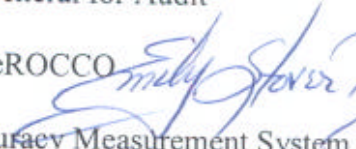




EXHIBIT 2

SEP 25 2003

MEMORANDUM FOR: ELLIOT P. LEWIS
Assistant Inspector General for Audit

FROM: EMILY STOVER DeROCCO 

SUBJECT: Audit of Benefit Accuracy Measurement System
Draft Report 22-03-009-03-315

Thank you for the opportunity to review and comment on the draft audit, "Improved Quality Control Practices Within the Benefit Accuracy Measurement System Could Save the Unemployment Insurance Trust Fund Approximately \$400 Million Annually."

We agree with the overarching audit findings that (1) incorporating a cross match of wage records or data from State Directories of New Hires (New Hires) into Benefit Accuracy Measurement (BAM) investigations would improve estimates of overpayment amounts caused by individuals continuing to claim unemployment insurance (UI) benefits after returning to work, and (2) operational use of New Hires information is useful in reducing this type of overpayment.

However, we do not agree with the audit's estimates of potential savings because the audit lacks sufficient explanation of the methodologies used by the Office of Inspector General (OIG) to develop its estimates. For example, the audit claims that \$428 million in overpayments could be saved by "expediting the implementation of New Hire database connectivity at 10 states and increasing its usage at another 8 states." The OIG estimate is substantially higher than the Employment and Training Administration (ETA) estimate of \$139 million maximum potential savings. We have been unable to replicate the OIG estimates based on the documentation provided.

Reducing UI overpayments is an ETA priority, and we have made significant progress toward creating a system that promotes overpayment reduction. As you know, we developed a work plan for reducing overpayments in response, in part, to OIG findings from an audit of the Department's Consolidated Principal Financial Statements. Among the completed activities on the work plan are:

- Development of an overpayment detection measure as a Government Performance and Results Act goal;
- Award of funds to 26 states to implement or enhance cross match systems with their State Directories of New Hires;



- Issuance of an advisory that summarized numerous analyses on UI overpayments, including the causes of overpayments and the costs-benefits of various overpayment detection efforts (See Unemployment Insurance Program Letter 23-03 or visit the Office of Workforce Security Web site at <http://www.workforcesecurity.doleta.gov>); and
- A successful national conference on benefit payment integrity ETA sponsored in conjunction with the National Association of State Workforce Agencies that provided a forum for disseminating successful practices for preventing, detecting, and collecting UI overpayments.

In the audit report, the OIG made nine recommendations designed to “heighten awareness of the current overpayment problem and reduce overpayments.” You will find from our responses (attached) that these recommendations or the underlying purposes of the recommendations have largely been addressed. Also attached are our suggestions for technical corrections to the audit report.

If you would like additional information, please contact me at 693-2700 or Ms. Cheryl Atkinson at 693-3200.

ETA Responses to Audit Recommendations
Audit of Benefit Accuracy Measurement System
Draft Report 22-03-009-03-315

Following are ETA's responses to the nine recommendations made in the audit report. The recommendations are quoted from the audit and appear in the order and format in which they appear in the report.

Recommendations

- 1) Amend ETA Handbook 395, Benefit Accuracy Measurement-State Operations, to prescribe a mandatory followup review for state BAM investigations to determine whether "unreported earnings," related overpayments occurred. The followup process should match state wage information with paid UI benefits and determine whether an overpayment (not previously detectable from the BAM investigation) occurred. We suggest the review occur 180 days after the week ending date of the payment originally investigated, so accurate wage information will be available. However, states connected to their New Hire database could choose to perform the followup earlier, provided reliable wage information was available.
- 2) Develop specific reporting and oversight procedures for all 180-day and/or New Hire database followup reviews. These procedures should address all state, regional, and national responsibilities.
- 3) Create a new formula for reporting overpayment information. The new formula should use existing BAM overpayment projections derived from initial investigations plus overpayment information obtained using a state's followup review procedure to validate "unreported earnings."

Agency Response

We agree conceptually with the recommendation that adding a process for a wage record or New Hires follow-up cross match as part of BAM investigations would produce a better estimate of total overpayments. As indicated in the OIG report, including a wage record cross match was considered during the implementation of the predecessor to BAM. However, the cross match segment was ultimately not included in the process out of concern that the cross match would delay completing the investigations too long.

We propose to pilot test cross matches of BAM cases with wage record and New Hires data in several states. The pilot would allow us to determine the magnitude by which estimates would be improved compared with the costs associated with the change in the process including the additional effort in the investigations, updating the BAM handbooks and reprogramming the BAM software at both the state and Federal levels. If

the pilot finds that national implementation is cost-beneficial, we will develop a procedure for incorporating the cross match into the BAM program. The pilot test is contingent upon the availability of funding and a sufficient number of states volunteering to participate in the pilot.

We think this effort responds to recommendations one, two and three.

Recommendations

- 4) Change ETA policy to make BAM overpayment information a TIER I measure in ETA's UI PERFORMS performance management system.
- 5) Include BAM overpayment analysis in the annual SQSP process. Monitors should negotiate overpayment issues with states to ensure these problems are addressed in SQSPs.
- 6) Utilize Unemployment Insurance Program Letters to communicate to the state partners the significance of the policy shift to overpayment prevention, and routinely make them aware of ongoing DOL initiatives to identify and prevent overpayments.
- 7) Utilize the BAM historical database to perform comparative (state-to-state) analyses, both at the national and regional levels.
- 8) Require Regional BAM Monitors to fulfill their program leadership duties and responsibilities. Specifically, require monitors to analyze BAM data for the states they monitor and identify trends of overpayments; work with assigned states to investigate overpayments identified by the national office; and, lead or facilitate process improvement initiatives designed to prevent overpayments in their assigned states.

Agency Response

The purpose of recommendations four through eight is to "make overpayment oversight a top priority." ETA agrees that overpayment oversight should be a top priority and has made significant efforts in this area. However, we propose to address overpayment oversight in a slightly different way than the methods suggested in the audit report.

Differences among states' laws, regulations, and policies regarding claimant eligibility influence the potential for error. States with strict and complex laws and policies tend to have higher improper payments. Therefore, comparing states' BAM overpayment rates can be misleading and the Department has consistently cautioned against making state-to-state overpayment rate comparisons.

However, during 2002, ETA used BAM data to develop a GPRA overpayment detection measure. The GPRA measure uses BAM data to compute an “operational overpayment rate” that includes the recoverable overpayments that states are most likely to detect through state operations. The operational overpayment rate is more comparable among states than the BAM annual overpayment rate because it excludes some of the elements that have the greatest variability among states (such as work search and employment service registration requirements). The GPRA measure compares the operational overpayment rate data with the amount of overpayments actually established for recovery to give a more comprehensive picture of states’ efforts to prevent and detect overpayments. The GPRA overpayment detection measure is discussed in detail in UIPL 15-03.

As part of an overall review of the UI performance management system, discussions are underway to include the GPRA overpayment detection measure as a “core measure” under UI PERFORMS. (UI PERFORMS is undergoing revision. The term “core measure” has been recommended as a substitute for the term “Tier 1.” Core measures will be equivalent to Tier 1 measures.) As a core measure, the overpayment detection measure will be subject to the same level of oversight as current Tier 1 measures, including being subject to corrective action for unacceptable performance.

GPRA measures, including the overpayment detection measure, are addressed in the SQSP process. State and regional office staff negotiate the substance of the SQSP, including the performance of the GPRA measures which are Federal Emphasis areas. (See UIPL 28-03.) We acknowledge that regional office staff do not conduct the analyses recommended in the BAM handbook. We think that it is more efficient for national office staff to continue to provide states and regional offices with analyses about overpayment rates and causes than for the regional offices to engage in overpayment analyses at this level. The regional offices will provide overpayment oversight through the SQSP process.

We think the purpose of recommendations four through eight—to make overpayment oversight a top priority—has been accomplished through the efforts described above.

Recommendations

- 9) Develop a process improvement initiative to implement New Hire database connectivity in the 10 states not currently connected and ensure all 50 states and the District of Columbia (DC) perform cross match procedures at least weekly. The process improvement initiative should be modeled after the CAP requirements set forth in ET Handbook 363, except the CAP should describe a federal initiative rather than a state initiative.

Agency Response

We generally agree that increased use of New Hires information has the potential to produce savings for the Unemployment Trust Fund (UTF) and have promoted state use of

New Hires data. This year, ETA provided funding to 26 states to connect to state New Hires databases or enhance existing New Hires cross match systems. In addition, we have promoted the use of New Hires data through workshops at the National Integrity Conference held in April. ETA will continue to encourage the use of New Hires data to reduce overpayments; however, rather than requiring specific state practices such as the use of New Hires data, we intend to set a performance goal for states with respect to overpayment prevention/detection and require states to determine which specific procedures they use to achieve the goal. We believe that all will use New Hires data because it is effective.

In addition, we think that access to the National Directory of New Hires would be a particularly beneficial tool for producing savings to the UTF and will continue to seek ways to give states that access.

ETA Comments To Audit of Benefit Accuracy Measurement System
Draft Report 22-03-009-03-315

Executive Summary

Page 1, paragraph 1: "BAM estimated UI benefit overpayments of \$2.5 billion for CY 2001 and \$3.7 billion for CY 2002."

Comment: The overpayment amounts noted in the report are correct; however, the report should also note that the increase in overpayments was attributable to the increase in UI benefit amounts paid from \$29.9 billion in CY 2001 to \$40.4 billion in CY 2002.

Section 1

Page 4, third full paragraph, last sentence: "In addition, the BAM investigator would have no means to determine if a claimant obtained employment after the investigation was completed."

Comment: This is true; however, the report should note that this has no impact on the validity of the BAM estimates.

Page 5, first full sentence: "Safeguards were implemented to require at least 95 percent of all results to be completed . . . within 90 days after a case was assigned."

Comment: Include in the report that the primary reason for this was to ensure that investigators make timely contacts while respondents' memories are fresh.

Page 5, fourth paragraph: "BAM projected unreported earnings overpayments at \$92 million in the six states we visited and our statistical projection was \$112 million."

Comment: We cannot replicate the OIG findings. Additional information is needed to support the OIG \$112 million projection. As written, the report leaves many unanswered questions. For example, the report does not state what proportion of these overpayments occurred in weeks other than the compensated (key) week that BAM sampled. In projecting to the population, if the overpayment occurred outside the BAM key week, to what population did the OIG project? Is it a claimant-based projection or a key week-based projection?

Also, the \$92 million BAM number used by the OIG includes only the BAM cause coded for unreported benefit year earnings (code 110). However, the BAM estimate also includes misreported earnings (code 120) and "other" causes related to the reporting or recording of BY earnings (code 150). For the states in question, these totaled \$128 million in CY 2001. It is likely that a portion of the BAM errors excluded by the OIG

will be picked up through the cross match (for example, wages initially reported or recorded in the wrong amount or in the wrong week). This suggests that the OIG's exclusion of these errors may inflate the difference between what BAM finds and the OIG findings.

Page 5, fifth paragraph: "Linear Regression Analysis," entire paragraph.

Comment: The linear regression analysis cites an unreported earnings overpayment amount of \$43 million for New York, versus \$1 million from BAM. Here, again, we cannot replicate the OIG findings because no detail is provided on the regression model that was used or the results for the other states. The lack of detail raises a number of questions. In how many states does the BAM amount exceed the amount estimated by the model? What were the independent variables in the model? Were the model results statistically significant?

Page 6, first full paragraph, fifth sentence: "This testimony stressed BAM CY 2001 overpayment projections were categorized into three groups. . . ."

Comment: Change statement to "The testimony categorized BAM CY 2001 overpayments into three groups."

Section II

Page 8, first sentence: "Preventing UI overpayments was not a priority under the UI PERFORMS quality control process."

Comment: UI PERFORMS is a performance management system that encompasses all aspects of performance and is not limited to quality control.

Page 8, third paragraph, first bullet: "Therefore, states were not required to achieve minimum levels of performance and received little oversight compared to Tier 1 measures;"

Comment: Because overpayment rates are not comparable among states, minimum levels of performance cannot be set on a system-wide basis. In addition, requiring states to meet specific BAM overpayment rates is in conflict with §602.43 of the Code of Federal Regulations.

Page 9, first paragraph, sentences six and seven: "To illustrate . . . Tier 1 measures have an ETA approved definition, source of data, and an established goal. Also, all Tier 1 measures have floor criteria."

Comment: Tier 1 measures do have criteria, but do not have "goals."

Page 9, first paragraph, eighth sentence: "In contrast, paid claims accuracy (the only BAM related overpayment Tier II measure) has no minimum level of performance and no defined criteria."

Comment: The report should note that denied claims accuracy was included in BAM in August 2001. Also, for purposes of UI PERFORMS, minimum levels of performance equate to "defined criteria."

Page 9, second paragraph: Entire paragraph.

Comment: As written, the paragraph is technically correct, but omits two important pieces of information. First, although no Tier 1 measures assess overpayment per se, there is a Tier 1 measure that assesses the quality of nonmonetary eligibility decisions. Second, the report should note that an overpayment detection measure was established as a FY 2002 GPRA goal.

Page 9, third paragraph, fifth sentence: "Conversely, errors related to Tier II problems are considered important, but not until all Tier I issues are resolved."

Comment: This statement is misleading. States, in fact, may simultaneously pursue Tier I corrective action plans and Tier II continuous improvement plans.

Page 10, second full paragraph, third from last sentence: "In contrast, a CIP is usually reserved for TIER II standards."

Comment: There are no "standards" for Tier II measures. We suggest that "performance" be substituted for "standards" in this sentence.

Page 11, first paragraph: "Unemployment Insurance Program Letters (UIPL) did not address overpayments," entire paragraph.

Comment: The first sentence of the paragraph states: "For the CY period 1999, 2000, and 2001, ETA issued 107 UIPLs, and with 2 exceptions, overpayment issues were not addressed."

UIPLs are an advisory series for the purpose of disseminating wide-ranging information to the states pertaining to all UI matters, not just to those matters pertaining to UI overpayments. The report infers that some percentage of these advisories should address overpayments. In addition, the assertion that only two pertained to overpayments is erroneous. The two UIPLs cited pertained specifically to implementing the New Hires systems in states in order to prevent and detect overpayments. However, these were not the only advisories pertaining to overpayments. The following are offered as examples of other UIPLs addressing the propriety of payments in the UI system:

- ✓ UIPL 07-99 – UI PERFORMS – Benefit Payment Control Measures

- ✓ UIPL 33-99 – Overpayment Recovery Technical Assistance Guide
- ✓ UIPL 01-2000 – Reporting New Hire Information on the ETA-227 Report
- ✓ UIPL 04-01 – Payment of Compensation and Timeliness of Determinations during a Continued Claims Series
- ✓ UIPL 15-01 – Obtaining Information Necessary to Determine Eligibility for Unemployment Compensation
- ✓ UIPL 19-01 – Unemployment Insurance Integrity Professional Development Conference

The third sentence of the paragraph states: “ETA’s only defined purpose of the UIPL [35-99] was to distribute copies of the audit report.” In fact, UIPL 35-99, in item 1, the “Purpose” states: “To distribute copies ... and to make recommendations for State Employment Security Agencies (SESAs) to take appropriate action in areas of weakness.” In addition, the recommendations of the OIG are summarized in item 4.

Further, item 5 includes “UIS Recommendations” and states: “The UIS agrees with the OIG assessment regarding the potential for the New Hire system. UIS encourages SESAs to realize this potential by implementing the New Hire system as the primary tool for the detection of overpayments. . . .”

Item 6, “Action Required” states: “SESA Administrators are requested to:

- a. Review the attached report from the OIG.
- b. Consider the recommendations offered by the OIG to improve the crossmatch system, and where necessary, take corrective action. (See section 4b above.)
- c. If not already instituted, consider using the State New Hire system as the primary tool for the detection of overpayments. . . .”

Section III

Page 14: Entire section.

Comment: As stated previously, we agree that increased use of New Hires data will reduce overpayments. ETA analyses estimated that states saved \$55 million in CY 2002 by using New Hires data. We projected potential savings of \$69 million if all states used New Hires data and savings of \$139 million if all states used New Hires data and established a number of overpayments equal to 2 percent of their first payments (the level achieved by the best performing states). The OIG-estimated savings of \$428 million is substantially greater than our estimates. Because of the substantial difference between

the OIG estimate, and the lack of adequate details that would allow us to replicate the OIG findings, we cannot accept the OIG savings estimate.

Background

Page 21, third sentence: “The week ending date of the selected payment is referred to as a key week, because results from the selected claims are used in statistical projections.”

Comment: To be accurate, the following should be substituted for the above sentence. “The selected payment is for a given week of compensated unemployment, identified by the week ending date. It is called the key week because results from the selected claims are used to make statistical projections for all those weeks of payments.”

Page 21, second and third paragraphs: Entire paragraphs.

Comment: Taken together, these two paragraphs suggest that UI PERFORMS was established pursuant to Title 20 CFR. In fact, Title 20 CFR establishes a quality control program (Benefits Quality Control which was renamed BAM). UI PERFORMS is a performance management system that includes quality control findings as part of its measurements rather than a quality control program; therefore, Title 20 CFR does not apply to UI PERFORMS as a whole.

Also, the reference to “law” should be changed to “regulation.”