United States Government Accountability Office

GAO

Testimony before the Subcommittee on Government Organization, Efficiency, and Financial Management, Committee on Oversight and Government Reform, House of Representatives

For Release on Delivery
Expected at 10:00 a.m. EST
Tuesday, February 7, 2012

IMPROPER PAYMENTS

Moving Forward with Governmentwide Reduction Strategies

Statement of Beryl H. Davis, Director
Financial Management and Assurance

GAO
Accountability * Integrity * Reliability

GAO-12-405T

IMPROPER PAYMENT

Moving Forward with Governmentwide Reduction Strategies

GAO Accountability * Integrity * Reliability

Highlights

Highlights of GAO-12-405T, a testimony before the Subcommittee on Government Organization, Efficiency, and Financial Management, Committee on Oversight and Government Reform, House of Representatives

Why GAO Did This Study

Over the past decade, GAO has issued numerous reports and testimonies highlighting improper payment issues across the federal government as well as at specific agencies. Fiscal year 2011 marked the eighth year of implementation of the Improper Payments Information Act of 2002 (IPIA), as well as the first year of implementation for the Improper Payments Elimination and Recovery Act of 2010 (IPERA). IPIA requires executive branch agencies to annually identify programs and activities susceptible to significant improper payments, estimate the amount of improper payments for such programs and activities, and report these estimates along with actions taken to reduce them. IPERA, enacted July 22, 2010, amended IPIA and expanded requirements for recovering overpayments across a broad range of federal programs.

This testimony addresses (1) federal agencies' reported progress in estimating and reducing improper payments, (2) remaining challenges in meeting current requirements to estimate and report improper payments and (3) actions that can be taken to move forward with improper payment reduction strategies. This testimony is primarily based on prior GAO reports, including GAO's fiscal year 2011 audit of the Financial Report of the United States Government. The testimony also includes improper payment information recently presented in federal entities' fiscal year 2011 financial reports.

View GAO-12-405T. For more information, contact Beryl H. Davis at (202) 512-2623 or davisbh@gao.gov.

What GAO Found

Federal agencies reported an estimated $115.3 billion in improper payments in fiscal year 2011, a decrease of $5.3 billion from the prior year reported estimate of $120.6 billion. The $115.3 billion estimate was attributable to 79 programs spread among 17 agencies. Ten programs accounted for about $107 billion or 93 percent of the total estimated improper payments agencies reported for fiscal year 2011. The reported decrease in fiscal year 2011 was primarily related to three programs—decreases in program outlays for the Department of Labor's Unemployment Insurance program, and decreases in reported error rates for the Earned Income Tax Credit program and the Medicare Advantage program. Further, the Office of Management and Budget reported that agencies recaptured $1.25 billion in improper payments to contractors, vendors, and healthcare providers in fiscal year 2011. Over half of this amount, $797 million, can be attributed to the Medicare Recovery Audit Contractor program which identifies Medicare overpayments and underpayments.

The federal government continues to face challenges in determining the full extent of improper payments. Some agencies have not yet reported estimates for all risk-susceptible programs, such as the Department of Health and Human Services' Temporary Assistance for Needy Families program. Internal control weaknesses continue to exist, heightening the risk of improper payments. Some agencies' estimating methodologies need to be refined. For example, two Department of Defense commercial payment programs were not included in the total governmentwide error rate because the estimation methodologies for these programs were still under development.

A number of actions are under way across government to help advance improper payment reduction goals. These actions and future initiatives will be needed to enhance federal government efforts to reduce improper payments. For example,

- Additional information and analysis on the root causes of improper payment estimates would help agencies target effective corrective actions and implement preventive measures. Although agencies were required to report the root causes of improper payments in three categories beginning in fiscal year 2011, of the 79 programs with improper payment estimates for fiscal year 2011, 42 programs reported the root cause information using the required categories. In addition, because the three categories are general, additional analysis is critical to understanding the root causes.
- Implementing strong preventive controls can help defend against improper payments, increasing public confidence and avoiding the difficult "pay and chase" aspects of recovering improper payments. Preventive controls involve activities such as upfront validation of eligibility using electronic data matching, predictive analytic tests, and training programs. Further, addressing program design issues, such as complex eligibility requirements, may also warrant further consideration.
- Effective detection techniques to quickly identify and recover improper payments are also important to a successful reduction strategy. Detection activities include data mining and recovery audits. Another area for further exploration is the broader use of incentives to encourage and support states in efforts to implement effective preventive and detective controls.

Chairman Platts, Ranking Member Towns, and Members of the Subcommittee:

Thank you for the opportunity to be here today to discuss the issue of improper payments in federal programs and activities, including efforts by federal agencies to identify and reduce improper payments.[1] As the steward of taxpayer dollars, the federal government is accountable for how its agencies and grantees spend hundreds of billions of taxpayer dollars annually, including safeguarding those expenditures against improper payments, and establishing mechanisms to recover those funds when overpayments occur. It is important to note that not all of the reported improper payment estimates represent a loss to the government. For example, errors consisting of insufficient or lack of documentation are included in the improper payment estimates. Over the past decade, we have issued numerous reports and testimonies highlighting improper payment issues across the federal government as well as at specific agencies.[2]

Today, my testimony will focus on:

- federal agencies' reported progress in estimating and reducing improper payments, and
- remaining challenges in meeting current requirements to estimate and report improper payments.

I will also provide observations on actions that can be taken to move forward with improper payment reduction strategies.

[1]It is important to recognize that improper payment estimates reported by federal agencies in fiscal year 2011 are not intended to be an estimate of fraud in federal agencies' programs and activities. An improper payment is defined 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 good or service, any duplicate payment, any payment for a good or service not received (except for such payments where authorized by law), and any payment that does not account for credit for applicable discounts. Office of Management and Budget (OMB) guidance also instructs agencies to report as improper payments any payments for which insufficient or no documentation was found.

[2]See the Related GAO Products list at the end of this statement for a selection of the products related to these issues.

In preparing this statement, we drew upon our previously issued work related to the fiscal year 2011 audit of the Financial Report of the United States Government,[3] as well as our other previously issued products dealing with improper payments. Our previous products are listed at the end of this statement. That work was conducted in accordance with generally accepted government auditing standards. We are also including improper payment information recently presented in federal entities' fiscal year 2011 performance and accountability reports (PAR) and agency financial reports (AFR).

Background

Fiscal year 2011 marked the eighth year of implementation of the Improper Payments Information Act of 2002 (IPIA),[4] as well as the first year of implementation for the Improper Payments Elimination and Recovery Act of 2010 (IPERA).[5] IPIA requires executive branch agencies to annually review all programs and activities to identify those that are susceptible to significant improper payments, estimate the annual amount of improper payments for such programs and activities, and report these estimates along with actions taken to reduce improper payments for programs with estimates that exceed $10 million. IPERA, enacted July 22, 2010, amended IPIA by expanding on the previous requirements for identifying, estimating, and reporting on programs and activities susceptible to significant improper payments and expanding requirements for recovering overpayments across a broad range of federal programs.[6] IPERA included a new, broader requirement for agencies to conduct recovery audits, where cost effective, for each program and activity with at least $1 million in annual program outlays. This IPERA provision significantly lowers the threshold for required recovery audits from $500

[3]U.S. Department of the Treasury, *2011 Financial Report of the United States Government* (Washington, D.C.: Dec. 23, 2011), pp. 211-231.

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

[5]Pub. L. No. 111-204, 124 Stat. 2224 (July 22, 2010).

[6]IPERA defines "significant improper payments" as gross annual improper payments in the program exceeding (1) both 2.5 percent of program outlays and $10 million of all program or activity payments during the fiscal year reported or (2) $100 million (regardless of the improper payment error rate). Further, the threshold for "significant improper payments" will be reduced in fiscal year 2014 and each year thereafter to gross annual improper payments in the program exceeding (1) both 1.5 percent of program outlays and $10 million of all program or activity payments during the fiscal year reported or (2) $100 million (regardless of the improper payment error rate).

million[7] to $1 million and expands the scope for recovery audits to all programs and activities. Another new IPERA provision calls for federal agencies' inspectors general to annually determine whether their respective agencies are in compliance with key IPERA requirements and to report on their determinations. Under Office of Management and Budget (OMB) implementing guidance, these reports are required to be completed within 120 days of the publication of the federal agencies' annual PAR or AFR, with the fiscal year 2011 reports for most agencies due on March 15, 2012.

OMB continues to play a key role in the oversight of the governmentwide improper payments problem. OMB has established guidance for federal agencies on reporting, reducing, and recovering improper payments[8] and has established various work groups responsible for developing recommendations aimed at improving federal financial management activities related to reducing improper payments.

[7]Section 831 of the National Defense Authorization Act for Fiscal Year 2002, Pub. L. No. 107-107, div. A, 115 Stat. 1012, 1186 (Dec. 28, 2001), required 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. IPERA repealed these requirements.

[8]OMB, Circular No. A-136 Revised, *Financial Reporting Requirements* (Oct. 27, 2011); OMB Memorandum M-11-16*, Issuance of Revised Parts I and II to Appendix C of OMB Circular A-123* (Apr. 14, 2011); OMB Memorandum M-11-04, *Increasing Efforts to Recapture Improper Payments by Intensifying and Expanding Payment Recapture Audits* (Nov. 16, 2010); and OMB Memorandum M-10-13, *Issuance of Part III to OMB Circular A-123, Appendix. C* (Mar. 22, 2010).

OMB and Agencies Reported Progress in Estimating and Reducing Improper Payments

Federal agencies reported improper payment estimates totaling $115.3 billion in fiscal year 2011, a decrease of $5.3 billion from the revised prior year reported estimate of $120.6 billion.[9] Based on the agencies' estimates, OMB estimated that fiscal year 2011 improper payments comprised about 4.7 percent of the $2.5 trillion in total spending during that year for the agencies' related programs (i.e., a 4.7 percent error rate). The decrease in the fiscal year 2011 estimate is attributed primarily to decreases in program outlays for the Department of Labor's Unemployment Insurance program, and decreases in reported error rates for fiscal year 2011 (compared to fiscal year 2010) for the Department of the Treasury's (Treasury) Earned Income Tax Credit program and the Department of Health and Human Services' (HHS) Medicare Advantage program.

The $115.3 billion in estimated federal improper payments reported for fiscal year 2011 was attributable to 79 programs spread among 17 agencies. Ten of these 79 programs account for most of the $115.3 billion of reported improper payments. Specifically, as shown in table 1, these 10 programs accounted for about $107 billion or 93 percent of the total estimated improper payments agencies reported for fiscal year 2011.

[9]In their fiscal year 2011 PARs and AFRs, select federal entities updated their fiscal year 2010 improper payment estimates to reflect changes since issuance of their fiscal year 2010 reports. These updates decreased the governmentwide improper payment estimate for fiscal year 2010 from $125.4 billion to $120.6 billion. Estimated improper payment amounts for fiscal years 2011 and 2010 may include estimates based on prior years' data, if current reporting year data were not available, as allowed by OMB guidance.

Table 1: Improper Payment Dollar Estimates: 10 Programs with the Highest Reported Amounts in Fiscal Year 2011

Program	Agency	Reported improper payment estimates: Dollars (in billions)	Reported improper payment estimates: Error rate (percentages)	Reported primary cause(s)
Medicare Fee-for-Service	Health and Human Services	$28.8	8.6%	Medically unnecessary services and insufficient documentation
Medicaid	Health and Human Services	$21.9	8.1%	Ineligible or indeterminable eligibility status for Medicaid beneficiaries
Earned Income Tax Credit	Treasury	$15.2	23.5%	Complexity of the tax law, structure of the program, confusion among eligible claimants, high turnover of eligible claimants, and unscrupulous return preparers
Unemployment Insurance	Labor	$13.7	12.0%	Overpayments to claimants who continue to claim benefits after they return to work, ineligibility, and claimants who failed to meet active work search requirements
Medicare Advantage	Health and Human Services	$12.4	11.0%	Insufficient documentation, errors in the transfer and interpretation of data, and payment calculations
Supplemental Security Income	Social Security Administration	$4.6	9.1%	Recipients failed to provide accurate and timely reports of new or increased wages
Old Age Survivors' and Disability Insurance	Social Security Administration	$4.5	0.6%	Computation errors, eligibility errors, non-verification of earnings, and incorrect processing of applications or payments
Supplemental Nutrition Assistance	Agriculture	$2.5	3.8%	Incomplete or inaccurate reporting of income by participant and incorrect eligibility determination by caseworkers
National School Lunch	Agriculture	$1.7	16.0%	Verification errors related to benefit calculation error, duplicate payments, insufficient documentation, and fraud or misrepresentation by program participants or others
Medicare Prescription Drug Benefit	Health and Human Services	$1.7	3.2%	Payment errors, payment adjustment errors, and complexity of program

Source: GAO summary of agencies' data.

The 10 programs with the highest error rates had rates ranging from 11.0 percent to 28.4 percent. Specifically, as shown in table 2, those 10 programs accounted for $45 billion, or 39 percent of the total estimated improper payments for fiscal year 2011.

Table 2: Improper Payment Error Rates: 10 Programs with the Highest Reported Rates in Fiscal Year 2011

Program	Agency	Reported improper payment estimates: Error rate (percentages)	Reported improper payment estimates: Dollars (in millions)	Reported primary cause(s)
Disaster Assistance Loans	Small Business Administration	28.4%	$96.3	Loan documentation errors
School Breakfast	Agriculture	25.0%	$705.0	Authentication and administrative errors, including authenticating the accuracy of qualifying for program specific requirements, criteria, or conditions.
Earned Income Tax Credit	Treasury	23.5%	$15,200.0	Complexity of the tax law, structure of the program, confusion among eligible claimants, high turnover of eligible claimants, and unscrupulous return preparers
National School Lunch	Agriculture	16.0%	$1,716.0	Verification errors related to benefit calculation error, duplicate payments, insufficient documentation, and fraud or misrepresentation by program participants or others
State Home Per Diem Grants	Veterans Affairs	13.7%	$97.6	Documentation and administrative errors related to ineligible recipients, noncompliance with policies and procedures, incorrect amounts, ineligible goods, and lack of documentation
Supplies and Materials	Veterans Affairs	13.6%	$221.1	Documentation and administrative errors related to noncompliance with policies and procedures, lack of documentation, ineligible goods, incorrect amounts, and discounts not taken
Non-VA Care Fee	Veterans Affairs	12.4%	$522.9	Verification and documentation and administrative errors related to incorrect application of payment methodologies, lack of documentation, lack of authorization, and data entry errors
Unemployment Insurance	Labor	12.0%	$13,697.0	Overpayments to claimants who continue to claim benefits after they return to work, ineligibility, and claimants who failed to meet active work search requirements
Child Care and Development Fund	Health and Human Services	11.2%	$638.0	Documentation and administrative errors due to missing or insufficient documentation
Medicare Advantage	Health and Human Services	11.0%	$12,390.0	Insufficient documentation, errors in the transfer and interpretation of data, and payment calculations

Source: GAO summary of agencies' data.

Since the implementation of IPIA in 2004, federal agencies have continued to identify new programs or activities as risk-susceptible and report estimated improper payment amounts. The fiscal year 2011 governmentwide estimate of $115.3 billion included improper payment estimates for nine additional programs that did not report an estimate in fiscal year 2010, with the HHS Medicare Prescription Drug Benefit (Part D) program having the highest estimate of the newly included programs. We view these agencies' efforts as a positive step towards increasing the transparency of the magnitude of improper payments. However, three additional programs providing estimates in fiscal year 2011 were not included in the governmentwide totals because their estimation methodologies were still under development. The three excluded programs were the: Department of Education's Direct Loan, Department of Defense's (DOD) Defense Finance and Accounting Service Commercial Pay, and DOD's Army Corps of Engineers Commercial Pay.

A number of federal agencies have reported progress in reducing improper payment error rates in some programs and activities. For example, we identified 40 federal agency programs, or about 50 percent of the total programs reporting improper payment estimates in fiscal year 2011, that reported a reduction in the error rate of estimated improper payments in fiscal year 2011 when compared to fiscal year 2010 error rates. We caution, however, that these rates have not been independently verified or audited. The following are examples of agencies that reported reductions in program error rates and estimated improper payment amounts (along with corrective actions to reduce improper payments) in their fiscal year 2011 PARs, AFRs, or annual reports.

- Treasury reported that the fiscal year 2011 Earned Income Tax Credit (EITC) program's estimated improper payment amount decreased from the fiscal year 2010 amount of $16.9 billion to $15.2 billion, which represented a decrease in the error rate from 26.3 percent to 23.5 percent. Treasury reported that corrective actions taken to reduce improper payments primarily focused on completing examinations on tax returns that claimed the EITC before issuing the EITC portion of the refund, identifying math or other statistical irregularities in taxpayer returns, and comparing income information provided by the taxpayer with matching information from employers to identify discrepancies.

- HHS reported that the fiscal year 2011 estimated improper payment amount for the Medicare Advantage (Part C) program decreased from the fiscal year 2010 reported amount of $13.6 billion to $12.4 billion, which represented a decrease in the error rate from 14.1 percent to 11.0 percent. HHS reported that it reduced payment errors by continuing to routinely implement controls in its payment system to ensure accurate and timely payments, and implementing three key initiatives, including contract level audits, physician outreach, and Medicare Advantage organization guidance and training.

In addition, agencies have further developed the use of recovery audits to recapture improper payments. In 2010, the President set goals, as part of the Accountable Government Initiative, for federal agencies to reduce overall improper payments by $50 billion, and recapture at least $2 billion in improper contract payments and overpayments to healthcare providers, by the end of fiscal year 2012. For fiscal year 2011, OMB reported that governmentwide agencies recaptured $1.25 billion in overpayments to contractors and vendors. Over half of this amount, $797 million, can be attributed to the Medicare recovery audit contractor program which identifies improper Medicare payments—both overpayments and underpayments—in all 50 states. Cumulatively, OMB reported $1.9 billion recaptured from overpayments to contractors, vendors, and healthcare providers for fiscal years 2010 and 2011 towards the President's goal of recapturing at least $2 billion by the end of fiscal year 2012.

Remaining Challenges in Complete and Accurate Reporting of Improper Payments

Despite reported progress in reducing estimated improper payment amounts and error rates for some programs and activities during fiscal year 2011, the federal government continues to face challenges in determining the full extent of improper payments. Specifically, some agencies have not yet reported estimates for all risk-susceptible programs and some agencies' estimating methodologies need to be refined. We have also found that internal control weaknesses exist, heightening the risk of improper payments occurring. Until federal agencies are able to implement effective processes to completely and accurately identify the full extent of improper payments and implement appropriate corrective actions to effectively reduce improper payments, the federal government will not have reasonable assurance that the use of taxpayer funds is adequately safeguarded. We are currently working on engagements related to improper payment reporting at both DOD and HHS. Furthermore, as I will discuss later in this statement, additional analysis is needed to assess the root causes of improper payments, a key factor in identifying and implementing effective corrective actions.

We found that not all agencies have developed improper payment estimates for all of the programs and activities they identified as susceptible to significant improper payments. Specifically, three federal entities did not report fiscal year 2011 estimated improper payment amounts for four risk-susceptible programs.[10] In one example, HHS's fiscal year 2011 reporting cited various statutory barriers that hindered it from reporting improper payment estimated amounts. HHS cited statutory limitations for its state-administered Temporary Assistance for Needy Families (TANF) program,[11] which prohibited it from requiring states to participate in developing an improper payment estimate for the TANF program. Despite these limitations, HHS officials stated that they will continue to work with states and explore options to allow for future estimates for the program. For fiscal year 2011, the TANF program reported outlays of about $17 billion. For another program, HHS cited the Children's Health Insurance Program Reauthorization Act of 2009[12] as prohibiting HHS from calculating or publishing any national or state-specific payment error rates for the Children's Health Insurance Program (CHIP) until 6 months after the new payment error rate measurement rule became effective on September 10, 2010. According to its fiscal year 2011 agency financial report, HHS plans to report estimated improper payment amounts for CHIP in fiscal year 2012. For fiscal year 2011, the CHIP program reported federal outlays of about $9 billion.

As previously discussed, OMB excluded estimated improper payment amounts for two DOD programs from the governmentwide total because those programs were still developing their estimating methodologies—Defense Finance and Accounting Service (DFAS) Commercial Pay[13] with fiscal year 2011 outlays of $368.5 billion and U.S. Army Corps of Engineers Commercial Pay with fiscal year 2011 outlays of $30.5 billion.

[10]The four risk-susceptible programs that did not report a required improper payments estimate for fiscal year 2011 were the Department of Education's Federal Family Education Loan, Federal Communications Commission's Interstate Telecommunications Relay Services Fund, and HHS's Children's Health Insurance Program and Temporary Assistance for Needy Families.

[11]The term state-administered refers to federal programs that are managed on a day-to-day basis at the state level to carry out program objectives.

[12]Pub. L. No. 111-3, 123 Stat. 8 (Feb. 4, 2009).

[13]DOD refers to payments to contractors and vendors collectively as commercial payments.

In DOD's fiscal year 2011 agency financial report, DOD reported that improper payment estimates for these programs were based on improper payments detected through various pre-payment and post-payment review processes rather than using methodologies similar to those used for DOD's other programs, including statistically valid random sampling or reviewing 100 percent of payments. In its fiscal year 2011 agency financial report, DOD stated that it plans to begin statistical sampling of the Commercial Pay program in fiscal year 2012.

Both GAO[14] and the DOD Inspector General (IG)[15] have previously reported on weaknesses in DOD's payment controls, including weaknesses in its process for assessing the risk of improper payments and reporting estimated amounts. DOD's payment controls are hindered by problems related to inadequate payment processing, poor financial systems, and inadequate supporting documentation. Nonetheless, the DOD Comptroller testified in May 2011 that DOD assessed its commercial payment program as low risk because DOD management has concluded that it had a highly effective pre-payment examination process. That process includes a software tool that tests for potential improper payments before disbursement.[16] However, the DOD IG has reported[17] that the tool had a false positive[18] rate of more than 95 percent and that its use was not standardized across payment systems. Additionally, the DOD IG reported that DOD's risk of making improper payments was high and identified deficiencies in DOD's estimate of high-dollar overpayments that caused it to underreport the amount of improper

[14]GAO, *DOD Financial Management: Weaknesses in Controls over the Use of Public Funds and Related Improper Payments*, GAO-11-950T (Washington, D.C.: Sept. 22, 2011) and *Improper Payments: Significant Improvements Needed in DOD's Efforts to Address Improper Payment and Recovery Auditing Requirements*, GAO-09-442 (Washington, D.C.: July 29, 2009).

[15]DOD, Inspector General, *DOD Needs to Improve High Dollar Overpayment Review and Reporting*, D-2011-050 (Arlington, Va.: Mar. 16, 2011).

[16]DOD, *Statement of The Honorable Robert F. Hale, Under Secretary of Defense (Comptroller) before the Subcommittee on Federal Financial Management, Government Information, Federal Services, and International Security, Committee on Homeland Security and Governmental Affairs, U.S. Senate* (Washington, D.C.: May 25, 2011).

[17]D-2011-050.

[18]A false positive is a payment flagged as a potential improper payment that, after review, is determined to be proper.

payments made.[19] Until DOD fully and effectively implements a statistically valid estimating process for its commercial payments and addresses the known control deficiencies in its commercial payment processes, the governmentwide improper payment estimates are not complete.

For fiscal year 2011, two agency auditors reported on compliance issues with IPIA and IPERA as part of their 2011 financial statement audits. Specifically, the Department of Agriculture (USDA) auditors identified noncompliance with the requirements of IPERA regarding the design of program internal controls related to improper payments. In the other noncompliance issue, while HHS estimated an annual amount of improper payments for some of its risk-susceptible programs, a key requirement of IPIA, it did not report an improper payment estimate for its TANF and CHIP programs for fiscal year 2011. Fiscal year 2011 marked the eighth consecutive year that auditors for HHS reported noncompliance issues with IPIA.

Current and Future Actions to Move Forward with Improper Payment Reduction Strategies

A number of actions are under way across the federal government to help advance improper payment reduction goals. These initiatives, as well as additional actions in the future, will be needed to advance the federal government efforts to reduce improper payments. Identifying and analyzing the root causes of improper payments is key to developing effective corrective actions and implementing the controls needed to advance the federal government's efforts to reduce and prevent improper payments. In this regard, implementing strong preventive controls can serve as the front-line defense against improper payments. Proactively preventing improper payments increases public confidence in the administration of benefit programs and avoids the difficulties associated with the "pay and chase"[20] aspects of recovering overpayments. For example, addressing program design issues that are a factor in causing improper payments may be an effective preventive strategy to be

[19] D-2011-050. The IG report stated that DFAS and the Army Corps of Engineers did not review all payment systems for high-dollar overpayments. DFAS did not review approximately $2.2 billion in payments from five entitlement systems and the Corps of Engineers did not complete a timely review of $7.3 billion of commercial payments.

[20] "Pay and chase" refers to the labor-intensive and time-consuming practice of trying to recover overpayments once they have already been made rather than preventing improper payments in the first place.

considered. Effective monitoring and reporting can also help detect emerging issues. In addition, agencies can also enhance detective controls to identify and recover overpayments. For instance, enhancing incentives for grantees, such as state and local governments, could help increase attention to preventing, identifying, and recovering improper payments.

Identifying and Analyzing Root Causes of Improper Payments

Agencies cited a number of causes for the estimated $115.3 billion in reported improper payments, including insufficient documentation; incorrect computations; changes in program requirements; and, in some cases, fraud. Beginning in fiscal year 2011, according to OMB's guidance,[21] agencies were required to classify the root causes of estimated improper payments into three general categories for reporting purposes: (1) documentation and administrative errors, (2) authentication and medical necessity errors, and (3) verification errors.[22] Information on the root causes of the current improper payment estimates is necessary for agencies to target effective corrective actions and implement preventive measures.

While agencies generally reported some description of the causes of improper payments for their respective programs in their fiscal year 2011 reports, many agencies did not use the three categories to classify the types of errors and quantify how many errors can be attributed to that category. Of the 79 programs with improper payment estimates in fiscal

[21]OMB, Circular No. A-136 Revised, *Financial Reporting Requirements* (October 27, 2011) and OMB Memorandum M-10-13, *Issuance of Part III to OMB Circular A-123, Appendix C* (Mar. 22, 2010).

[22]OMB defines these error types as: *Documentation and Administrative Errors* - Errors caused by the absence of supporting documentation necessary to verify the accuracy of a payment or errors caused by incorrect inputting, classifying, or processing of applications or payments by a relevant Federal agency, State agency, or third party who is not the beneficiary; *Authentication and Medical Necessity Errors* - Errors caused by an inability to authenticate eligibility criteria through third-party databases or other resources because no databases or other resources exist, or providing a service that was not medically necessary given the patient's condition; and *Verification Error*s - Errors caused by the failure or inability to verify recipient information, including earnings, income, assets, or work status, even though verifying information does exist in third-party databases or other resources (in this situation, as contrasted with "authentication" errors, the "inability" to verify may arise due to legal or other restrictions that effectively deny access to an existing database or resource), or errors due to beneficiaries failing to report correct information to an agency.

year 2011, we found that agencies reported the root causes information using the required categories for 42 programs in their fiscal year 2011 PARs and AFRs. Together, these programs represented about $46 billion, or 40 percent of the total reported $115 billion in improper payment estimates for fiscal year 2011. Of the $46 billion, the estimated improper payment amounts were spread across the three categories, with documentation and administrative errors being cited most often. We did not calculate the dollar amounts in each category due to the imprecise narratives included in some of the agencies' reporting of identified causes, which would have required more detailed information and/or detailed examination of the underlying data. Nonetheless, additional analysis regarding the root causes is needed in order to identify and implement effective corrective and preventive actions in the various programs.

Implementing Effective Preventive Controls to Avoid Improper Payments

Many agencies and programs are in the process of implementing preventive controls to avoid improper payments, including overpayments and underpayments. Preventive controls may involve a variety of activities such as upfront validation of eligibility, predictive analytic tests, training programs, and timely resolution of audit findings. Further, addressing program design issues that are a factor in causing improper payments may be an effective preventive strategy to be considered.

Upfront eligibility validation through data sharing. Data sharing allows entities that make payments—to contractors, vendors, participants in benefit programs, and others—to compare information from different sources to help ensure that payments are appropriate. When effectively implemented, data sharing can be particularly useful in confirming initial or continuing eligibility of participants in benefit programs and in identifying improper payments that have already been made. Analyses and reporting on the extent to which agencies are participating in data sharing activities, and additional data sharing efforts that agencies are currently pursuing or would like to pursue is another important element needed to advance the federal government's efforts to reduce improper payments.

For example, the Department of Labor (Labor) reported that its Unemployment Insurance Program utilizes HHS's National Directory of

New Hires Database[23] to improve the ability to detect overpayments due to individuals who claim benefits after returning to work—the largest single cause of overpayments reported in the program. In June 2011, Labor established the mandatory use of the database for state benefit payment control no later than December 2011. Labor also issued a program letter that included recommended operating procedures for cross-matching activity for National and State Directories of New Hires.

In another case, to address the issue of inaccuracy of self-reported financial income on applications for student aid, the Department of Education (Education), in conjunction with the Internal Revenue Service (IRS), implemented a 6-month pilot version of an IRS data retrieval tool in January 2010 for its Pell Grant Program. The tool allows student aid applicants and, as needed, parents of applicants, to transfer certain tax return information from the IRS directly to Education's online application. Education reported that nearly 3.5 million students used the data exchange tool, representing approximately 21 percent of the applications submitted for the 2011 - 2012 academic year.

Predictive analytic technologies. The analytic technologies used by HHS's Centers for Medicare and Medicaid Services (CMS) are examples of preventive techniques that may be useful for other programs to consider. The Small Business Jobs Act of 2010 requires CMS to use predictive modeling and other analytic techniques—known as predictive analytic technologies—both to identify and to prevent improper payments under the Medicare fee-for-service program.[24] These predictive analytic technologies will be used to analyze and identify Medicare provider networks, billing patterns, and beneficiary utilization patterns and detect those that represent a high risk of fraudulent activity. Through such analysis, unusual or suspicious patterns or abnormalities can be identified and used to prioritize additional review of suspicious transactions before payment is made. The legislation required that contractors selected begin using these technologies on July 1, 2011, in the 10 states identified by CMS as having the highest risk of fraud, waste, or abuse in Medicare fee-for-service payments. Rather than focusing on the 10 states, CMS

[23]The National Directory of New Hires database, maintained by HHS, contains information on all newly hired employees, quarterly wage reports for all employees, and unemployment insurance claims nationwide.

[24]Pub. L. No. 111-240, § 4241, 124 Stat. 2504, 2599 (Sept. 27, 2010).

contractors began using these technologies to screen all fee-for-service claims nationwide prior to payment as of June 30, 2011, through CMS's new Fraud Prevention System.

Training programs for providers, staff, and beneficiaries. Training can be a key element in any effort to prevent improper payments from occurring. This can include both training staff on how to prevent and detect improper payments and training providers or beneficiaries on program requirements. For example, the Medicaid Integrity Institute, an initiative of CMS's Medicaid Integrity Group (MIG), trains state-level staff and facilitates networking by sponsoring free workshops for states. In addition, the MIG sponsors education programs for providers and beneficiaries, such as for pharmacy providers, to promote best prescribing practices and appropriate prescribing guidelines based on Food and Drug Administration labeling, potentially reducing improper payments.[25]

Timely resolution of audit findings. *Standards for Internal Control in the Federal Government*[26] requires that the findings of audits and other reviews be promptly resolved. Managers are to (1) evaluate findings from audits and other reviews promptly, including those showing deficiencies and recommendations reported by auditors and others who evaluate agencies' operations; (2) determine proper actions in response to findings and recommendations from audits and reviews; and (3) complete, within established time frames, all actions that correct or otherwise resolve the matters brought to management's attention.

Program design review and refinement. To the extent that provider enrollment and eligibility verification problems are identified as a significant root cause in a specific program, agencies may look to establish enhanced controls in this area. For example, CMS has taken steps to strengthen standards and procedures for Medicare provider enrollment to help reduce the risk of providers intent on defrauding or abusing the program.[27] Further, exploring whether certain complex and/or

[25]GAO, *Medicaid Program Integrity: Expanded Federal Role Presents Challenges to and Opportunities for Assisting States,* GAO-12-288T (Washington D.C.: Dec. 7, 2011).

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

[27]GAO, *Improper Payments: Reported Medicare Estimates and Key Remediation Strategies*, GAO-11-842T (Washington, D.C.: July 28, 2011).

inconsistent program requirements, such as eligibility criteria and requirements for provider enrollment, contribute to improper payments would lend insight to developing effective strategies for enhancing compliance and may identify opportunities for streamlining or changing eligibility or other program requirements.

Implement Effective Detective Controls to Identify and Recover Overpayments

Although strong preventive controls remain the frontline defense against improper payments, agencies also need effective detection techniques to quickly identify and recover those overpayments that do occur. Detection activities play a significant role not only in identifying improper payments, but also in providing data on why these payments were made and, in turn, highlighting areas that need strengthened prevention controls. The following are examples of key detection techniques to be considered.

- Data mining. Data mining is a computer-based control activity that analyzes diverse data for relationships that have not previously been discovered. The central repository of data commonly used to perform data mining is called a data warehouse. Data warehouses store tables of historical and current information that are logically grouped. As a tool in managing improper payments, applying data mining to a data warehouse allows an organization to efficiently query the system to identify potential improper payments, such as multiple payments for an individual invoice to an individual recipient on a certain date, or to the same address. For example, in the Medicare and Medicaid program, data on claims are stored in geographically disbursed systems and databases and are not readily available to CMS's program integrity analysts. CMS has been working for most of the past decade to consolidate program integrity data and analytical tools for detecting fraud, waste, and abuse. The agency's efforts led to the initiation of the Integrated Data Repository (IDR) program, which is intended to provide CMS and its program integrity contractors with a centralized source that contains Medicaid and Medicare data from the many disparate and dispersed legacy systems and databases. CMS subsequently developed the One Program Integrity (One PI) program,[28] a web-based portal and set of analytical tools by which

[28]The One PI portal is a web-based user interface that enables a single log-in through centralized, role-based access to the system.

these data can be accessed and analyzed to help identify cases of fraud, waste, and abuse based on patterns of paid claims.[29]

- Recovery auditing. While internal control should be maintained to help prevent improper payments, recovery auditing is used to identify and recover overpayments. The Tax Relief and Health Care Act of 2006 required CMS to implement a national Medicare recovery audit contractor (RAC) program by January 1, 2010.[30] In fiscal year 2011, HHS reported that the Medicare Fee-for-Service recovery audit program identified $961 million in overpayments and recovered $797 million nationwide. Further, the Medicaid RAC program was established by the Patient Protection and Affordable Care Act.[31] Each state must contract with a RAC, which is tasked with identifying and recovering Medicaid overpayments and identifying underpayments. The final regulations indicated that state Medicaid RACs were to be implemented by January 1, 2012. Similar to the Medicare RACs, Medicaid RACs will be paid on a contingency fee basis—a percentage of any recovered overpayments plus incentive payments for the detection of underpayments.

It is important to note that some agencies have reported statutory or regulatory barriers that affect their ability to pursue recovery auditing. For example, in fiscal year 2011, the Office of Personnel Management (OPM) reported that it faces regulatory barriers that restrict its ability to recover overpayments for its Retirement Program. OPM reported that based on current law and Treasury's regulations, financial institutions are barred from providing OPM with the information necessary to recover various overpayments. Only the Social Security Administration, Railroad Retirement Board, and the Department of Veterans' Affairs may receive the information necessary to identify the withdrawer to attempt to recover the overpayments because those agencies are the only ones named in the law to receive that type of information from financial institutions. According to OPM, Treasury

[29]We reported in July 2011 that IDR includes most types of Medicare claims data, but not the Medicaid data needed to help analysts detect improper payments of Medicaid claims. See *Fraud Detection Systems: Centers for Medicare and Medicaid Needs to Ensure More Widespread Use*, GAO-11-475 (Washington D.C.: July 12, 2011).

[30]Pub. L. No. 109-432, div B., title III, § 302, 120 Stat. 2922, 2991-92 (Dec. 20, 2006), *codified* at 42 U.S.C. § 1395ddd(h).

[31]Pub. L. No. 111-148, §6411, 124 Stat. 119, 773 (Mar. 23, 2010).

has drafted language to address the issue and is working to publish a notice of proposed rulemaking to amend its regulation.

In another instance, USDA reported that Section 281 of the Department of Agriculture Reorganization Act of 1994[32] precluded the use of recovery auditing techniques because Section 281 provides that 90 days after the decision of a state, county, or an area committee is final, no action may be taken to recover the amounts found to have been erroneously disbursed as a result of the decision unless the participant had reason to believe that the decision was erroneous. This statute is commonly referred to as the Finality Rule.

- Federal-state incentives. Another area for further exploration is the broader use of incentives for states to implement effective preventive and detective controls.[33] Agencies have applied limited incentives and penalties for encouraging improved state administration to reduce improper payments. Incentives and penalties can be helpful to create management reform and to ensure adherence to performance standards.

Chairman Platts and Ranking Member Towns, this completes my prepared statement. I would be happy to respond to any questions that you or other members of the subcommittee may have at this time.

[32]Pub. L. No. 103-354, § 281, 108 Stat. 3178, 3233 (Oct. 13, 1994), *codified, as amended, at* 7 U.S.C. § 7001.

[33]OMB's implementing guidance for IPERA allows agencies to use up to 25 percent of funds recovered under a payment recapture audit program, including providing a portion of funding to state and local governments.

Contacts and Acknowledgments

For more information regarding this testimony, please contact Beryl H. Davis, Director, Financial Management and Assurance, at (202) 512-2623 or by e-mail at DavisBH@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 Jack Warner, Assistant Director; W. Tyler Benson; Francine Delvecchio; Crystal Lazcano; Kerry Porter; and Carrie Wehrly.

Related GAO Products

For our report on the U.S. government's consolidated financial statements for fiscal year 2011, see U.S. Department of the Treasury. *2011 Financial Report of the United States Government*. Washington, D.C.: December 23, 2011, pp. 211-231.

Medicaid Program Integrity: Expanded Federal Role Presents Challenges to and Opportunities for Assisting States. GAO-12-288T. Washington, D.C.: December 7, 2011

DOD Financial Management: Weaknesses in Controls over the Use of Public Funds and Related Improper Payments. GAO-11-950T. Washington, D.C.: September 22, 2011.

Improper Payments: Reported Medicare Estimates and Key Remediation Strategies. GAO-11-842T. Washington, D.C.: July 28, 2011.

Fraud Detection Systems: Centers for Medicare and Medicaid Needs to Ensure More Widespread Use. GAO-11-475. Washington, D.C.: July 12, 2011

Improper Payments: Recent Efforts to Address Improper Payments and Remaining Challenges. GAO-11-575T. Washington, D.C.: April 15, 2011.

Improper Payments: Status of Fiscal Year 2010 Federal Improper Payments Reporting. GAO-11-443R. Washington, D.C.: March 25, 2011.

Opportunities to Reduce Potential Duplication in Government Programs, Save Tax Dollars, and Enhance Revenue. GAO-11-318SP. Washington, D.C.: March 1, 2011.

High-Risk Series: An Update. GAO-11-278. Washington, D.C.: February 2011.

Improper Payments: Significant Improvements Needed in DOD's Efforts to Address Improper Payment and Recovery Auditing Requirements. GAO-09-442. Washington, D.C.: July 29, 2009.

Improper Payments: Progress Made but Challenges Remain in Estimating and Reducing Improper Payments. GAO-09-628T. Washington, D.C.: April 22, 2009.

Improper Payments: Status of Agencies' Efforts to Address Improper Payment and Recovery Auditing Requirements. GAO-08-438T. Washington, D.C.: January 31, 2008.

Improper Payments: Federal Executive Branch Agencies' Fiscal Year 2007 Improper Payment Estimate Reporting. GAO-08-377R. Washington, D.C.: January 23, 2008.

Improper Payments: Weaknesses in USAID's and NASA's Implementation of the Improper Payments Information Act and Recovery Auditing. GAO-08-77. Washington, D.C.: November 9, 2007.

Improper Payments: Federal and State Coordination Needed to Report National Improper Payment Estimates on Federal Programs. GAO-06-347. Washington, D.C.: April 14, 2006.

GAO's Mission

The Government Accountability Office, the audit, evaluation, and investigative arm of Congress, exists to support Congress in meeting its constitutional responsibilities and to help improve the performance and accountability of the federal government for the American people. GAO examines the use of public funds; evaluates federal programs and policies; and provides analyses, recommendations, and other assistance to help Congress make informed oversight, policy, and funding decisions. GAO's commitment to good government is reflected in its core values of accountability, integrity, and reliability.

Obtaining Copies of GAO Reports and Testimony

The fastest and easiest way to obtain copies of GAO documents at no cost is through GAO's website (www.gao.gov). Each weekday afternoon, GAO posts on its website newly released reports, testimony, and correspondence. To have GAO e-mail you a list of newly posted products, go to www.gao.gov and select "E-mail Updates."

Order by Phone

The price of each GAO publication reflects GAO's actual cost of production and distribution and depends on the number of pages in the publication and whether the publication is printed in color or black and white. Pricing and ordering information is posted on GAO's website, http://www.gao.gov/ordering.htm.

Place orders by calling (202) 512-6000, toll free (866) 801-7077, or TDD (202) 512-2537.

Orders may be paid for using American Express, Discover Card, MasterCard, Visa, check, or money order. Call for additional information.

Connect with GAO

Connect with GAO on Facebook, Flickr, Twitter, and YouTube. Subscribe to our RSS Feeds or E-mail Updates. Listen to our Podcasts. Visit GAO on the web at www.gao.gov.

To Report Fraud, Waste, and Abuse in Federal Programs

Contact:

Website: www.gao.gov/fraudnet/fraudnet.htm
E-mail: fraudnet@gao.gov
Automated answering system: (800) 424-5454 or (202) 512-7470

Congressional Relations

Katherine Siggerud, Managing Director, siggerudk@gao.gov, (202) 512-4400, U.S. Government Accountability Office, 441 G Street NW, Room 7125, Washington, DC 20548

Public Affairs

Chuck Young, Managing Director, youngc1@gao.gov, (202) 512-4800
U.S. Government Accountability Office, 441 G Street NW, Room 7149
Washington, DC 20548