Housing Authority accounted for 16 of the 211 sampled HUD payment transactions and those 16 large transactions totaled $160.7 million, or 83 percent, of the total sampled dollars of $192.8 million.

In response to HUD's review, the New York City Housing Authority revised its cash management policies to comply with HUD's policies. The Housing Authority also implemented a new financial system in FY 2004 that they claimed eliminated the complex monthly funding drawdown/reconciliation process that hindered the full and timely completion of HUD's sample testing. Based on the results of the testing that was completed, HUD believes that adequate supporting documentation for both categories of incomplete testing items would likely have been provided if additional time and cost had been spent to complete the review. However, the cost of additional HUD resources to pursue and test those documents outweighed the potential benefit that would be gained, given that the causes and corresponding corrective actions for the limited types of errors detected were already known.

Under the circumstances, HUD followed up with a review of the New York City Housing Authority's FY 2004-2005 payment transactions under their new practices and financial system, in lieu of another review of payments in the entire Capital Fund Program. The follow-up review conducted in September 2005 verified that corrective actions were taken by the Housing Authority to eliminate the causes of the improper payments found in FY 2003.

3. **In September of 2005, you appeared before this subcommittee to testify on Housing-related programs for the poor. One of the primary concerns we had was related to the rent determination process, which was the source of a large amount of improper payments (in FY 2004 Section 8 Project Based had overpayments totaling $348 million with an error rate of 4.5 percent). You testified that you recommended to HUD that the "agency include an assessment of compliance with rent subsidy determination policies" in order to "use it to help corrective actions where they are needed. Since that hearing, what is the progress on that assessment of compliance? How much has the improper payment rate in the Section 8 program been reduced since then?**

HUD continues to conduct its annual study of "Quality Control for Rental Assistance Subsidy Determinations" as a basis for determining the nature and extent of errors due to non-compliance with HUD requirements. Errors associated with the rent determination process are due to:

1) Program administrator error – the program administrator's failure to properly apply over 40 income exclusions and deductions and correctly determine income, rent, and subsidy levels; and
2) Tenant income reporting error – the tenant beneficiary's failure to properly disclose all income sources and amounts upon which subsidies are determined.

From 2000 through 2005, HUD substantially reduced the gross improper payments for these 2 categories of error from $3.22 billion to $1.28 billion. The following paragraphs provide additional data on each of these 2 categories of error.

Program Administrator Error - HUD's update of the measure of program administrator rent and subsidy determination errors in FY 2005 found a 58.7 percent reduction in this improper payment component since FY 2000, as shown in the following chart:

Rental Assistance Programs	FY 2005 Full Year Estimates of Error in Program Administrator Income, Rent & Subsidy Determinations				FY 2000 Estimate of Error*	Percent Reduction in Gross Improper Payments
	Assistance Overpayments $1,000's	Assistance Underpayments $1,000's	Net Improper Payments $1,000's	Gross Improper Payments $1,000's	Gross Improper Payments $1,000's	
Public Housing	$116,952	$103,512	$13,440	$220,464	$602,557	*63.4%
Tenant-based Vouchers & Mod Rehab	$309,600	$146,640	$162,960	$456,240	$1,096,535	58.4%
Total PHA Administered	$426,552	$250,152	$176,400	$676,704	$1,699,092	60.2%
Multifamily Project-based Assistance	$157,836	$90,744	$67,092	$248,580	$539,160	53.9%
Total 2005*	$584,388 (+/-$117,130)	$340,844 (+/-$104,134)	$243,544 (+/-$148,872)	$925,232 (+/-$164,206)	$2,238,252 (+/- $271,000)	58.7%

* - Estimates are provided at a 95 percent confidence level.

The significant reduction in this error component is attributed to the continuation of HUD's efforts to work with its housing industry partners at PHAs and multifamily housing projects through enhanced program guidance, training, oversight, and enforcement.

The Office of Public and Indian Housing initiated on-site Rental Integrity Monitoring reviews which focused on the 490 largest PHAs that receive 80 percent of HUD's public housing and tenant-based voucher program funds. Technical assistance was provided to PHAs with the most significant program deficiencies and follow-up on Rental Integrity Monitoring reviews was conducted to assess program improvements and the need for corrective and enforcement action.

The Office of Multifamily Housing has placed nearly all Section 8 Program project-based assistance under Performance-Based Contract Administrators who review 100 percent of monthly vouchers and perform annual on-site management and occupancy reviews at all projects. Twenty percent of the remaining project-based assistance contracts still administered by HUD staff or traditional contract administrators also received on-site monitoring reviews in FY 2005.

Tenant income reporting errors in FY 2005 were $359 million, a decline of 63 percent from the FY 2000 baseline of $978 million. These tenant income reporting errors continue to be addressed through an improved methodology for reviewing income discrepancies identified through computer matching. HUD entered into a Computer Matching Agreement with the Department of Health and Human Services to obtain current wage and unemployment data, and incorporate that information into HUD's Enterprise Income Verification (EIV) system, providing a more timely and cost-effective means of verifying tenant income upon which subsidies are based. This was implemented for the Public Housing and Voucher Programs, and HUD anticipates continued positive decreases in the level of improper payments associated with tenant income reporting errors for the Public Housing programs.

HUD also is moving forward with plans to implement the new computer matching authority for its Multifamily Project-Based Assistance Programs. HUD is hopeful full implementation will be achieved by late FY 2007 or the beginning of FY 2008, and anticipates reductions in the level of improper payments in its Multifamily Housing portfolio.

4. Another concern we had during the last hearing was rent determination simplification. What simplification initiatives have been launched by the Department since that time?

Elimination of over 40 existing income exclusions and deductions, in favor of a flat housing subsidy or allowance, would clearly reduce opportunities for improper payments, however, such a change would have varying impacts on current program benefit levels to individual households, with many winners and losers under such a change scenario at the same program funding level.

Congressman Frank has proposed the Section 8 Voucher Reform Act of 2007, which seeks to:

- Allow PHA's to use prior year's actual earned income, versus projected future income, for determining the level of rental assistance, and delay rent increases due to increased income for at least a year;
- Provide new definitions of income, income inclusions and exclusions;
- Prohibit rental assistance for individuals that have a present ownership interest in, and a legal right to reside in real property that is suitable for occupancy as a residence;
- Prohibit rental assistance for families (at time of initial or periodic recertification) who are not low-income families and authorize PHA to delay eviction from unit for period not to exceed 6 months (this is close to implementing term limits for rental assistance – once a family is no longer a low-income family, the family needs to move to an unassisted unit so others can benefit from the program).

This legislative proposal would promote income integrity and result in the reduction of some types of subsidy payment errors. Since actual past income would be used, participants may be inclined to be more forthcoming with income information – since amounts are more verifiable and increases in income would not result in an increase in rent for at least a year. Numerous current income exclusions would be removed, resulting in fewer opportunities for program administrator errors.

HUD is currently considering a legislative proposal of its own – the Rental Assistance Simplification Act (RASA) – that would seek to give Public Housing Agencies greater flexibility to set simpler rent structures that would enable them to better meet local housing needs within fixed assistance funding levels. HUD's previous legislative proposal, the State and Local Housing Flexibility Act (SLHFA), which also sought to provide program simplification and flexibility, was not enacted.

Question#:	1
Topic:	IPIA
Hearing:	Eliminating and Recovering Improper Payments
Primary:	The Honorable Tom A. Coburn M.D.
Committee:	HOMELAND SECURITY (SENATE)

Responses to Questions from David M. Norquest

Question: Based upon the Department's Performance and Accountability Report and the independent auditor's assessment, the following programs are out of compliance with the IPIA: Customs and Border Protection (CBP); Office of Grants and Training (GT); Federal Air Marshals (FAM); Federal Emergency Management Agency (FEMA); Transportation Security Administration (TSA); Immigration and Customs Enforcement (ICE). When will the six programs be in compliance and report improper payments?

Answer: The Department will work with Customs and Border Protection (CBP); Office of Grants and Training (G&T); Federal Air Marshals (FAM); Federal Emergency Management Agency (FEMA); Transportation Security Administration (TSA); and Immigration and Customs Enforcement (ICE) to complete required testing and reporting of improper payments in FY 2007. FEMA and G&T are currently undergoing profound organizational change to implement the Post-Katrina Emergency Management Reform Act (e.g., new responsibilities, reorganization, expansion of accounting services, and changes in management). As a result, FEMA and G&T face significant challenges and risks.

To establish a foundation and sustainable Improper Payments Information Act (IPIA) Program, DHS will perform the following activities during FY 2007 and FY 2008:

- Strengthen monitoring and oversight of DHS Component IPIA efforts.
- Work with DHS Components to accurately define all Component programs based on related activities and goals.
- Conduct IPIA training for Component personnel for program identification, risk assessment, and sample testing.
- Conduct a detailed qualitative and quantitative risk assessment for all Component programs to identify potential high risk programs.
- Sample payments for programs identified as possibly at high risk.
- Develop corrective action plans for all high risk programs.
- Report progress and results in the FY 2007 and FY 2008 PARs.

Question#:	2
Topic:	Recovery
Hearing:	Eliminating and Recovering Improper Payments
Primary:	The Honorable Tom A. Coburn M.D.
Committee:	HOMELAND SECURITY (SENATE)

Question: In FY 2006, over $502 million was identified for recovery; however, only $6 million was actually recovered. Why were so few funds recovered, and why didn't DHS include recovery audit amounts in its FY 2006 PAR?

Answer: DHS, through Administrator Paulison and FEMA's Chief Financial Officer, has been diligently working to improve recovery efforts and bolster corrective action efforts for improper payments. Extensive sample payment tests were completed late in FY 2006 to determine internal control improvements after the 2005 hurricane season and report a statistically valid estimated error amount and rate. This test work focused on improving key internal controls over payments with the goal of minimizing future improper payments.

Recovery of improper vendor payments rests with FEMA's Acquisition Office, Chief Financial Office, and Office of Chief Council. During the normal course of reviewing invoices submitted for processing, staff at the Disaster Finance Center work closely with FEMA's Acquisition Office staff to recover any identified overpayments to vendors. The catastrophic circumstances encountered during the 2005 hurricane season have made it difficult to establish and recover funds based on unique processes and circumstances.

Erroneous payments to individual households are identified and recouped through the process established in the Debt Collection Improvement Act (DCIA). That process includes: identifying the overpayment; sending a letter to the debtor; providing a timeline for the payment or appeal; and possibly providing notification of potential legal remedies for payment collection with additional timelines for appeals. FEMA has sent nearly 134,000 letters to individuals who have been incorrectly paid under the Individual and Household Payments (IHP) program. We have identified approximately $436 million for recoupment and have collected $11.3 million to date. The debt collection process can take many months to complete, however, because of appeals and the time it takes to establish an actual schedule for recouping the funds. The long timeline in the debt collection process accounts for the relatively low percentage of dollars that have been recouped from the overpayments that have been identified. As the timeline for appeals expires and the debt collection process moves forward, we anticipate that more collections will occur. DHS and FEMA are committed to ensuring the timely recoupment of taxpayer dollars made in overpayments through the DCIA timeline and bolstered by an effective internal controls process.

Question#:	3
Topic:	PAR
Hearing:	Eliminating and Recovering Improper Payments
Primary:	The Honorable Thomas R. Carper
Committee:	HOMELAND SECURITY (SENATE)

Question: It is noted at one point in the Department of Homeland Security's Fiscal Year 2006 Performance and Accountability Report that improper payments risk assessments at Customs and Border Protection, the Federal Law Enforcement Training Center, Immigration and Customs Enforcement, the Transportation Security Administration, the Coast Guard, and the Secret Service identified that improper payments had been made but the amounts made were below the reporting threshold set in OMB's implementing guidance for the Improper Payments Information Act. Were all programs and activities in these department components tested? How much in improper payments was discovered in the testing that was conducted? What percentage of program outlays did these improper payments make up?

Answer: The following programs and activities were tested in FY 2006:

- All programs were tested at the Federal Law Enforcement Training Center with a total error amount of $3,649 or 0.05%.
- All programs were tested at Immigration and Customs Enforcement with a total error amount of $1,310,201 or 0.3%.
- All programs were tested at Secret Service with a total error amount of $159 or less than 0.00%.
- Four of five programs were tested at Customs and Border Protection with a total error amount of $22,614 or less than 0.01%. The four programs covered 68% of all outlays.
- One of two programs was tested at the Coast Guard with a total error amount of $52,000 or less than 0.01%. Testing covered 52% of all outlays. The Coast Guard tested 2 of 3 programs for the Transportation Security Administration (the Federal Air Marshall Service was not tested) with a total error amount of $10,288,335 or 1.32%. Testing covered 86% of all outlays.

Question#:	4
Topic:	Risk Assessment
Hearing:	Eliminating and Recovering Improper Payments
Primary:	The Honorable Thomas R. Carper
Committee:	HOMELAND SECURITY (SENATE)

Question: It is also noted in the Fiscal Year 2006 Performance and Accountability Report that improper payments risk assessments at the Office of Grants and Training was not completed, in part due to difficulty in extending testing all way down to grant end users. Please elaborate on this. What did these problems entail? What steps are being taken to complete risk assessments for grant programs? When do you expect that risk assessments will be completed?

Answer:
In FY 2007 the Department will perform qualitative risk assessments of all DHS programs to identify programs that are susceptible to a high level of improper payments. This work will be the basis for determining additional programs that may need to be tested for improper payments. Consistent with the Department's new risk assessment process, DHS will work with FEMA and the Office of Grants and Training (G&T) to identify appropriate mechanisms to integrate improper payment testing with existing grant monitoring activities. G&T's current financial monitoring activities include pre-monitoring analysis and actual on-site monitoring visits. Through these monitoring activities, G&T is able to identify unallowable costs and over/under payments at the recipient and sub-recipient levels. Once identified, G&T has a process in place to recover funds. Examples of some of the analyses G&T uses to monitor grant activities include:

Pre-Monitoring Analysis:
- Single Audit Act Report (OMB A-133)
- Programmatic Reporting
- Previous Monitoring Reports (if available)
- Financial Status Report (SF269 analysis)
- OIG Reports
- Excess Cash (payment requests compared to expenditures)
- Payment History

On-site Analyses:
- General Ledger Review
- Flow of funds
- Recipient reimbursement policies and procedures
- Payment Documentation (i.e., testing of invoices (recipient and sub-recipient), payroll, travel, etc.)
- Payment history and trend analysis
- Continuation of Financial Status Report & Excess Cash

Question#:	4
Topic:	Risk Assessment
Hearing:	Eliminating and Recovering Improper Payments
Primary:	The Honorable Thomas R. Carper
Committee:	HOMELAND SECURITY (SENATE)

It is important to note, the difficulty in extending formal improper payment testing down to G&T's end users was one of a number of obstacles that prevented G&T from completing the FY 2006 improper payment testing of its grant population. Another obstacle to IPIA implementation includes issues resulting from the transfer of this function from G&T's legacy service provider to FEMA's newly-established Office of Grant Operations including: insufficient institutional knowledge and guidance and overall OGO staffing limitations, which prohibited the full resourcing of improper payment activities in order to meet other near-term and mission related competing priorities.

Responses to Questions from Timothy B. Hill

Hearing: *"Eliminating and Recovering Improper Payments"*

Senator Tom Coburn, M.D.

Senate Subcommittee on Federal Financial Management, Government Information, Federal Services, and International Security

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1. CMS expects Medicaid and SCHIP to be fully compliant with the Improper Payments Information Act by 2008. What needs to happen between now and then to ensure compliance by that date?

A: CMS implemented the Payment Error Rate Measurement (PERM) system for the Medicaid and SCHIP programs as a means to comply with the Improper Payments Reform Act (IPIA). The primary purpose of this system is to collect and maintain individually identifiable claims information that can be used in calculating Medicaid and SCHIP payment error rates. CMS is continuing to develop the infrastructure to support the measurement program. The measurement of a Medicaid fee-for-service (FFS) error rate is well underway for the FY 2006 error rate. A preliminary six month Medicaid FFS error rate for FY 2006 will be reported in the FY 2007 Performance and Accountability Report (PAR) and the full year FY 2006 Medicaid FFS error rate will be reported in the FY 2008 PAR.

For the FY 2007 error rate (to be reported in the FY 2008 PAR), we expanded the measurement to include improper payments based on FFS, managed care, and beneficiary eligibility for both Medicaid and the State Children's Health Insurance Program (SCHIP). We are currently collecting the FY 2007 State claims data for review of errors in FFS and managed care and the States are implementing the eligibility reviews. To improve our ability to meet milestone dates and report on error rate(s) as scheduled, we established dedicated teams to manage the progress of the FY 2007 measurement. In addition, we reached out to the States by implementing a technical advisory group, where the States and CMS can work together to resolve broader policy and operational issues. Further, we will be meeting monthly with the States beginning in May 2007 to resolve day-to-day operational issues slowing progress. CMS expects to publish the FY 2007 Medicaid and SCHIP national error rates in the FY 2008 PAR.

2. HHS maintained its "red" current status under the Eliminating Improper Payments program initiative in the Presidential Management Scorecard rating dated December 31, 2006. When does HHS expect to achieve a "green" status and what steps will be needed to achieve this change?

A: There are currently seven HHS programs identified as high-risk programs. HHS has now developed error rate measurement methodologies for each of these seven programs, which should result in a move from "red" to "yellow" status score on this PMA initiative in FY 2007. In addition, HHS has developed a plan for meeting the "green" scorecard

criteria and significant progress has already been made towards implementing that plan. Specifically, three of our seven high-risk programs (Medicare, Foster Care, and Head Start) currently report error rates in HHS' annual Performance and Accountability Report (PAR) and are making significant progress on meeting target reduction rates. It is particularly noteworthy that we have made great strides over the past decade reducing the error rate from 13.8% in 1996 to 4.4% in 2006 in Medicare – one of the largest Federal programs with FY 2006 outlays of $247 billion in fee-for-service payments. For our remaining four high-risk programs (Medicaid, State Children's Health Insurance Program, Temporary Assistance for Needy Families, and the Child Care Development Fund), we will report error rates in our FY 2008 PAR, thereby positioning HHS to meet the scorecard criteria for "green" for future periods.

3. The Child Care and Development Fund, and Temporary Assistance for Needy Families (TANF) programs are still not reporting improper payments estimates, even though these programs were required to report this information since 2002, with their fiscal year 2003 budget submission under previous OMB Circular No. A-11 requirements. OMB reports that national error rates will be included in HHS' fiscal year 2008 PAR. Will these error rates be generated from a statistically valid sampling methodology? Please describe the sampling methodology for each program.

A: ACF, in concert with HHS and based on agreements with OMB, will use statistically valid sampling methodologies to establish national improper payment error rates under the TANF and CCDF programs. The measurement approach for both programs was developed after considerable discussion with OMB, HHS' Office of the Assistant Secretary for Resources and Technology and for the TANF measurement with the HHS OIG. The specific sampling methodology for each program is outlined below:

TANF: The OIG is currently conducting/completing improper payment case reviews in three States (Michigan, New York and Pennsylvania) to test the sampling and review methodology that will be used in future reviews. These results will be reported in the FY 2007 PAR.

In FY 2008, the OIG is planning to randomly select eight States, conducting 150 case reviews in each State over a six month period, using a statistical model that will allow HHS to estimate a statistically valid national improper payment rate for the TANF program. These results will be reported in the FY 2008 PAR.

CCDF: ACF recently published an NPRM on March 2, 2007 (72 Fed. Reg. 9491) in which it proposes that, each State, the District of Columbia, and Puerto Rico will conduct the improper payment reviews for the CCDF program once every three years, on a rotating basis. HHS will report the results of the first set of states in the 2008 PAR. The Child Care Bureau has designated a 12 month review period, based on the Federal Fiscal Year ending September 30, for the data collection methodology. The primary sampling unit for this analysis will be an active case (case) for whom a child care subsidy was authorized for payment during a sample review month. States will create 12 sampling

frames of active cases (i.e., one sampling frame per month for each month in the 12 month review period). States will select a statewide random sample of at least 271 active cases. This model will allow the CCDF program to produce a statistically valid improper authorizations for payment rate.

4. In FY 2006, over $1.6 million was identified for recovery; however only $40,000 was actually recovered. Why didn't the agency recover more of the $1.6 million?

A: The HHS Recovery Auditing program to date has not produced great results as far as identification of overpayments or recoveries are concerned. However, that can also be interpreted as good news regarding the fiscal integrity of HHS programs.

More specifically, the question refers to recoveries in the most recent period of only $40,000, compared to $1.6 million identified for recovery. The term "identified for recovery" refers to the amount that our contractors initially believed could be recovered during a particular period. Our recovery auditing contractor, Connolly Consulting, has not closed the books on the years (2002-2003) represented by those figures and in fact is still actively pursuing claims in that regard. However, as Connolly has investigated the claims that had been originally categorized as "identified for recovery" they have discovered that many of them were not recoverable payment errors. An example of this situation is duplicate payments that had been previously adjusted by HHS finance offices. As Connolly has gotten more attuned to HHS payment systems, they have discovered that many of the claims that had previously been cited as erroneous are in fact correct, or have already been corrected in a prior period.

5. When does HHS anticipate reporting improper payment estimates for the Medicare Advantage Program and the Prescription Drug Benefits program?

A. CMS currently anticipates first reporting a component payment error rate for the Medicare Advantage Program (Part C) and for the Prescription Drug Benefits Program (Part D) in the FY 2007 PAR. As part of the CMS development of this risk based measurement process, CMS expects the error rate reporting for Parts C and D may be expanded in future years depending upon identified risks.

Responses to written questions submitted by Senator Coburn resulting from the March 29, 2007, hearing at which Mr. Terry Bowie testified regarding "Eliminating and Recovering Improper Payments."

Question 1: The Improper Payments Information Act requires that agencies annually review all of their programs and activities to identify those that are susceptible to significant improper payments. At the hearing, you testified that NASA used the results of the prior year's recovery audit for its FY 2006 risk assessment. Upon what pool of funds was this recovery audit applied – and what percentage of all NASA spending does that amount represent? If less than 95 percent, how can NASA claim that, the recovery audit information is a valid proxy for the annual risk assessment required by law.

Answer 1: NASA is currently performing a comprehensive risk assessment for 2007 that fully meets the requirements of the Improper Payments Information Act in accordance with OMB guidance. The subject recovery audit covered contract payments by NASA for research and development programs from 1997 through 2005, amounting to approximately $57 billion of payments or approximately 50 percent of total Agency outlays for that period. It did not cover payroll, rents, facility and other such expenditures. At that time, NASA believed the results of the Recovery Audit was a greater sample for risk assessment testing and therefore a valid proxy for the annual risk assessment, as reported in the Agency's FY 2006 Performance and Accountability Report (PAR). NASA will not take this approach in the future. We have contracted with a professional accounting firm to perform the 2007 risk assessment.

Question 2: According to Section 831 of the National Defense Authorization Act of 2001, agencies entering into contracts with a total value in excess of $500 million are required to perform a recovery audit. In its testimony, NASA stated that its recovery audit excluded fixed-priced contracts, which represents 12 percent of contract payments. What was the dollar value of these contracts that did not undergo a recovery audit?

Answer 2: NASA reviewed contract payments from all contract types – including fixed-price contracts – in its recovery audit, as stated in its testimony:

> "For its FY 2006 risk assessment, NASA used the results of the prior year's recovery audit. Through that process, NASA reviewed approximately $57 billion of cost and fixed-price contract payments across all programs dating back to 1997."

Question 3: Why were four of the twelve Centers excluded from recovery audits, as noted in the FY 2006 PAR?

Answer 3: All of the NASA Centers were included in the recovery audit. Nine NASA Centers make contract payments and all nine of these Centers were included in the NASA recovery audit program. One Center (Stennis Space Center) was inadvertently left out of the FY 2006 Performance and Accountability Report. It will be included in the FY 2007 report as applicable. The Stennis Space Center had no reportable amounts for recovery in FY 2006. NASA included the results of eight of its Centers when it should have reported the results of nine.

Question 4: You testified that questioned costs identified by the NASA OIG are not analogous to improper payments. Yet, the definition of questioned costs used by the NASA OIG includes contract costs that did not comply with rules, regulations, laws, contractual terms, or a combination of these. Why does NASA believe these types of

questioned costs are not improper?

Answer 4: NASA employs the Defense Contract Audit Agency (DCAA) to conduct audits of NASA's contracts under a reimbursable agreement each year. NASA's OIG reports the results of the DCAA audits in their Semi-annual Report to Congress. The questioned costs that are reported by NASA's OIG represent costs that the DCAA has identified as needing further analysis. The determination of whether the questioned costs represent legitimate or improper payments takes place between the contracting officer and the vendor or sometimes between DCAA and Defense Contract Management Agency (DCMA.). Therefore, the OIG reported DCAA questioned contract costs are a preliminary listing of costs under question which require review. Only after they are reviewed and validated can the costs be determined to constitute legitimate or improper payments.

Question 5: When will NASA report a full and complete improper risk assessment (not using recovery audit as proxy) for FY 2007?

Answer 5: NASA is conducting a comprehensive risk assessment for 2007 that will fully meet the requirements of the law in accordance with Office of Management and Budget (OMB) guidance. NASA will report the results of this risk assessment in its FY 2007 Performance and Accountability Report.

Public Law 107–300
107th Congress

An Act

Nov. 26, 2002
[H.R. 4878]

To provide for estimates and reports of improper payments by Federal agencies.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

Improper Payments Information Act of 2002.
31 USC 3321 note.

SECTION 1. SHORT TITLE.

This Act may be cited as the "Improper Payments Information Act of 2002".

31 USC 3321 note.

SEC. 2. ESTIMATES OF IMPROPER PAYMENTS AND REPORTS ON ACTIONS TO REDUCE THEM.

(a) IDENTIFICATION OF SUSCEPTIBLE PROGRAMS AND ACTIVITIES.—The head of each agency shall, in accordance with guidance prescribed by the Director of the Office of Management and Budget, annually review all programs and activities that it administers and identify all such programs and activities that may be susceptible to significant improper payments.

(b) ESTIMATION OF IMPROPER PAYMENT.—With respect to each program and activity identified under subsection (a), the head of the agency concerned shall—

(1) estimate the annual amount of improper payments; and

Deadline.

(2) submit those estimates to Congress before March 31 of the following applicable year, with all agencies using the same method of reporting, as determined by the Director of the Office of Management and Budget.

(c) REPORTS ON ACTIONS TO REDUCE IMPROPER PAYMENTS.—With respect to any program or activity of an agency with estimated improper payments under subsection (b) that exceed $10,000,000, the head of the agency shall provide with the estimate under subsection (b) a report on what actions the agency is taking to reduce the improper payments, including—

(1) a discussion of the causes of the improper payments identified, actions taken to correct those causes, and results of the actions taken to address those causes;

(2) a statement of whether the agency has the information systems and other infrastructure it needs in order to reduce improper payments to minimal cost-effective levels;

(3) if the agency does not have such systems and infrastructure, a description of the resources the agency has requested in its budget submission to obtain the necessary information systems and infrastructure; and

(4) a description of the steps the agency has taken to ensure that agency managers (including the agency head) are held accountable for reducing improper payments.

(d) DEFINITIONS.—For the purposes of this section:

(1) AGENCY.—The term "agency" means an executive agency, as that term is defined in section 102 of title 31, United States Code.

(2) IMPROPER PAYMENT.—The term "improper payment"—

(A) means any payment that should not have been made or that was made in an incorrect amount (including overpayments and underpayments) under statutory, contractual, administrative, or other legally applicable requirements; and

(B) includes any payment to an ineligible recipient, any payment for an ineligible service, any duplicate payment, payments for services not received, and any payment that does not account for credit for applicable discounts.

(3) PAYMENT.—The term "payment" means any payment (including a commitment for future payment, such as a loan guarantee) that is—

(A) made by a Federal agency, a Federal contractor, or a governmental or other organization administering a Federal program or activity; and

(B) derived from Federal funds or other Federal resources or that will be reimbursed from Federal funds or other Federal resources.

(e) APPLICATION.—This section—

(1) applies with respect to the administration of programs, and improper payments under programs, in fiscal years after fiscal year 2002; and

(2) requires the inclusion of estimates under subsection (b)(2) only in annual budget submissions for fiscal years after fiscal year 2003.

(f) GUIDANCE BY THE OFFICE OF MANAGEMENT AND BUDGET.—Not later than 6 months after the date of enactment of this Act, the Director of the Office of Management and Budget shall prescribe guidance to implement the requirements of this section. Deadline.

Approved November 26, 2002.

LEGISLATIVE HISTORY—H.R. 4878:

SENATE REPORTS: No. 107–333 (Comm. on Governmental Affairs).
CONGRESSIONAL RECORD, Vol. 148 (2002):
July 9, considered and passed House.
Oct. 17, considered and passed Senate, amended.
Nov. 12, House concurred in Senate amendment.

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