U.S. Department of Labor

Office of Inspector General—Office of Audit

RECOVERY ACT: EFFECTIVENESS OF PENNSYLVANIA IN DETECTING AND REDUCING UNEMPLOYMENT INSURANCE IMPROPER PAYMENTS AND IMPLEMENTATION OF EMPLOYMENT AND TRAINING ADMINISTRATION NATIONAL STRATEGIES

This audit was performed by WithumSmith+Brown PC, CPAs, under contract to the Office of Inspector General, and by acceptance, it becomes a report of the Office of Inspector General.

Elliot P. Lewis

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Assistant Inspector General for Audit

Date Issued:	**March 31, 2015**
Report Number:	**18-15-001-03-315**

U.S. Department of Labor
Office of Inspector General
Office of Audit

BRIEFLY…

Highlights of Report Number 18-15-001-03-315, to the Assistant Secretary for Employment and Training.

WHY READ THE REPORT

The Unemployment Insurance (UI) program is designed to provide benefits to individuals out of work and is administered at the state level, but benefits are funded by both state and federal monies. The American Recovery and Reinvestment Act of 2009 provided additional funding for benefits for the Extended Benefits (EB), Emergency Unemployment Compensation (EUC), and Federal Additional Compensation (FAC) programs.

The audit covered Pennsylvania's efforts to detect, reduce, recover, and report UI improper payments from the inception of the Recovery Act through December 2012. The state paid $13.6 billion in EB, EUC, and FAC benefits, in addition to $14.1 billion in state-funded UI benefits during that period.

WHY OIG CONDUCTED THE AUDIT

Our audit objective was to answer the following question:

> How effective was Pennsylvania at detecting, reducing, recovering and reporting UI improper payments and at implementing Employment and Training Administration (ETA) National Strategies to reduce improper payments?

READ THE FULL REPORT

To view the report, including the scope, methodology, and full agency response, go to:
http://www.oig.dol.gov/public/reports/oa/2015/18-15-001-03-315.pdf

March 2015

RECOVERY ACT: EFFECTIVENESS OF PENNSYLVANIA IN DETECTING AND REDUCING UNEMPLOYMENT INSURANCE IMPROPER PAYMENTS AND IMPLEMENTATION OF EMPLOYMENT AND TRAINING ADMINISTRATION NATIONAL STRATEGIES

WHAT OIG FOUND

We found that Pennsylvania did not effectively detect, reduce, or recover improper payments, and the integrity of the data Pennsylvania reported to ETA could not be determined. Pennsylvania's detection and recovery rates remained well short of its target of 50 percent during our audit period, and its improper payments rates remained above the target rate of 10 percent. This was due in part to the state experiencing a significant increase in volume of UI claims, combined with the increased complexity of the EB and EUC programs, which overloaded Pennsylvania's capacity and strained its resources. Pennsylvania implemented seven of eight ETA National Strategies, but was not able to demonstrate their effectiveness.

WHAT OIG RECOMMENDED

We made several recommendations for ETA to work with Pennsylvania to help the state demonstrate the effectiveness of ETA's National Strategies and improve its detection and recovery rates.

ETA and Pennsylvania generally agreed with the recommendations and described planned and in-process corrective actions, except Pennsylvania disagreed that it does not measure the effectiveness of the National Strategies. However, the State said it would continue to work with ETA to adopt new approaches to prevent, detect, and recover overpayments.

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WithumSmith+Brown
A Professional Corporation
Certified Public Accountants and Consultants

8403 Colesville Road, Suite 340
Silver Spring, Maryland 20910 USA
301.585.7990 . fax 301.585.7975

www.withum.com
Additional Offices in New Jersey
New York and Pennsylvania

Independent Auditors' Report

March 31, 2015

Ms. Portia Y. Wu
Assistant Secretary
for Employment and Training
200 Constitution Avenue, N.W.
Washington, DC 20210

The Unemployment Insurance (UI) program is designed to provide benefits to individuals out of work and is administered at the state level, but benefits are funded by both state and federal monies, derived primarily from employer taxes. The Pennsylvania Department of Labor and Industry (L&I) is responsible for designing controls to detect and recover UI benefit overpayments.

The American Recovery and Reinvestment Act of 2009 (Recovery Act), which was enacted in February 2009, provided additional funding for benefits for the Extended Benefits (EB), Emergency Unemployment Compensation (EUC), and Federal Additional Compensation (FAC) programs.

We conducted a performance audit to answer the following question:

> How effective was Pennsylvania at detecting, reducing, recovering, and reporting UI improper payments and at implementing Employment and Training Administration (ETA) National Strategies to reduce improper payments?

We found Pennsylvania did not meet established targets for detecting, reducing, and recovering improper payments; and reported data could not be validated. Further, while Pennsylvania implemented seven of eight ETA National Strategies for reducing improper payments, Pennsylvania could not demonstrate that these strategies effectively reduced improper payments.

The Recovery Act provided funding from the general fund of the U.S. Treasury and extended the ending date of EUC benefits; created and funded a new program, FAC; and provided for 100 percent federal funding and extended the date of EB benefits. These three programs were further extended and funded by legislation subsequent to the Recovery Act. Although states were required to separately track and report the activities of these programs, they were not required to track and report on the separate funding sources within these programs. Therefore, Pennsylvania did not have a mechanism in place to identify overpayments and recoveries related to Recovery Act funding. As a result, we were not able to separately report on or determine the effectiveness of Pennsylvania's ability to detect, reduce, recover, and report on UI improper payments related solely to Recovery Act improper payments.

WithumSmith+Brown (WS+B), under contract with the Department of Labor (DOL) Office of Inspector General (OIG), audited Pennsylvania's effectiveness in detecting, reducing, recovering, and reporting improper payments for the period from the inception of the Recovery Act through December 31, 2012. Between February 2009 and December 2012, L&I paid $13.6 billion in EB, EUC, and FAC benefits, in addition to $14.1 billion in state-funded UI benefits.

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our results and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our results and conclusions based on our audit objective. Our objective, scope, methodology, and criteria are detailed in Appendix A.

Objective — How effective was Pennsylvania at detecting, reducing, recovering and reporting UI improper payments and at implementing ETA National Strategies to reduce improper payments?

> *Pennsylvania did not meet established targets for detecting, reducing, and recovering improper payments; reported data could not be validated; and it could not demonstrate that implemented strategies were effective.*

We found that Pennsylvania did not effectively detect, reduce, or recover improper payments, and the integrity of the data Pennsylvania reported to ETA could not be determined. Pennsylvania's detection rates remained well short of its target of 50 percent during our audit period. Its recovery rates generally remained below 50 percent, although ETA did not implement its Overpayment Recovery Rate measure until 2013. Furthermore, Pennsylvania's improper payment rates remained above the target rate of 10 percent. This was due in part to the state experiencing a significant increase in volume of UI claims, combined with the increased complexity of the EB and EUC programs, which overloaded Pennsylvania's capacity and strained its resources. During the time of high workload, ensuring timely payments to eligible claimants was the first priority for Pennsylvania. As a result, Pennsylvania transferred program integrity staff to process claims during the recession. Additionally, Pennsylvania's implementation of its

new Unemployment Compensation (UC) Management System, while continuing to operate its legacy mainframe system, created numerous issues in the administration of benefit payments and overpayment processing and reporting, hindering Pennsylvania's ability to detect, reduce, recover, and report improper payments.

In addition, of ETA's eight National Strategies aimed at reducing, detecting, and recovering improper payments, Pennsylvania implemented seven, but could not demonstrate the effectiveness of these strategies. The national strategy that Pennsylvania did not implement was the State Information Data Exchange System (SIDES). SIDES had not been implemented because Pennsylvania was waiting for the implementation of its new UC Management System. Pennsylvania subsequently implemented SIDES after our audit period in July 2014.

Pennsylvania did not meet established targets for detecting, reducing, and recovering improper payments; and reported data could not be validated.

Detecting Improper Payments

Although some of the ETA strategies that Pennsylvania implemented helped to increase the dollar value of overpayments it detected, the strategies did not significantly alter detection rates. Pennsylvania remained well short of its detection rate target of 50 percent during our audit period. Pennsylvania's detection rates remained in the 20 to 30 percent range from 2009 to 2011, then peaked at 46 percent in 2012, before dropping down to 40 percent in 2013. The peak in 2012 may be attributed to the decrease of benefit payments from 2011 to 2012 by $1.5 billion, which in turn, significantly decreased the estimated overpayments during 2012. Additionally, Pennsylvania continued working on its backlog of potential overpayments in 2012, which also contributed to the increase of overpayments established. Chart 1 below depicts the amounts detected as compared to the estimate of improper payments.

The primary means ETA uses to assess states' effectiveness at detecting improper payments is the detection rate, which measures the actual overpayments detected as a percentage of the detectable, recoverable overpayments as calculated by the Benefit Accuracy Measurement (BAM) program. The BAM program is a national program designed to statistically sample benefit payments made and estimate the improper payments in the UI program. ETA's target for all states was to detect and establish for recovery 50 percent of the detectable, recoverable overpayments.

Chart 1 - Overpayments Detected by Calendar Year
Compared to
## Total Improper Payments Estimated[1,2]
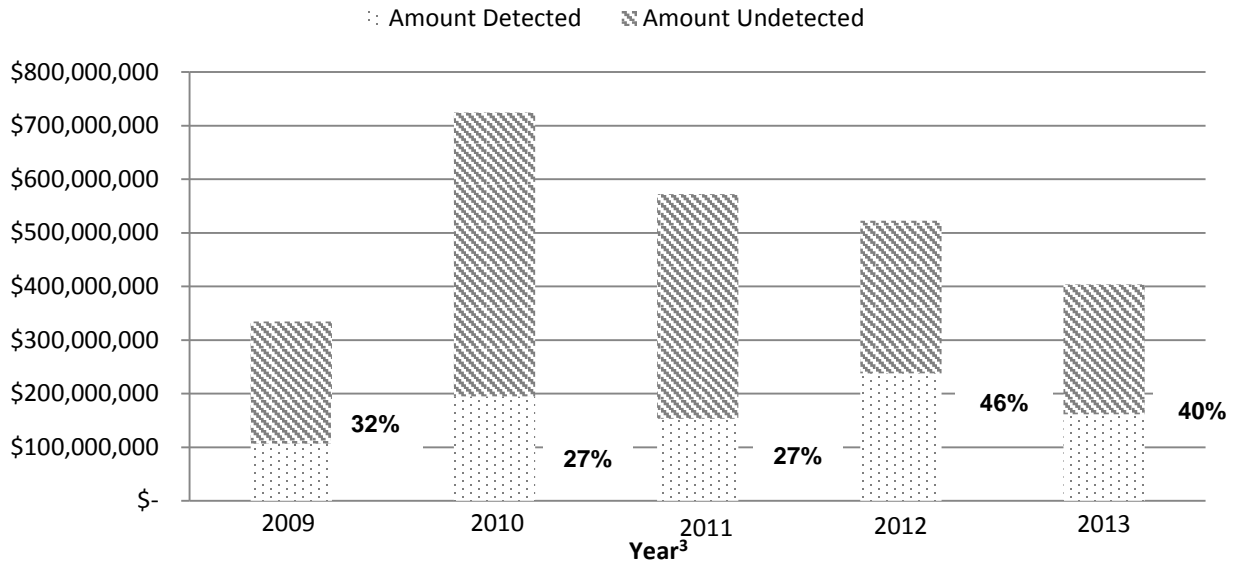
As depicted in Chart 2, from calendar year (CY) 2009 through CY 2013, Pennsylvania detected 33 percent of the estimated improper payments occurring during that time.

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[1] Although our audit period was through December 2012, we included subsequent period data for purposes of additional analysis.

[2] The denominator for the Detection of Overpayments ratio is estimated from the sample-based Benefit Accuracy Measurement program.

[3] ETA's methodology uses a data collection period of the numerator (BPC data) which begins and ends six months after the denominator (BAM data) to allow sufficient time to detect and establish overpayments identified through the wage-benefit cross match, which is only available quarterly.

**Chart 2 - Amount Detected Compared to Estimate of Total
Improper Payments
CY 2009 through CY 2013[4]**
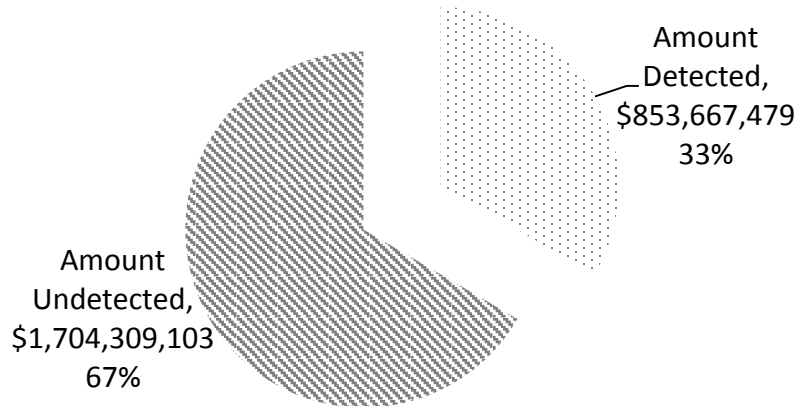
The ETA National Strategies Pennsylvania implemented to detect improper payments included the National Directory of New Hires (NDNH), State Directory of New Hires, and several state-specific strategies, including other types of cross matches. The cross-match process included using computer-assisted analysis of Pennsylvania UI information from various state and federal databases to identify claimants who may be ineligible to receive benefits. Identified matches must be researched before an overpayment determination can be made. However, we noted that obtaining third-party corroboration for cross matches can be difficult, and limited staffing resources hampered the state's ability to research the identified matches. As a result, backlogs of matches requiring research developed.

Further, data on the number of matches identified and researched, as well as the results of research, were not regularly maintained and analyzed, making it difficult to determine the effectiveness of the cross-match processes. Pennsylvania established Designated Overpayments Teams, a state-specific strategy, at the end of 2011 to help reduce the backlog of potential overpayments. Since the teams' inception in September 2011, through December 2013, they have helped detect and record approximately $174 million in overpayments.

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[4] Although our audit period was through December 2012, we included subsequent period data for purposes of additional analysis.

Reducing Improper Payments

Pennsylvania was not able to demonstrate effectiveness in reducing improper payments during our audit period. The primary means ETA uses to measure whether states effectively reduce improper payments are the rates calculated through the Benefit Accuracy Measurement program. This program provides a statistical estimate of the rate of improper payments during a period of time. Pennsylvania's improper payment rates during our audit period increased above the target rate of 10 percent, as depicted in Chart 3.

Chart 3 - Improper Payment Rates by Year[5,6]

Year Ended June 30
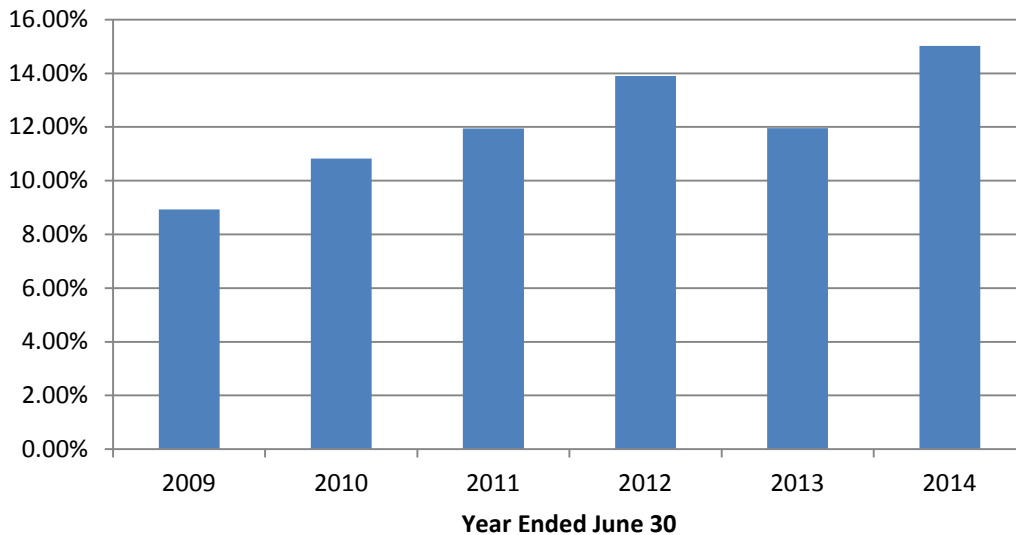
Many of the ETA strategies that Pennsylvania implemented were aimed at detecting or recovering overpayments, rather than preventing overpayments. The improper payment rate would not be impacted by improvements in detecting or recovering overpayments, since these strategies would not reduce the actual occurrence of overpayments, but rather would increase the detection of overpayments that have occurred. The effectiveness of strategies implemented by Pennsylvania that were aimed at preventing overpayments, such as a Cross-Functional UI Task Force, a State Quality Service Plan (SQSP)/Program Integrity Action Plan, and Claimant and Employer Messaging, cannot be adequately measured other than by the increase or reduction in the state's improper payment rate over time.

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[5] Although our audit period was through December 2012, we included subsequent period data for purposes of additional analysis.
[6] A confidence interval, expressed as +/- x percentage points, is constructed for the estimated improper payment rates. The actual rate is expected to lie within 95 percent of the intervals constructed from repeated samples of the same size and selected in the same manner as the BAM sample.

Recovering Improper Payments

We found no significant changes in the effectiveness of Pennsylvania's recovery efforts during our audit period. Other than the implementation of the Treasury Offset Program (TOP) in 2012, there were no significant changes in recovery methods utilized by Pennsylvania during our audit period. One measure of states' effectiveness at recovering improper payments is the rate of recoveries as a percentage of the overpayments detected and established (i.e., the recovery rate). Pennsylvania's annual recovery rates remained relatively unchanged in the 35 percent to 45 percent range, with the exception of a small spike in 2013 to 53 percent. We attribute the spike to a sharp decline in overpayments detected from 2012 to 2013 combined with the timing differences which can distort the measure when overpayments detected in one year are recovered in subsequent years.

Although Pennsylvania's recovery rates generally remained below 50 percent during our audit period, the annual dollar amount of recoveries doubled from 2009 to 2012, as the population from which to detect and recover overpayments increased. Recoveries were also aided by the extension of benefit weeks available to claimants as a result of legislation, since a significant portion of recoveries include offsets of future benefits. Charts 4 and 5 show the amount recovered compared to the amount detected by year and in total.

Chart 4 - Amount Recovered Compared to Amounts Detected by Calendar Year[7]

Legend: Amount Recovered / Amount Detected but Not Recovered

2009: 39%
2010: 36%
2011: 46%
2012: 35%
2013: 53%

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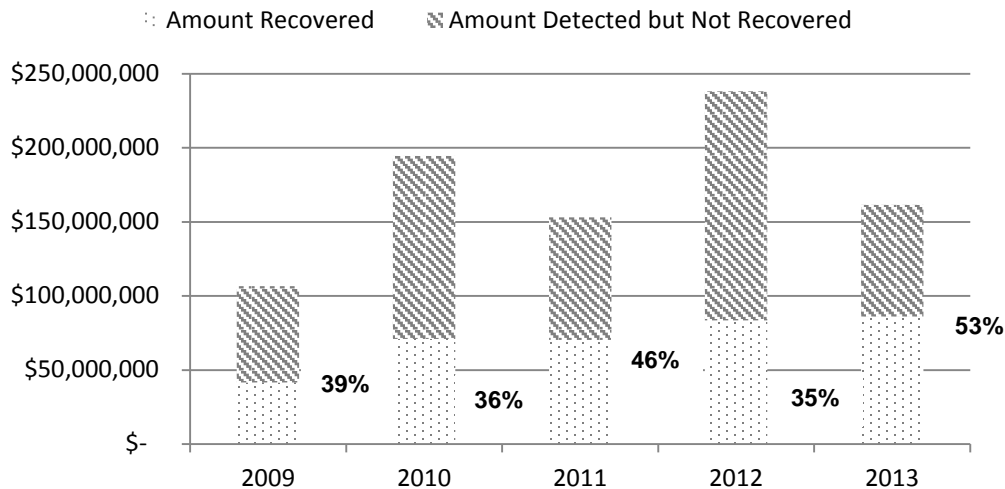
[7] Although our audit period was through December 2012, we included subsequent period data for purposes of additional analysis.

Chart 5 - Total Recoveries Compared to Amounts Detected[8,9]

Calendar Years 2009 to 2013

Detected but Not Recovered, $501,670,362 , 59%

Amount Recovered, $351,997,117 , 41%
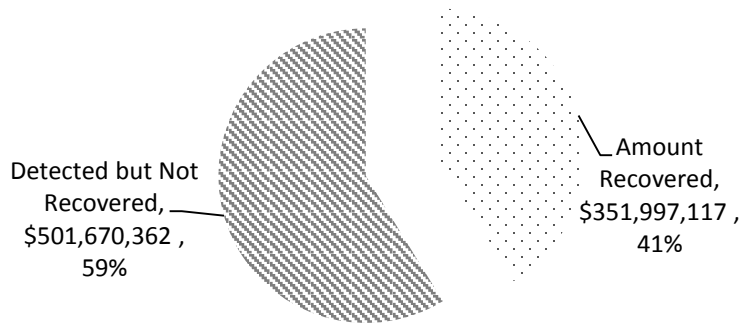
Once an overpayment was detected and proper notice was given to the claimant, Pennsylvania employed several types of recovery methods, which varied based on the nature of the overpayment (such as whether there was fraud or fault on behalf of the claimant). We found that benefit offset accounted for 53 percent[10] of the total recoveries made by Pennsylvania. Recovery methods utilized by Pennsylvania were:

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[8] Although our audit period was through December 2012, we included subsequent period data for purposes of additional analysis.

[9] Amounts detected included approximately $3.4 million of overpayments that were waived by PA.

[10] Includes State UI only. ETA does not require dollar amounts by recovery method for EUC to be reported on the EUC 227 report; therefore, this information was not available.

Table 1 - Recovery Methods Utilized by Pennsylvania

Method	Description
Benefit Offset	Reduction of future Pennsylvania UI benefit payments.
Treasury Offset Program (TOP)	Intercept and recovery by U.S. Treasury from Federal tax refund.
Voluntary repayment /billing notices/checks	Claimant voluntarily repays by check after receipt of notice.
Repayment plans	Claimant enters into a repayment plan with the state.
Interstate recovery[11]	Pennsylvania participates in the Interstate Reciprocal Coverage Arrangement (IRCA), which is a cooperative agreement among participating states designed to ensure continuity of coverage for UC benefits without receiving duplicate payments. When a claimant receives UC benefits from PA and another state simultaneously, IRCA allows PA to recoup duplicate week overpayments without the claimants permission.
Estates/probate/ bankruptcy	Pennsylvania recovers from estate of deceased claimant if estate is $5,000 or greater. Pennsylvania receives notice of bankruptcy and, if there are assets to be distributed, files a proof of claim.
Amnesty[12]	A one-time program used by claimant to allow for repayment of a certain portion of debt with the remaining portion being waived.
Liens	Pennsylvania records liens on claimants' property to recover funds in the event of a sale.

Source: *Auditors' analysis of descriptions and recovery methods utilized by Pennsylvania*

During 2012, Pennsylvania implemented TOP, whereby certain overpayments were submitted to the U.S. Treasury to intercept federal income tax refunds. This was an important new tool for Pennsylvania, which produced approximately $9 million of recoveries during 2012 related to 9,600 claimants. During 2013 and 2014, PA recovered approximately $17 million and $18 million, respectively, through TOP. However, these recoveries did not significantly alter the recovery rate.

One of the methods not utilized by Pennsylvania, the state income tax offset, has been used successfully by other states and could potentially increase the recovery amounts for Pennsylvania. Pennsylvania issued approximately $688 million in personal income tax refunds during the year ended June 30, 2012. Pennsylvania officials stated that state law does not provide for the intercept of state income tax refunds for UI debts, but that it plans to explore whether this may be a viable option for recoupment.

Reporting Improper Payments

We could not determine the effectiveness of Pennsylvania's reporting of overpayment and recovery activity to ETA, because Pennsylvania could not determine the integrity of the underlying mainframe data and pass ETA's data validation process. The ETA 227 report, *Overpayment, Detection, and Recovery Activities*, required summary-level information on overpayment detection and recovery activity by various categories, such

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[11] Partially implemented – Pennsylvania does not participate in the Interstate Reciprocal Overpayment Recovery Arrangement, which is a cooperative agreement to facilitate the overpayment recovery process.
[12] Implemented subsequent to our audit period.

as detection methods and fund types. Pennsylvania used a combination of mainframe reports, manual reports, and U.S. Treasury Offset reports in order to prepare the quarterly ETA 227, necessitating a manual, labor-intensive process requiring Pennsylvania to implement a variety of compensating controls to ensure the information was compiled and reported accurately. Therefore, although Pennsylvania ensured that the amounts reported on the ETA 227 flowed from the amounts recorded in its systems, Pennsylvania did not have any assurance the amounts in its systems were accurate.

ETA Handbook 361, *Unemployment Insurance Data Validation Handbook* (November 2009), established data validation requirements for the ETA 227 and related data elements, which states are required to perform and pass. To complete data validation, the state was required to provide ETA with individualized records (extracts) to be used to recalculate the report figures. The legacy system did not enable Pennsylvania to obtain the necessary extracts, and therefore Pennsylvania was not able to perform data validation to ensure the integrity of the underlying data reported to ETA.

Crosscutting System Weaknesses

Pennsylvania's ability to detect, reduce, recover, and report improper payments was hindered in part by its legacy mainframe system and the implementation of the new UC Management System. The state experienced significant problems and delays in implementing the new system. Pennsylvania's mainframe system, which was in the process of being replaced since 2005, impeded Pennsylvania from implementing certain controls or applications. System weaknesses included inabilities to: process EUC overpayments (which had to be performed outside the system), link with the ES Registration system, and fully implement SIDES, as well as difficulties in offsetting future benefit payments where interest is applicable. In addition, the mainframe system lacked adequate reporting capabilities and contributed to Pennsylvania's inability to perform data validation. Additional weaknesses resulting from the use of the mainframe for benefits processing included the inability to process FAC payments, and difficulty training employees to use the old platform.

The implementation of UC Management System was intended to modernize the UI system to enable Pennsylvania to increase features and functionality and automate certain manual processes. This system modernization was a very large, complex process requiring unique skill sets and specialized resources. Approximately $170 million had been invested in or dedicated to the new system, primarily from Reed Act funds[13], which have since been exhausted. Based on the results of an independent consultant's report in July 2013, Pennsylvania decided to stop development of the new system and continue with its legacy mainframe system while researching other options. Pennsylvania began making programming changes in the legacy system and continued

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[13] The "Reed Act" is a portion of the Employment Security Financing Act of 1954 that provides a mechanism for returning excess federal taxes to the state employment security agencies. When certain conditions are met, amounts are transferred to the states, which can then utilize the funds for a variety of UI or employment service (ES) administration or benefit purposes, with limited federal oversight.

to research options available for the benefits legacy system, including the possibility of joining a consortium of states and applying for DOL funding to support the modernization of its information technology (IT) systems, and assessing UI systems successfully implemented in other states.

Pennsylvania implemented seven of eight ETA National Strategies, but was not able to demonstrate these strategies were effective.

Although seven of the eight ETA National Strategies were implemented, Pennsylvania could not provide evidence of the strategies' effectiveness. Some strategies had an indirect impact on preventing overpayments that could not be measured in a meaningful way. For other strategies, information was not collected in a way to evaluate their effectiveness. Additionally, an analysis of the changes in the improper payment rates, detection rates, and recovery rates, showed no significant improvement in these rates, preventing demonstration of the strategies' effectiveness.

In 2011, ETA issued a "call to action" to help improve improper payment rates throughout the UI system and identified eight National Strategies that were designed to help states prevent, detect, and recover UI improper payments. The strategies were:

- **Cross-Functional Task Forces** – These are cross-functional teams that include a combination of management, front-line workers, and state subject matter experts that will assess and address root causes of improper payments in individual states. The key objectives for these task forces is to have every state focus on the root causes of overpayments that have the highest impact in the state and use this process to inform strategic planning that will achieve immediate and meaningful reductions in the improper payment rate.

- **SQSP/Program Integrity Action Plan** – As part of the submission of the SQSP (beginning in fiscal year (FY) 2012), states are required to develop a Program Integrity Action Plan. States are to analyze their Benefit Accuracy Measurement data to identify the top root causes for improper payments and develop strategies that will be effective in reducing or recovering improper payments, using an ETA prescribed format.

- **Mandatory Use of NDNH and Recommended Operating Procedures (ROP)** – For several years, ETA has encouraged states to use NDNH to reduce improper payments in the UI program. New-hire directories, which were created for the purpose of child support enforcement, have allowed for improved access to wage data and data from other states regarding new hires and wages. Studies conducted about NDNH have concluded that the use of this tool results in earlier detection of improper payments, thereby increasing the likelihood of recovery. Detailed recommended operating procedures have been developed to provide states with information about best practices in conducting this match. The ROP requires immediate contact with a claimant when there is a match to let them know there is a potential overpayment. This action is considered by ETA to be

one of the most effective strategies for addressing the Benefit Year Earnings' root cause. Any states not already doing so were required to begin conducting cross matches using NDNH by December 2011, and all states were strongly encouraged to implement procedures in line with the recommendations.

- **SIDES** – SIDES is a web-based system that allows electronic transmission of UI information requests from UI agencies to multi-state employers and/or third party administrators, as well as transmission of replies containing the requested information back to the UI agencies. The current implementation of SIDES allows for the exchange of separation and earnings verification information.

- **Claimant Messaging** – Statewide claimant messaging is a campaign designed to: improve claimants' awareness of their responsibility to report any work and earnings if they are claiming benefits, and improve claimants' understanding of work search requirements as a condition of eligibility for benefits. A state's campaign must consider how it may incorporate the Department's messaging products and tools.

- **Employer Messaging** – Statewide employer messaging is a campaign designed to improve employers' awareness of their responsibility to respond to state requests for separation information and/or earnings/wage verifications. The state's campaign must consider how it may incorporate the Department's messaging products and tools.

- **TOP** – TOP permits states to recover certain unemployment compensation debts from federal income tax refunds. This strategy is required for those states that received FY 2013 supplemental budget requests.

- **State-Specific Strategies** –State-specific strategies are to prevent improper payments and reduce the state's improper payment rates in key root cause areas. States must identify the extent to which the strategy is expected to reduce its improper payment rate, that is, identify a reduction target.

A ninth strategy, ES Registration, applied only to states whose ES Registration error rates exceeded 3percent.

- **ES Registration** –Strategies include technology or other solutions designed to address improper payments due to a claimant's failure to register with the state's ES or job bank in accordance with the state's UI law. These changes were to be implemented by April 30, 2012.

Pennsylvania did not initially implement SIDES because Pennsylvania was waiting for the implementation of the new UC Management System.

Table 2 illustrates the status of Pennsylvania's implementation of these strategies as of June 2013, when we performed our fieldwork:

Table 2 - Status of Implementation of ETA National Strategies

Strategy	Status
Cross-Functional Task Force	✔
SQSP/Program Integrity Action Plan	✔
NDNH	✔
SIDES	🚫
Claimant Messaging	✔
Employer Messaging	✔
State-Specific Strategies	✔
TOP	✔
✔ - Implemented 🚫 - Implemented after our audit period	

Source: Auditor analysis of Pennsylvania's implementation.

Pennsylvania received a Supplementary Budgetary Request from ETA for $223,535 in October 2011, to help pay for costs associated with SIDES. Pennsylvania's plan was to use this funding to help pay for the implementation of SIDES in the new UC Management System, with a projected completion date of September 30, 2012. However, because of issues encountered in the implementation of the new UC Management System, Pennsylvania decided to proceed with installation of one component of the SIDES infrastructure, which would serve to provide communications between the mainframe system and SIDES. ETA granted Pennsylvania an extension to March 31, 2014 to complete the SIDES component installation. SIDES was implemented by Pennsylvania in July 2014, after our audit fieldwork.

One of the state-specific strategies that Pennsylvania implemented in 2011 was the establishment of Designated Overpayment Teams at the UC service centers. Each service center has a Designated Overpayment Team, which helped reduce the state's backlog of unrecorded UC, EUC, and EB overpayments. Since their inception in September 2011, through December 2013, the Designated Overpayment Teams have helped detect and record approximately $174 million in overpayments.

Recommendations

We recommend that the Assistant Secretary for Employment and Training work with and encourage the Pennsylvania L&I to:

1. Continue to make improvements and enhancements to its legacy system, while other alternatives to replacing the legacy system are researched.

2. Develop measures for determining the effectiveness of cross-matching and other strategies.

3. Explore the steps necessary to utilize state income tax offset as a method of recovery, and make legislative recommendations if necessary.

ETA'S RESPONSE

The Assistant Secretary for Employment and Training concurred with our recommendations. In its response, ETA stated the IT Support Center is working with Pennsylvania to explore alternatives to address its need to modernize its IT system. ETA also stated it will work with Pennsylvania to encourage and provide technical assistance to develop and implement metrics that can be used to measure the effectiveness of Pennsylvania's strategies. Finally, ETA stated it will work with Pennsylvania to encourage implementation of the state income tax offset method of recovery, and share information regarding best practices and provide technical assistance in drafting state legislation. ETA's response to our draft report is included in its entirety in Appendix D.

PENNSYLANVIA'S RESPONSE

Pennsylvania partially agreed with our recommendations. In its response, Pennsylvania indicated it has been making modifications to the legacy system and is in the process of researching options to replace the legacy system. Pennsylvania also indicated it will explore whether implementation of state income tax interception for UC overpayments is a viable option. Pennsylvania disagreed that it does not have measures for determining the effectiveness of its strategies and stated that it does measure the effectiveness of these strategies and has implemented all recommended ETA National Strategies to prevent, detect, and recover overpayments. Pennsylvania provided specific results, such as the number and dollar amount of overpayments established as a result of the specific strategies it considered measurable and indicated that all of these strategies contributed to the improvement in its improper payment rate, detection rate, and recovery rate. Pennsylvania's response to our draft report is included in its entirety in Appendix E.

AUDITORS' CONCLUSION

While Pennsylvania is able to quantify some of the results of its strategies, it has not evaluated how the results of these strategies affect the targeted rates or other measures over time. Without comparing the results against a benchmark or other indicator, effectiveness of a strategy cannot be adequately determined.

WithumSmith+Brown, PC

Appendices

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Appendix A

Objective, Scope, Methodology, and Criteria

Objective

We conducted an audit to answer the following question:

> How effective was Pennsylvania at detecting, reducing, recovering, and
> reporting UI improper payments and at implementing ETA National Strategies
> to reduce improper payments?

Scope

The audit covered the processes and procedures Pennsylvania used to detect, reduce,
recover, and report UI improper payments between February 2009 and December
2012. Our audit work was performed at Pennsylvania Labor & Industry's main office for
UI activities located in Harrisburg, Pennsylvania, a Pennsylvania UI Service Center
located in Lancaster, Pennsylvania, and ETA's National Office in Washington, DC.

We conducted this performance audit in accordance with generally accepted
government auditing standards. Those standards require that we plan and perform the
audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our
conclusions based on our audit objective. We believe that the evidence obtained
provides a reasonable basis for our conclusions based on our audit objective.

Methodology

To conduct the audit, we interviewed officials in the ETA Office of Unemployment
Insurance in Washington, DC and reviewed relevant ETA policy letters and guidance
issued to the states. We obtained information and data specific to Pennsylvania from
the ETA National Office and the ETA Regional Office (Region 2). We also interviewed
officials at the Pennsylvania Department of Labor and Industry in Harrisburg,
Pennsylvania, reviewed Pennsylvania state policies and procedures, and performed
walkthroughs and testing of certain internal controls. We also performed testing on
reports submitted to ETA and on a judgmental selection of recorded overpayments. We
also visited a UC Service Center in Lancaster, Pennsylvania.

In planning and performing our audit, we obtained an understanding of Pennsylvania's
internal controls considered significant to the audit objective. The testing of
Pennsylvania's controls was not determined to be significant to our audit objective. We
considered Pennsylvania's internal controls relevant to our audit objective by obtaining
an understanding of those controls and assessing risk for the purpose of achieving our
objective. The objective of our audit was not to provide assurance on the internal
control, therefore, we did not express an opinion on ETA's or Pennsylvania's internal
controls. Our consideration of internal control would not necessarily disclose all matters

that might be significant deficiencies. Because of the inherent limitation on internal control, misstatements or noncompliance may occur and not be detected.

Criteria

- Recovery Act of 2009 (Public Law 111-5)
- Federal Unemployment Tax Act (Title 26, United States Code, Chapter 23)
- Social Security Act
  - Title III, Grants to States for Unemployment Compensation Administration
  - Title IX, Miscellaneous Provisions Relating to Employment Security
  - Title XII, Advances to State Unemployment Funds
  - Title XV, Unemployment Compensation for Federal Employees
- Federal-State Extended Unemployment Compensation Act of 1970, as amended
- Internal Revenue Code, as amended
- Improper Payments Information Act of 2002 (Public Law (P.L.) 107-300)
- Executive Order 13520, Reducing Improper Payments (2009)
- Improper Payments Elimination and Recovery Act of 2010 (P.L. 111-204)
- Middle Class Tax Relief and Job Creation Act of 2012

Appendix B

Acronyms and Abbreviations

BAM	Benefit Accuracy Measurement
BPC	Benefit Payment Control
CY	Calendar Year
DOL	Department of Labor
EB	Extended Benefits
ES	Employment Service
ETA	Employment and Training Administration
EUC	Emergency Unemployment Compensation
FAC	Federal Additional Compensation
FY	Fiscal Year
IRCA	Interstate Reciprocal Coverage Arrangement
IT	Information Technology
L&I	Department of Labor and Industry
NDNH	National Directory of New Hires
OIG	Office of Inspector General
OMB	Office of Management and Budget
PA	Pennsylvania
P.L.	Public Law
RECOVERY ACT	American Recovery and Reinvestment Act of 2009
ROP	Recommended Operating Procedures
SIDES	State Information Data Exchange System
SQSP	State Quality Service Plan
SSN	Social Security Number
TOP	Treasury Offset Program
UC	Unemployment Compensation
UI	Unemployment Insurance
WS+B	WithumSmith+Brown

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Appendix C

Glossary

Cash – Checks or money orders

Claimant Benefit Offsets – Deductions of claimants' weekly benefit payments that are applied toward their overpayment balances. Pennsylvania law allows 30 percent of a claimant's weekly benefit to be offset in cases of non-fraud overpayments, and 100 percent for fraud overpayments.

Data Validation – States are required to file a series of standardized reports on their UI operations with ETA on a monthly or quarterly basis. Since state programs differ significantly within established parameters and states utilize a variety of accounting and data processing arrangements, the issue of comparability among state reports has emerged. State reporting requirements are standardized, but states use a variety of reporting procedures and must interpret reporting requirements within the context of their own laws and accounting conventions. The UI Data Validation program was established in an attempt to identify and address discrepancies in reported numbers. The program requires that states recreate reported numbers independently from their reporting process and compare these numbers with actual numbers reported to DOL. States must address any discrepancies found that exceed the established tolerance error rate. The data validation program also requires that states examine a sample of reported cases to verify that the correct information is being counted.

State Directory of New Hires – The process of cross matching social security numbers (SSN) maintained in the State Directory of New Hires database against SSNs of claimants receiving benefits. This database is operated by state departments. Non-governmental employers are required to submit new-hire information, which populates the database. State Workforce Agencies investigate matches to determine if claimants are receiving UI payments while working, creating a potential overpayment due to unreported earnings.

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Appendix D

ETA's Response to Draft Report

U.S. Department of Labor

Assistant Secretary for
Employment and Training
Washington, D.C. 20210

MAR 2 6 2015

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

FROM: PORTIA WU
                    Assistant Secretary

SUBJECT: Response to the Office of the Inspector General (OIG) Audit
                    Report No. 18-15-001-03-315 – Recovery Act: Effectiveness of
                    Pennsylvania in Detecting and Reducing Unemployment Insurance
                    Improper Payments and Implementation of Employment and
                    Training Administration National Strategies

Thank you for the opportunity to respond to the report cited above. The Employment and
Training Administration (ETA) has been and continues to work aggressively with states to
improve the prevention, detection, and recovery of Unemployment Insurance (UI) improper
payments and to bring down the rate. ETA is committed to working with Pennsylvania to
address your recommendations and improve the integrity of its UI program.

ETA appreciates the acknowledgement on page 2 of the report that the recession created a major
challenge for states in addressing improper payments. States experienced significant increases in
the volume of UI claims that resulted in the shifting of resources to ensure timely payments to
eligible claimants. In addition, the complexity of the temporary benefit programs overloaded
state capacity. Many states, like Pennsylvania, also struggled with antiquated and inflexible
information technology systems that impacted their capacity to address program integrity issues.
These strains on state resources further hindered their ability to detect, prevent, and recover
improper payments.

As you noted in your report, ETA has identified a number of national strategies for state
implementation designed to address major root causes of UI improper payments as part of a
comprehensive strategic plan. ETA will continue working with states to identify and implement
new and innovative strategies to improve program integrity and bring down the improper
payment rate.

To promote development of innovative integrity strategies, ETA has established a national UI
Integrity Center of Excellence (Center) through a cooperative agreement with the New York
State Department of Labor. The Center is working collaboratively with ETA, a Steering
Committee comprised of representatives from five state workforce agencies, and the National
Association of State Workforce Agencies (NASWA) to guide the Center's work and ensure its
strategies support all states' integrity activities, creating greater efficiency, improving operations,
and saving millions of taxpayer dollars. The strategies and tools being developed by the Center
will be made available to all states and include, among others: data analytics and predictive
modeling methodologies and tools to improve UI fraud prevention and detection: a secure portal

for the rapid exchange of fraud information between states as it is identified; staff training on fraud solutions and integrity practices that is locally adaptable; highlighting integrity practices that should be included in state UI modernization efforts; and creation of a "model" plan for Benefit Payment Control operations.

I have attached our responses to the recommendations in the report. If you have questions, please contact Leo Miller, Acting Regional Administrator for the Philadelphia Office, at (215) 861-5204.

Attachment

2

**Employment and Training Administration (ETA) Response To
Office of the Inspector General (OIG) Report No. 18-15-001-03-315 – Recovery Act:
Effectiveness of Pennsylvania in Detecting and Reducing Unemployment Insurance
Improper Payments and Implementation of Employment and Training Administration
National Strategies**

ETA has been working aggressively with states to address the issue of UI improper payments and for the implementation of the national strategies for the detection, prevention, and recovery of improper payments. Below are ETA's specific responses to the recommendations in this report.

1. ETA should work with and encourage Pennsylvania to continue to make improvements and enhancements to its legacy system, while other alternatives to replacing the legacy system are researched.

Supporting modernization and enhancements to state information technology (IT) legacy systems has been a high priority for ETA for many years. To address this challenge, ETA funds and works collaboratively with the Information Technology Support Center (ITSC) operated by the National Association of State Workforce Agencies (NASWA), to provide technical assistance and support to individual states and state consortia on their UI information technology (IT) modernization efforts.

At Pennsylvania's request, ITSC is working with the state to explore alternatives to address its need to modernize its IT system, including conducting a business process analysis to identify areas of improvement in their claims-intake process to improve program integrity. ETA and ITSC will continue to identify opportunities that may be available to the Pennsylvania to modernize its IT system.

2. ETA should work with and encourage Pennsylvania to develop measures for determining the effectiveness of cross-matching and other strategies.

ETA will work with Pennsylvania to encourage and provide technical assistance to develop and implement metrics that can be used to measure the effectiveness of the state's strategies. We agree that it would be beneficial for the state to track the results of their integrity strategies to the extent feasible. However, we note that many variables impact a state's overall improper payment rate and root causes making it particularly challenging to develop measures that accurately evaluate the effectiveness of individual strategies.

3. ETA should work with and encourage Pennsylvania to explore the steps necessary to utilize state income tax offset as a method of recovery, and make legislative recommendations if necessary.

ETA will work with Pennsylvania to encourage the implementation of the state income tax offset as a method of recovery of UI overpayments. If the state decides to pursue the state income tax offset recovery method, ETA will share information regarding best practices from other states

1

that have implemented the offset and provide any technical assistance that may be necessary for drafting state legislation to ensure it conforms to Federal law.

2

Appendix E

Pennsylvania's Response to Report

<u>PENNSYLVANIA RESPONSE TO US DEPARTMENT OF LABOR
OFFICE OF INSPECTOR GENERAL AUDIT REPORT
3/20/15</u>

<u>Pennsylvania Has Made Improvement in the Targets for Detecting, Reducing
and Recovering Improper Payments</u>

<u>Detecting Improper Payments</u>

Although Pennsylvania's improper payment detection rate decreased slightly from 46% to 40% from 2012 to 2013, the rates have significantly improved since the 27% rate in 2010 and 2011. Pennsylvania is committed to continued improvement in detecting improper payments.

<u>Reducing Improper Payments</u>

From 2012 to 2013, Pennsylvania's improper payment rate improved, decreasing from nearly 14% to approximately 12%. Pennsylvania is committed to continued improvement in reducing improper payments.

<u>Recovering Improper Payments</u>

From 2012 to 2013, Pennsylvania's improper payment recovery rate improved, increasing from 35% to 53%. It is important to note that ETA did not have an Overpayment Recovery Rate measure until 2013. So during the review period of 2009 to 2012, any reference to a failure to meet the 50% requirement is inaccurate. Also, contrary to the report, Pennsylvania is a full participant in the Interstate Reciprocal Recovery Arrangement (IRORA). Pennsylvania is committed to continued improvement in recovering improper payments.

<u>Reporting Improper Payments</u>

As indicated in the audit report, Pennsylvania was unable to conduct data validation during the audit period due to the limitations in the Legacy mainframe system and the anticipated transition to a new computer system, UC Management System (UCMS), which was discontinued. However, Pennsylvania is currently working with ETA to revise its data validation guidebook and expects to begin UC Benefits data validation in 2016.

<u>Pennsylvania Has Implemented Eight of the Eight
ETA National Strategies and Can Demonstrate That They Are Effective</u>

Pennsylvania has implemented <u>all</u> eight of the eight ETA National Strategies aimed at the prevention, detection and recovery of UI overpayments. Pennsylvania strongly disagrees with the broad assertion in the audit report that "Pennsylvania could not provide evidence of the [ETA National] strategies' effectiveness." Pennsylvania provided the Office of Inspector General statistics on every measurable ETA strategy one year ago which is summarized below. All of these strategies contributed to the improvement in Pennsylvania's improper payment rate, detection rate and recovery rate.

1. **Cross Functional UI Integrity Task Force**

   - Status – implemented
   - Target – prevention, detection, recovery
   - Measurable Results – The UI Integrity Task Force is a cross-functional team that includes a combination of management, front-line workers, and state subject matter experts that assess and address root causes of improper payments. The key objective for the task force is to focus on the root causes of overpayments that have the highest impact in the state and use this process to plan strategies that will achieve immediate and meaningful reductions in the improper payment rate. See the results of all of the State Specific Strategies below.

2. **State Quality Service Plan (SQSP)**

   - Status - implemented
   - Target – prevention and detection
   - Measurable Results – The SQSP is a roadmap to state improvement, whereby states identify action steps to improve performance and then chart outcomes. A key component of the SQSP is the reporting and tracking of performance. The assessment of the SQSP actions is the performance outcome. Utilizing the SQSP action plan, PA increased its overpayment detection performance from 34.80% for the 4th qtr. of 2012 to 38.88% in 4th qtr. 2013.

3. **National Directory of New Hires (NDNH) and State Directory of New Hires (SDNH)**

   - Status - implemented
   - Target - prevention
   - Measurable Results –

Period	No. of Overpayments (OP) Established	Dollar Amount of Overpayments Established
2009	2,157	$1,880,255
2010	1,533	$1,234,370
2011	4,950	$3,649,432
2012	5,704	$3,702,590
2013	5,269	$3,083,780
Totals	**19,613**	**$13,550,427**

4. **State Information Data Exchange Systems (SIDES)**

   - Status - implemented
   - Target - prevention
   - Measurable Results – SIDES is a web-based system that allows electronic transmission of UI information requests from UI agencies to employers and/or Third Party Administrators, as well as transmission of replies containing the requested information back to the UI agencies. To date, over 12,000 employers participate in SIDES and exchange UI information with PA electronically.

5. **Claimant Messaging**

- Status - implemented
- Target – prevention
- Measurable Results – Implementation of a statewide claimant messaging campaign designed to: 1) improve claimants' awareness of their responsibility to report any work and earnings if they are claiming benefits, and 2) improve claimants' understanding of work search requirements as a condition of eligibility for benefits. This strategy is an awareness campaign, the results of which are difficult to quantify.

6. **Employer Messaging**

- Status - implemented
- Target - prevention
- Measurable Results – Implementation of a statewide employer messaging campaign designed to improve employers' awareness of their responsibility to respond to state requests for separation information and/or earnings/wage verifications. This strategy is an awareness campaign, the results of which are difficult to quantify.

7. **Treasury Offset Program (TOP)**

- Status - implemented
- Target - recovery
- Measurable Results – TOP allows the state to offset federal tax refund payments to collect unemployment compensation debts.

Period	No. of Garnished Refunds	Percent Increase between 2012-2013	Dollar Amount Recovered	Percent Increase between 2012-2013
2012 (2011 tax year)	4,317		$9,468,396.18	
2013 (2012 tax year)	9,019		$16,776,213.37	
Totals	13,336	208.92%	$26,244,609.55	177.18%

8. **State Specific Strategies**

   a. **DOT team (Designated Overpayment Teams)**

- Status - implemented
- Target – detection
- Measurable Results – DOTs were responsible for establishing over $63 million in overpayments for calendar year 2013; with a total of $174,348,508 in overpayments established since their inception in September 2011.

b. **Foreign IP blocker**

- Status - implemented
- Target - prevention
- Measurable Results – Foreign IP blocker runs the IP addresses that access the UC claimant website and creates a list of hits for further investigation. During calendar year 2013, 6,477 foreign IP addresses were blocked.

c. **UC Fraud Hotline and UC Fraud Link**

- Status - implemented
- Target – prevention and detection
- Measurable Results – In 2013 the Internal Audit Division (IAD) supervisors received a total of 1,441 new cases and staff completed 1,556 cases. From January 1, 2013 through December 31, 2013, IAD investigations resulted in the detection of an estimated $4,547,399 in fraud related overpayments.

d. **Border State, Intrastate and Interstate Cross-Match**

- Status - implemented
- Target - prevention
- Measurable Results –

Border State and Intrastate Cross-Match

Period	No. of Overpayments Established	Dollar Amount of Overpayments Established
February 1, 2009 to December 31, 2009	636	$629,870
2010	1,205	$1,344,686
2011	3,019	$3,317,615
2012	9,655	$16,800,427
2013	5,627	$12,033,003
Totals	**20,143**	**$34,125,601**

Interstate Cross-Match

Period	No. of OP Established	Dollar Amount of Overpayments Established
February 1, 2009 to December 31, 2009	67	$202,287
2010	531	$1,748,019
2011	693	$1,578,642
2012	1,233	$3,170,309
2013	1,449	$2,278,641
Totals	**3,973**	**$8,977,898**

e. **Justice Network (JNET)/Department of Corrections Cross-match**

- Status - implemented
- Target - prevention
- Measurable Results –

JNET Cross-Match

Period	No. of Overpayments Established	Dollar Amount of Overpayments Established
As of 1/16/13	268	$965,454

Period	Number of JNET Hits
2012	2,337
2013	18,961
Totals	**21,298**

Department of Corrections Cross-Match

Period	No. of Overpayments Established	Dollar Amount of Overpayments Established
CY 2012	202	$38,941

Period	Number of PA Department of Corrections Hits
2012	202
2013	86
Totals	**288**

f. **Amnesty Program**

- Status - implemented
- Target - recovery
- Measurable Results –

Type	No. of Overpayments Recovered	Dollar Amount of Overpayments Recovered
Claimants	6,524	$5,166,152
Employers	6,459	$10,418,837
Total	12,983	$15,584,989

g. **PA Department of Transportation (PennDOT) Cross-match**

- Status - implemented

- Target - prevention
- Measurable Results – There were 359 hits from this cross-match during calendar year 2012 and 137 hits from this cross-match between January 1, 2013, and June 30, 2013.

Recommendations Response

1) As indicated to the audit team and mentioned in the audit report, Pennsylvania has been making modifications to the Legacy mainframe system to improve its overall process efficiency since the discontinuance of the UCMS project in 2013. Pennsylvania is also in the process of researching the options to replace the legacy system.

2) As demonstrated in this response, Pennsylvania does measure the effectiveness of the ETA National Strategies and state specific strategies on overpayments. Pennsylvania has implemented all of the recommended ETA National Strategies and continues to work with ETA to adopt new approaches to prevent, detect and recover overpayments.

3) Pennsylvania will explore whether implementation of state income tax interception for UC overpayments is a viable option.

Conclusion

While Pennsylvania's overpayment performance did not meet all of the existing ETA standards during the audit period of 2009-2012, it must be reaffirmed that this occurred during a recessionary period that was unrivaled in recent history. Pennsylvania's claims load more than doubled during the review period and the focus had to be on providing UC benefit services to the unemployed. In addition, during this period, federal legislation resulted in complex benefit administration that was extremely difficult to manage and implement in a 40 year old Legacy mainframe system. As the workload has normalized, Pennsylvania is recommitted to improving all aspects of UC performance including overpayment metrics. Several improvements have been pointed out in this response and positive progress is expected to continue in the future.

TO REPORT FRAUD, WASTE OR ABUSE, PLEASE CONTACT:

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    202-693-6999

Fax: 202-693-7020

Address: Office of Inspector General
    U.S. Department of Labor
    200 Constitution Avenue, N.W.
    Room S-5506
    Washington, D.C. 20210