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## Federal Improper Payment Mandates and Their Financial Risk for State Governments

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## FEDERAL IMPROPER PAYMENT MANDATES & THEIR FINANCIAL RISK FOR STATE GOVERNMENTS

A Practical Guide to Help States Mitigate Federal Improper Payment Mandates.

### Abstract

As the recipient of billions in federal dollars, state governments are key stakeholders in combatting improper payments. While federal improper payment laws have mandated responsibility to federal agencies, states ultimately administer numerous federal programs, thus are subject to the same improper payment laws. Due to statistical sampling and extrapolation requirements in federal audits, state governments are at a tremendous financial risk for federal disallowances in administering federal programs. Federal reports and academic literature can inform state governments on improving state policies to mitigate their financial risk of federal improper payment laws.

**Seth Grove**

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*“This isn’t just about lines on a spreadsheet or numbers in a budget, because when we fail to spend people’s tax dollars wisely, that’s money we’re not investing in better schools for our kids or tax relief for families or innovation to create new industries and new jobs. When government doesn’t work like it should, it has a real effect on people’s lives, on small business owners who need loans, on young people who want to go to college, on the men and women who’ve served this country and are trying to get the benefits that they’ve earned. And when we continue to spend as if deficits don’t matter, that means our kids and our grandkids may wind up saddled with debts that they’ll never be able to pay.”*

President Barack H. Obama  
July 22, 2010

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## **Executive Summary**

The Congressional Budget Office (CBO) estimates that in federal fiscal year (FY) 2020 the federal government will have a deficit of \$1.0 trillion or 4.6 percent of gross domestic product (GDP).<sup>1</sup> In 2030, the projected gap between expenditures and revenues will increase to 5.4 percent of GDP.<sup>2</sup> Federal debt held by the public is currently at 91 percent of GDP and is expected to increase to 180 percent of GDP in 2050, that will be the highest level ever recorded in the United States.<sup>3</sup> While deficits have declined during periods of economic expansion, large deficits have continued despite consistent growth in the economy.<sup>4</sup> Between 2012 and 2019, the debt rose by nearly 6 percent annually compared with nominal GDP growth of about 4 percent.<sup>5</sup> At the end of 2019, federal debt held by the public was equal to 79.2 percent of GDP, higher than at any other time since just after World War II. In 2019, the government’s interest costs for debt totaled \$404 billion.<sup>6</sup>

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<sup>1</sup> Congressional Budget Office. “The Budget and Economic Outlook: 2020 to 2030.” January 28, 2020.

<sup>2</sup> Congressional Budget Office. “The Budget and Economic Outlook: 2020 to 2030.” January 28, 2020.

<sup>3</sup> Congressional Budget Office. “The Budget and Economic Outlook: 2020 to 2030.” January 28, 2020.

<sup>4</sup> Congressional Budget Office. “The Federal Deficit: A Primer.” March 2020.

<sup>5</sup> Congressional Budget Office. “The Federal Deficit: A Primer.” March 2020.

<sup>6</sup> Congressional Budget Office. “The Federal Deficit: A Primer.” March 2020.

Nevertheless, to put debt on a sustainable path, lawmakers would need to significantly change tax and spending policies: increasing revenues more than under current law, reducing spending below projected amounts, or adopting some combination of those approaches. The more time that passes before changes are made, the greater the burden those changes will place on future generations. It is unlikely, Congress will make the wholesale changes necessary to bring the federal budget into balance. Instead, they will look for other revenue sources like improper payments.

An improper payment is 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. They include:<sup>7</sup>

- Any payments to an ineligible party or any payments for an ineligible good or service.
- Any duplicate payment.
- Any payments for a good or service not received.
- Any payments that do not account for applicable credit discounts.
- Any payments where insufficient or lack of documentation prevents a reviewer from discerning whether a payment was proper.

The federal government has expended numerous resources to uncover, calculate, and reduce improper payments across the federal government through several bipartisan laws and executive branch actions. Combined, these federal actions create the backbone of current improper payment policies in the United States impacting subnational governments and federal grant recipients. State governments view federal improper payment laws as unfunded mandates.

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<sup>7</sup> Payment Integrity Information Act of 2019. Public Law 116-117, 116<sup>th</sup> Cong., 2<sup>nd</sup> sess. (March 2, 2020).

Federal improper payments laws are written to ensure the federal government benefits from the financial rewards of reducing improper payments.<sup>8</sup> While the federal government reaps the rewards of improper payment policies, state governments can face huge financial liabilities as the federal government distributes \$721 billion or 16 percent of its budget to state and local governments.<sup>9</sup> This is compounded by federal auditing requirements of statistical sampling and extrapolation where small amounts in verified errors can lead to severe liabilities.<sup>10</sup> Subnational governments have tremendous financial risk, and states in particular, as they administer numerous federal programs and receive numerous federal pass through dollars.

In order for state policymakers to mitigate the inherent risk in federal improper payment policies, they must understand the historical context of how the improper payment policy framework has been developed, how statistical sampling and extrapolation works, and what current practices have been developed to mitigate improper payments. While the United States Government Accounting Office (GAO) reports and scholarly literature can inform policymakers about successful programs and policies developed for the federal government, research is lacking for state government policymakers to mitigate their financial risk.

To inform state policymakers and continue the literature search on improper payments, this paper reviews the development of federal improper payment laws and the GAO's work on improper payments reporting. Further, a literature review of improper payments is made to help

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<sup>8</sup> Edward Sheen. "Eliminating Improper Payments: A Review, Framework for Action and Seven Fundamental Questions." *Journal of Government Financial Management*, Winter 2006. Page 46.

<sup>9</sup> Office of Management and Budget. *Budget of the United States Government, Fiscal Year 2019, Historical Tables*. Table 12.2. "Total Outlays for Grants to State and Local Governments, by Function and Fund Group: 1940–2025"; and Table 14.2. "Total Government Expenditures: 1948–2019."

<sup>10</sup> "RY 2019 Pennsylvania Medicaid Payment Error Rate Measurement (PERM) Cycle 1 Summary Report." Centers for Medicare and Medicaid Services. November 26, 2019. Page 6.

state policymakers develop policies and measures to mitigate financial risk of federal improper payment mandates.

## **SUMMARY OF RECOMMENDATIONS**

### **FEDERAL GOVERNMENT**

- PROVIDE FINANCIAL INCENTIVES AND UTILIZE FINANCIAL DISINCENTIVES
- STANDARDIZE REPORTING OF PUBLIC ASSISTANCE REPORTING INFORMATION SYSTEM (PARIS) AND DO NOT PAY DATA SHARING PROGRAMS
- CLOSE AUDIT GAPS IN PAYMENT ERROR RATE MEASUREMENT (PERM) REPORTS

### **STATE GOVERNMENT**

- ADOPT A STATE LEVEL IMPROPER PAYMENT STATUTE ALIGNED TO THE FEDERAL STATUTES
- ALIGN STATE INTERNAL CONTROLS TO THE FEDERAL “GREEN BOOK”
- MAXIMIZE USE OF FEDERAL DATA SHARING PROGRAMS AND ENSURE FOLLOW UPS ARE COMPLETED
- CREATE STATE DATA SHARING PROGRAM
- SHIFT RISK TO SUBRECIPIENTS
- PROVIDE STATE LEGISLATIVE OVERSIGHT

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*“Of course, we have all known about the high rates of improper payments in all of these programs for years now. And while these numbers, by their sheer size, are staggering, none of them should be surprising. This is a problem that has been many years in the making. And if you ask me, the time for addressing it is long past due.”*

U.S. Senator Orrin G. Hatch (R-Utah)

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### **Federal Improper Payment Laws**

Federal statutes on improper payments did not happen overnight but were developed through several pieces of legislation stretching over a decade. All the legislation passed with unanimous votes of Congress, substantiating Congress’s collective view that improper payment policies are a nonpartisan issue and a very important policy issue to both parties. The historical development of federal improper payment laws lays a foundation of how the federal government is setting policy which can inform state government policymakers of why current federal laws are in place and how state governments can develop their own improper payment laws.

Congress has passed and the President has issued several substantial pieces of legislation or executive orders to eliminate improper payments: The Improper Payments Information Act of 2002 (IPIA)<sup>11 12</sup>, Executive Order 13520<sup>13</sup>, The Improper Payments Elimination and Recovery Act of 2010 (IPERA)<sup>14</sup>, The Improper Payments Elimination and Recovery Improvement Act of 2012 (IPERIA)<sup>15</sup>, The Federal Improper Payments Coordination Act of 2015<sup>16</sup>, and The Payment

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<sup>12</sup> Improper Payments Information Act of 2002, Public Law 107-333. 107th Cong. November 26, 2002.

<sup>13</sup> Obama, Barack. “Executive Order 13520 – Reducing Improper Payments.” November 20, 2009.

<sup>14</sup> Improper Payments Elimination and Recovery Act of 2010, Public Law, 111th Cong. July 22, 2010.

<sup>15</sup> Improper Payments Elimination and Recovery Improvement Act of 2012, Public Law, 112th Cong. January 10, 2013.

<sup>16</sup> Federal Improper Payments Coordination Act of 2015, 114th Cong. sess. (2015-2016).



Integrity Information Act of 2019 (PIIA)<sup>17</sup>. All these laws and executive orders have required federal agencies to track and develop corrective action plans to reduce improper payments.

### ***The Improper Payments Information Act of 2002 (IPIA)***

On November 26, 2002, President George W. Bush signed into law the IPIA. The IPIA required agency heads, in accordance with the Office of Management and Budget (OMB), to review all programs and activities under their jurisdiction to identify the programs and activities which may be susceptible to improper payments. For each program, the agency head is required to estimate the annual amount of improper payments, submit those estimates to Congress, provide corrective action plans to reduce improper payments, and include the estimates of improper payments in the of agency's budget submissions.

### ***Executive Order 13520 – Reducing Improper Payments & Presidential Memorandums***

Seven years after the enactment of IPIA, President Barack Obama issued Executive Order (EO) 13520 on reducing improper payments, which provided the backbone for all future improper payment laws enacted by Congress. EO 13520 targeted four main areas<sup>18</sup>:

- Transparency and Public Participation.
- Agency Accountability and Coordination.
- Enhanced Focus on Contractors and Working with State and Local Stakeholders.
- Develop of Policy Recommendations.

The Transparency and Public Participation section of EO 13520 refocused improper payment policy to address high-priority programs that have the highest dollar value or where the majority of government-wide improper payments have occurred. It further required agencies to publicize and set annual or semiannual targets for reducing improper payments in high-priority

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<sup>17</sup> Payment Integrity Information Act of 2019. Public Law 116-117, 116<sup>th</sup> Cong., 2<sup>nd</sup> sess. March 2, 2020.

<sup>18</sup> Obama, Barack. "Executive Order 13520 – Reducing Improper Payments." November 20, 2009.

programs. Publication of improper payments through EO 13520 resulted in the creation of [www.PaymentAccuracy.gov](http://www.PaymentAccuracy.gov) operated by OMB that is required to be displayed on each agency's website.<sup>19</sup> This website includes the names of the accountable agency officials designated to be responsible for meeting agency improper payments targets; current and historical rates and amounts of improper payments; current and historical rates and amounts of recovery of improper payments; and the entities that have received the greatest amount of outstanding improper payments.<sup>20</sup> Lastly, this section required the Secretary of the United States Treasury to establish an internet-based method to collect public information on suspected incidents of waste, fraud, and abuse that have led to improper payments.<sup>21</sup>

The Agency Accountability and Coordination section required every agency to designate a Senate-confirmed official to be accountable for meeting the improper payment targets under EO 13520 without burdening program access and participation by eligible beneficiaries. The agency's designated official is required to submit a report to each agency Office of Inspector General (OIG) that includes each agency's methodology for identifying and measuring improper payments; a plan, with supporting analysis, on how each agency will meet improper payment targets; and a plan, with supporting analysis, to ensure the initiatives taken will not unduly burden program access and participation by eligible beneficiaries.<sup>22</sup> If agencies do not meet their agency goals for two consecutive fiscal years, the agency is required to submit a report to the agency's OIG and Chief Financial Officer including a remedial plan and causes of the agency's failure.<sup>23</sup> The Secretary of the United States Treasury is required to recommend to the

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<sup>19</sup> <https://www.paymentaccuracy.gov/>.

<sup>20</sup> Obama, Barrack. "Executive Order 13520 – Reducing Improper Payments." November 20, 2009. Page 2.

<sup>21</sup> Obama, Barrack. "Executive Order 13520 – Reducing Improper Payments." November 20, 2009. Page 2.

<sup>22</sup> Obama, Barrack. "Executive Order 13520 – Reducing Improper Payments." November 20, 2009. Pages 2-3.

<sup>23</sup> Obama, Barrack. "Executive Order 13520 – Reducing Improper Payments." November 20, 2009. Page 3.

President methods to improve information sharing among agencies and subnational governments to improve eligibility verification and pre-payment examination.<sup>24</sup> Finally, this section of EO 13520 required agencies to develop a report to recover improper payments and prevent improper payments in the future.<sup>25</sup>

The Enhanced Focus on Contractors and Working with State and Local Stakeholders section of EO 13520 is designed to enhance government contractor accountability for improper payments.<sup>26</sup> This section established two different working groups of federal agencies, state government officials, and local government officials to make recommendations on improving the effectiveness of Single Audits to identify improper payments and eliminate minimal value requirements and to improve incentives and accountability for subnational governments to reduce improper payments.<sup>27</sup> The last section of EO 13520 directed the Director of OMB to develop policy recommendations to reduce improper payments to be included in the FY 2011 budget and future budgets.<sup>28</sup>

EO 13520 was followed up by two memorandums from President Obama in March and June of 2010 to reinforce the executive branch's efforts to curtail improper payments as laid out in EO 13520. These two memorandums directed federal agencies to expand the use of payment recapture audits or recovery audits and created the "Do Not Pay List". A recovery audit is when government subcontracts auditing work to a private entity, usually a certified public accountant

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<sup>24</sup> Obama, Barrack. "Executive Order 13520 – Reducing Improper Payments." November 20, 2009. Page 3.

<sup>25</sup> Obama, Barrack. "Executive Order 13520 – Reducing Improper Payments." November 20, 2009. Page 3.

<sup>26</sup> Obama, Barrack. "Executive Order 13520 – Reducing Improper Payments." November 20, 2009. Page 4.

<sup>27</sup> Obama, Barrack. "Executive Order 13520 – Reducing Improper Payments." November 20, 2009. Page 4.

<sup>28</sup> Obama, Barrack. "Executive Order 13520 – Reducing Improper Payments." November 20, 2009. Page 4.

or fraud examiner, on a contingency basis to examine payments in order to uncover duplicative payments, payments for services not rendered, overpayments, and fictitious vendors.<sup>29</sup>

The Do Not Pay List memorandum of June 18, 2010 required federal agencies to utilize current federal databases to ensure recipients of federal benefits are eligible.<sup>30</sup> This prepayment screening process requires agencies to use the Social Security Administration's Death Master File, the General Service Administration's Excluded Parties List System, the Department of the Treasury's Debt Check Database, the Department of Housing and Urban Development's Credit Alert System or Credit Alert Interactive Voice Response System, and the Department of Health and Human Services' Office of Inspector General's List of Excluded Individuals/Entities.<sup>31</sup> The memorandum called this network of databases the "Do Not Pay List".

#### ***The Improper Payments Elimination and Recovery Act of 2010 (IPERA)***

IPERA of 2010 consolidated IPIA of 2002 and the Recovery Audit Act of 2002<sup>32</sup>. It retained their core provisions, expanded the scope of recovery audits, and codified portions of EO 13520. The most important aspects of IPERA were:

- Established how agencies should estimate improper payments.
- Established risk factors for agency heads to account for when analyzing improper payments.
- Established requirements on how agencies are to comply with IPERA.

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<sup>29</sup> Obama, Barack. "Memorandum: Finding and Recapturing Improper Payments." Federal Register, Vol. 75, No. 49. March 10, 2010.

<sup>30</sup> Obama, Barack. "Memorandum: Enhancing Payment Accuracy Through a "Do Not Pay List"." Federal Register, Vol. 75, No. 120. June 18, 2010. Page 1.

<sup>31</sup> Obama, Barack. "Memorandum: Enhancing Payment Accuracy Through a "Do Not Pay List"." Federal Register, Vol. 75, No. 120. June 18, 2010. Page 1.

<sup>32</sup> "Section 831 of the National Defense Authorization Act for Fiscal Year 2002" P.L. 107-107, 107<sup>th</sup> Cong. November 26, 2002.

### ***The Improper Payments Elimination and Recovery Improvement Act of 2012 (IPERIA)***

IPERIA also made some minor changes to IPERA. It codified the Do Not Pay List in EO15230, renamed it the Do Not Pay (DNP), and required all agencies for every program to use DNP for all payments. It required OMB to designate a high-risk program list to focus efforts on these programs. IPERIA also added new guidance for OMB to establish new standards for sampling payments. It prohibited agencies from relying on self-reporting by recipients for estimates, required agencies to report all improper payments in their estimates including those payments recovered or in the process of being recovered, and required agencies to include payments to employees in their estimates.

### ***The Federal Improper Payments Coordination Act of 2015***

The Federal Improper Payments Coordination Act of 2015 improved the data sharing of the DNP between agencies and expanded its use to states, including any state contractor or agent, and the judicial or legislative branches of government. It also required federal agencies to review the death records maintained by the Social Security Administration.

### ***The Payment Integrity Information Act of 2019***

The Payment Integrity Information Act of 2019 reorganized and revised all the improper payments laws. It allowed OMB to establish one or more pilot programs and required OMB to update its plan for improving the Social Security Administration's death data. Finally, it established an interagency working group on payment integrity that includes state and local government officials.

The federal government has put significant time and resources into developing federal improper payment laws both within the executive and legislative branches. Over seventeen

years, Congress has passed five major laws to detect and curb improper payments in federal programs. Regardless of the efforts by Congress and other means, it is impossible to stop every improper payment in every program.

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*“Every single taxpayer dollar that is misallocated takes precious resources away from programs meant to serve our nation’s most vulnerable.”*

U.S. Senator Orrin Hatch (R-Utah)

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## **United States Government Accountability Office Reports**

Between 2009 and 2013, estimated improper payments fluctuated in amount, but have been increasing since 2013. For 2019, improper payments for Medicaid and the Children’s Health Insurance Program (CHIP) reintegrated eligibility into the Payment Error Rate Measurement (PERM) which contributes to the increase. Eligibility had been part of the PERM

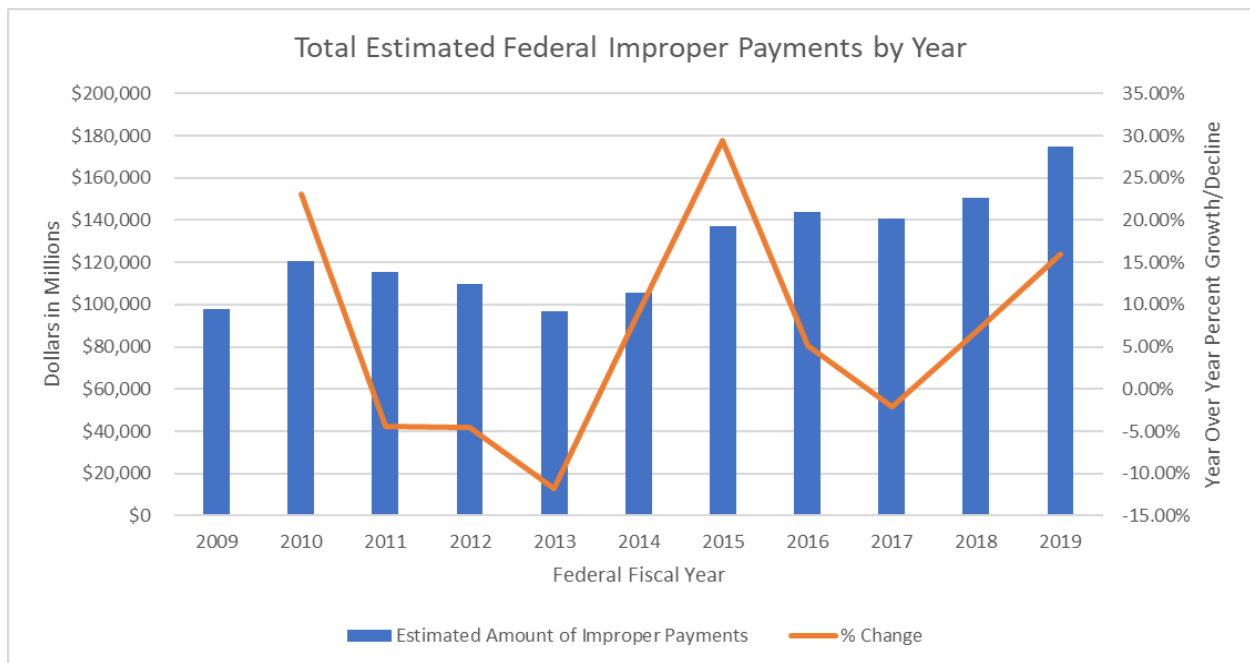


Figure 1 Data from PaymentAccuracy.gov operated by the U.S. OMB

reporting prior to 2015, but the Obama administration suspended it from federal fiscal years 2015 – 2018. PERM is the process used by the Centers for Medicare and Medicaid (CMS) to conform to federal improper payment laws and to calculate improper payment error rates for Medicaid and CHIP.<sup>33</sup>

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<sup>33</sup> <https://www.cms.gov/Research-Statistics-Data-and-Systems/Monitoring-Programs/Medicaid-and-CHIP-Compliance/PERM/lawsandregulations>.

Root causes of improper payments are grouped into the following major categories by

OMB:

- Insufficient documentation to determine,
- Administrative or process errors,
- Inability to authenticate eligibility,
- Program design or structural issues,
- Medical necessity,
- Failure to verify data, and
- Other reasons.<sup>34</sup>

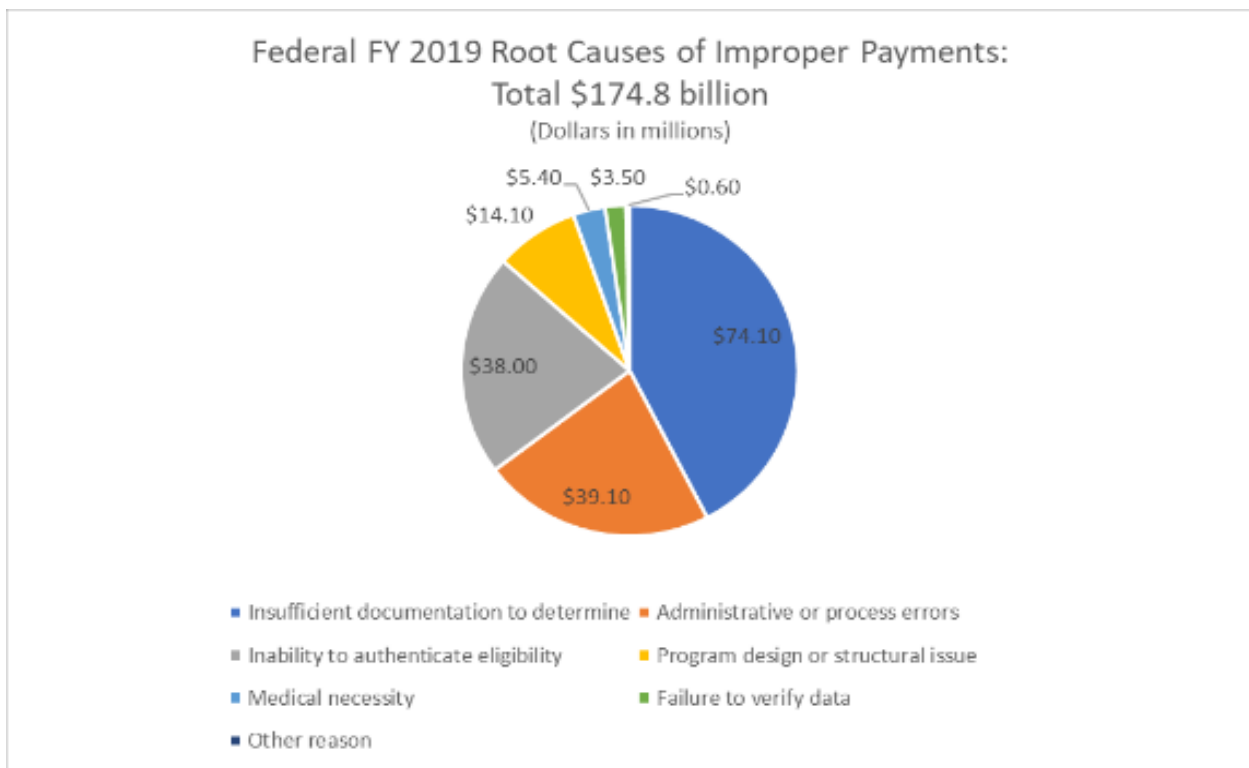


Figure 2 Data as Reported by U.S. GAO.

<sup>34</sup> "Payment Integrity: Federal Agencies' Estimates of FY 2019 Improper Payments." United States Government Accountability Office. March 2020. Pages 24-25.



Insufficient documentation to determine is the largest category representing 42.4 percent of all improper payments in FY 2019.<sup>35</sup> Insufficient documentations encompass payments made without the required supporting documentation. Administrative or process errors are 22.4 percent of improper payments and are caused by incorrectly entering data, misclassifying data, or incorrectly processing applications or payments.<sup>36</sup> The first two categories alone represent 64.8 percent of all improper payments made in FY 2019 and indicate large amounts of correctable errors within federal programs.

Since October 1999, the Government Accounting Office (GAO) has produced numerous reports to Congress about improper payments.<sup>37</sup> For 2019, the GAO reported improper payment estimates for fiscal year 2019 totaling approximately \$175 billion, which is an increase of \$24 billion over the previous fiscal year. Sixty-nine percent or \$121 billion was concentrated in three areas: (1) Medicaid, (2) Medicare, and (3) Earned Income Tax Credit.<sup>38</sup> Of these three, Medicaid is the only shared program with state governments and represented \$57.4 billion or 14.9 percent of program expenditures.<sup>39</sup>

Coordination between state governments and the federal government had focused on technical assistance and guidance from the federal government to state governments in order for states to estimate improper payments.<sup>40</sup> The GAO found the most effective tool for state

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<sup>35</sup> "Payment Integrity: Federal Agencies' Estimates of FY 2019 Improper Payments." United States Government Accountability Office. March 2020. Page 24.

<sup>36</sup> "Payment Integrity: Federal Agencies' Estimates of FY 2019 Improper Payments." United States Government Accountability Office. March 2020. Page 24.

<sup>37</sup> "Financial Management: Increased Attention Needed to Prevent Billions in Improper Payments." United States Government Accountability Office. October 1999.

<sup>38</sup> "Payment Integrity: Federal Agencies' Estimates of FY 2019 Improper Payments." United States Government Accountability Office. March 2020. Page 7.

<sup>39</sup> "Payment Integrity: Federal Agencies' Estimates of FY 2019 Improper Payments." United States Government Accountability Office. March 2020. Page 20.

<sup>40</sup> "Medicaid: State Efforts to Control Improper Payments Vary." United States Government Accountability Office. June 2001. Page 5.

governments to engage in improper payment detection and reduction efforts is to make it part of federal program requirements.<sup>41</sup> The GAO survey data showed that 50 states and the District of Columbia estimated improper payments for federal programs when the federal programs required, 29 states voluntarily entered a pilot program to estimate improper payments on a limited set of federal programs, and 11 states started their own initiatives.<sup>42</sup>

The GAO's *Standards for Internal Control in the Federal Government*, also known as the Green Book, cites five components of internal control to detect and reduce improper payments:

- Control Environment
- Risk Assessment
- Control Activities
- Information/Communication
- Monitoring

Out of these five components, states use risk assessment and computer related techniques to detect and reduce improper payments.<sup>43</sup> Further, 15 states are utilizing recovery audits by contracting with an auditing firm on a contingent fee or auditing by using in-house audits. States reported recovering \$180 million in FY 2003 and \$155 million in FY 2004.<sup>44</sup>

29 CFR Section 97.51 (Later Disallowances and Adjustments) and 42 CFR Section 430.42 (Disallowance of Claims for FFP) permit federal agencies to recover federal funds that

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<sup>41</sup> "Improper Payments: Federal and State Coordination Needed to Report National Improper Payment Estimates on Federal Programs." United States Government Accounting. April 2006. Pages 9-11.

<sup>42</sup> "Improper Payments: Federal and State Coordination Needed to Report National Improper Payment Estimates on Federal Programs." United States Government Accounting. April 2006. Page 9.

<sup>43</sup> "Improper Payments: Federal and State Coordination Needed to Report National Improper Payment Estimates on Federal Programs." United States Government Accounting. April 2006. Pages 16-17.

<sup>44</sup> "Improper Payments: Federal and State Coordination Needed to Report National Improper Payment Estimates on Federal Programs." United States Government Accounting. April 2006. Page 19.

were not allowed by states or other entities. Further, the federal government provides a few incentives and disincentives or penalties for reducing improper payments. Only the Food Stamp Program statute provides incentives and disincentives for state governments to reduce improper payments.<sup>45</sup> The federal government requires states to complete a Payment Error Rate Measurement (PERM) Report every three years to determine the improper payment rate for Medicaid and the Children’s Health Insurance Program (CHIP). This report analyzes improper payments through testing claim samples and applying the samples to the entire program. After a state completes its PERM report, the state is required to file a corrective action plan with the Center for Medicare and Medicaid Services (CMS), and then the state is assigned a new improper payment target rate by the federal government. If a state does not meet its target rate for two consecutive PERM Reports, the amount above the targeted payment rate and the actual improper payment rate becomes a disallowance and the state must reimburse the federal government for this amount. To date, the federal government has not applied a disallowance for PERM reports.

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<sup>45</sup> “Improper Payments: Federal and State Coordination Needed to Report National Improper Payment Estimates on Federal Programs.” United States Government Accounting. April 2006. Page 21.

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*“Horror is a reaction; it's not a genre.”*

John Carpenter – Movie Director

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## **Statistical Sampling and Extrapolation**

Extrapolation is “the action of estimating or concluding something by assuming that existing trends will continue, or a current method will remain applicable.” It is impossible for auditors to audit every claim, so under Medicaid, the federal government and states have used statistical sampling to uncover improper payments and apply extrapolation to the entire program.<sup>46</sup>

In 1975, the Seventh Circuit ruled extrapolation to be a valid audit technique and the federal government adopted the ruling a few years later into statute.<sup>47</sup> On January 15, 2020, the United States Court of Appeals for the Fifth Circuit ruled in favor of the Centers for Medicare and Medicaid Services (CMS) allowing CMS to use extrapolation in *Palm Valley Health Care, Inc. v. Azar* (Palm Valley Health Care, Inc. v. Azar, No. 18-41067, 2020 BL 14097 (5<sup>th</sup> Cir. Jan. 15, 2020)).<sup>48</sup> This case specifically shows the impact of extrapolation and how it provides extreme financial risk to subnational governments and final recipients of federal dollars. In the *Palm Valley* case, CMS’s contractor conducted an audit due to Palm Valley’s unusually high submission of claims. The contractor, using CMS’s selected methodology, selected 54 claims to review out of the 10,699 filed during the audit period. The contractor found 29 of the 54 claims were overpayments totaling \$81,681 with an error rate of 53.7%. Penn Valley used the appeals

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<sup>46</sup> Heyeck, Larry. “Medicaid Overpayments: The Use of Statistical Sampling and Extrapolation.” Health Lawyer. 07363443, August 2016, Vol. 28, Issue 6. Page 2-3.

<sup>47</sup> Heyeck, Larry. “Medicaid Overpayments: The Use of Statistical Sampling and Extrapolation.” Health Lawyer. 07363443, August 2016, Vol. 28, Issue 6. Page 3.

<sup>48</sup> Jeffrey Alberg. “Federal Court Upholds CMS’ Use of Extrapolation to Claw-Back Improper Payments.” February 17, 2020.

process and the administrative law judge ruled four of the 29 claims invalid. Using extrapolation, CMS required Penn Valley to pay \$12,589,185. Ultimately, the actual \$81,681 in overpayments ended up costing Penn Valley \$12.5 million in reimbursements to the federal government. As the federal government continues to deficit spend and focus on improper payment policies, subnational governments, and other subrecipients of federal funds must be cognizant of the federal government's use of improper payment recoveries as a revenue source.

Minnesota was recently required to repay the federal government \$73 million because the state was making payments to substance abuse providers in violation of federal law.<sup>49</sup> This happened because Minnesota pays for substance abuse through a consolidated fund of federal and state dollars. The providers should have been paid through state dollars only and not federal dollars. In August of 2019, the Office of Inspector General for the United States Department of Health and Human Services released an audit of Florida's Low-Income Pool Program. The audit showed Jackson Memorial Hospital received \$412 million more than its allowable costs and was required to repay this amount back to the federal government.<sup>50</sup>

The PERM process for Medicaid relies heavily on statistical sampling and extrapolation in determining improper payment rates. It is impossible for either the federal government or state governments to audit every payment made under Medicaid. For example, Pennsylvania's 2019 PERM Report (Figure 3) reflects the impact of extrapolation. For Medicaid's Fee for Service (FFS) program, 75 actual errors were found in 761 audit samples creating an error rate of 22.21%. The error rate for the sample was then applied to the entire program creating the

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<sup>49</sup> Faircloth, Ryan. "Minnesota owes the feds \$48 million for Improper Medicaid Payments." Pioneer Press. August 26, 2019.

<sup>50</sup> Chiedi, Joanne M. "Florida Medicaid Paid Hundreds of Millions to Jackson Memorial Hospital Under Its Low-Income Pool Program." Office of Inspector General, U.S. Department of Health and Human Services. August 2009. Report in Brief.

projected federal dollars in error. This means the actual federal dollars in error from the sample

| <b>Pennsylvania 2019 PERM Report Sample Errors</b> |                           |                                    |  |   |  |
|--|---------------------------|------------------------------------|--|---|--|
| <b>Medicaid Program Component</b>                  | <b># of Sample Claims</b> | <b># of Sample Claims in Error</b> | <b>Sample Federal Dollars in Error</b> | <b>Projected Federal Dollars in Error</b> | <b>% of Total Projected Federal Dollars in Error</b> |
| Medicaid FFS                                       | 761                       | 75                                 | \$90,548                               | \$519,992,086                             | 22.21%   |
| Medicaid Managed Care                              | 40                        | 0                                  | \$0                                    | \$0                                       | 0.00%  |
| Medicaid Eligibility                               | 677                       | 201                                | \$96,160                               | \$1,821,156,133                           | 77.79%   |

Figure 3: Data from 2019 PERM Report for Commonwealth of Pennsylvania and reflects the impact of extrapolation on state financial liabilities.

of \$90,548 was increased to \$519,992,086 in projected federal dollars in error after extrapolation.

While this should be terrifying to state budget analysts, the samples are the key to extrapolation analyses. In Pennsylvania’s 2019 PERM Report, Medicaid Managed Care had 40 sample claims with no claims in error. Had the sample pulled 40 different samples but those sample claims with say 20 errors, the error rate would have been 50 percent. This would have increased the total projected federal dollars in error and the state’s financial liability to the federal government. As shown in figure 3, the Medicaid Eligibility program with 201 errors out of 677 sample claims resulted in \$1.8 billion in projected federal dollars in error.

Medicaid Managed Care is a unique program as the federal government only requires an audit of dollars paid from state government to managed care organizations (MCOs) called capitated payments. These audits are data process reviews not medical reviews.<sup>51</sup> Therefore, Medicaid Managed Care has a smaller sample size and lower payment error rate. The PERM

<sup>51</sup> Office of Financial Management, Centers for Medicare and Medicaid Services. “Payment Error Rate Measurement (PERM) Overview.” January 2014. Page 4. <https://www.cms.gov/Research-Statistics-Data-and-Systems/Monitoring-Programs/Medicaid-and-CHIP-Compliance/PERM/Downloads/PERMOverview.pdf>

report does not reflect the payment error rates of MCOs that make payments to providers or a medical review of these payments as PERM requires for FFS.

Medicaid eligibility reflects how well states verify eligibility of Medicaid recipients in their states. This is new for the 2019 PERM cycle and will establish a new baseline of improper payments for Medicaid after all the state PERM reports are completed in 2021.

Eligibility disallowance is another area covered in PERM reports. Based on Pennsylvania's 2019 PERM report, the total extrapolated dollars for disallowance were \$908,011,385 due to eligibility disallowances.<sup>52</sup> Since eligibility disallowances were not in effect and Pennsylvania met its good faith effort established by Section 1903(u) of the Social Security Act, Pennsylvania will not face repaying the federal government \$908 million.<sup>53</sup> However, CMS expects to recover the federal shares from FFS and managed care overpayments found in error in Pennsylvania on a claim-by-claim basis.<sup>54</sup> Section 1903(u) of the Social Security Act gives the Secretary of Health and Human Services the ability to recover any improper payment over an error rate of 0.03 or 3 percent.<sup>55</sup>

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<sup>52</sup>Centers for Medicare and Medicaid Services. "Notification of RY 2019 Medicaid Improper Payment Rates." November 26, 2019. Page 2.

<sup>53</sup>Centers for Medicare and Medicaid Services. "Notification of RY 2019 Medicaid Improper Payment Rates." November 26, 2019. Page 2.

<sup>54</sup>Centers for Medicare and Medicaid Services. "Notification of RY 2019 Medicaid Improper Payment Rates." November 26, 2019. Page 2.

<sup>55</sup>42 U.S. Code CHAPTER 7—SOCIAL SECURITY, Section 1904(u).

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*“The government solution to a problem is usually as bad as the problem.”*

Milton Friedman

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### **Identified Solutions in Literature**

Much of the research on improper payments focuses on federal agencies, but over almost two decades of work by federal agencies, we can glean best practices that states can adopt to detect, reduce, and eliminate improper payments. The four main steps to reducing improper payments are identify/analyze root causes, preventative controls, detective controls, and collaboration with other entities.<sup>56</sup>

#### ***Four Steps to Reduce Improper Payments***

Uniform guidance cannot be provided for all agencies to follow regarding lowering improper payments.<sup>57</sup> By utilizing the four steps of analyzing root-causes, implementing preventative controls, implementing detective controls, and creating collaboration with other entities governments, it is possible to establish effective tools to reduce and eliminate improper payments. The four steps are listed and discussed below:

| <b>4 Steps to Reducing Improper Payments</b> |  |
|--|--|
| <b>Step 1</b>                                | <b>Root-cause Analysis</b>               |
| <b>Step 2</b>                                | <b>Preventative Controls</b>             |
| <b>Step 3</b>                                | <b>Detective Controls</b>                |
| <b>Step 4</b>                                | <b>Collaboration with Other Entities</b> |

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<sup>56</sup> Beryl Davis, Jim Healy, and Phillip McIntyre. “Strategies to Help Curb Improper Payments.” A Journal of Government Financial Management. Fall 2017. Page 58.

<sup>57</sup> Elizabeth Owens and Carol Jessup. “Federal Improper Payments: An Overview.” Journal of Financial Management, Summer 2014. Page 16.



- **Root-cause analysis** is the first step in addressing improper payments.<sup>58</sup> Analyzing the root causes of improper payments helps inform management and policymakers what weaknesses are resulting from inadequate internal controls or program integrity policies. In addition, root-causes at the agency or program level must be identified to inform management and policymakers on further actions needed to eliminate improper payments.
- **Preventative controls** are internal controls used by agencies to ensure correct payments prior to the payment being made. These controls are important because they avoid the need to recover dollars, and most importantly increase public confidence in program administration.<sup>59</sup>
- **Detective controls** are internal controls used on the back end once payments are made. These controls review payments to identify improper payments and provide the information on why they were made.<sup>60</sup>
- **Collaboration with other entities** has been imbedded in most federal improper payment statutes. Since states administer federal programs, like unemployment compensation and Medicaid, and subnational governments are recipients of billions in federal expenditures, it is beneficial for collaboration between these stakeholders to take place to improve program administration.<sup>61</sup>

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<sup>58</sup> Beryl Davis, Jim Healy, and Phillip McIntyre. "Strategies to Help Curb Improper Payments." A Journal of Government Financial Management Fall 2017. Page 58.

<sup>59</sup> Beryl Davis, Jim Healy, and Phillip McIntyre. "Strategies to Help Curb Improper Payments." A Journal of Government Financial Management Fall 2017. Page 58.

<sup>60</sup> Beryl Davis, Jim Healy, and Phillip McIntyre. "Strategies to Help Curb Improper Payments." A Journal of Government Financial Management Fall 2017. Page 58.

<sup>61</sup> Beryl Davis, Jim Healy, and Phillip McIntyre. "Strategies to Help Curb Improper Payments." A Journal of Government Financial Management Fall 2017. Page 58.

Within these four steps to reduce improper payments, the research has further identified best practices. The best practices range from corrective action plans and transparency, to data sharing programs.

### ***Corrective Action Plans***

A corrective action plan (CAP) is a step-by-step plan of action developed to achieve targeted outcomes to resolve identified errors as well as:

- Identify the most cost-effective actions that can be implemented to correct the causes of errors.
- Improve processes or methods so outcomes are more effective and efficient.
- Achieve measurable improvement.
- Eliminate repeated deficient practices.

Once root causes are identified, agencies should develop corrective action plans designed to eliminate improper payments.<sup>62</sup> State governments are required under federal law to develop corrective action plans for Single Audits, Food Stamp Program, Medicaid and CHIP.<sup>63 64 65</sup> For Medicaid and CHIP, corrective action plans must address all errors in the PERM and all other deficiencies identified. Also, for Medicaid and CHIP eligibility, an evaluation of whether state actions will reduce eligibility errors and improper payments must be reduced.

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<sup>62</sup> Wendy Morton-Huddleston, Calandra Layne, and Hudson Riehle. "Marching On! Sustaining Improper Payments Prevention Program." *Journal of Government Financial Management*, Winter 2016-2017. Page 14.

<sup>63</sup> 7 CFR § 275.17 - State corrective action plan.

<sup>64</sup> 42 CFR § 431.992 - Corrective action plan.

<sup>65</sup> 2 CFR § 200.511 - Audit findings follow-up.

## *Transparency*

IPERIA requires federal agencies to publicly:

- Disclose improper payments estimates.
- Identify the methodology for calculating improper payments.
- Identify improper payment reduction targets.
- Publish improper payment risk-assessments for all programs deemed high-risk.
- Place improper payment amounts in their Agency Financial Report (AFR).<sup>66</sup>

The publishing of improper payments helps to inform the public of the issues surrounding program integrity and internal controls as well as hold government agencies accountable for meeting improper payment reduction targets. While the federal government has robust transparency requirements, subnational governments do not usually disclose improper payments since such disclosures would essentially expose large and difficult to fix state problems that may have potentially adverse political repercussions.<sup>67</sup> For example, the State of Kentucky has a statute which requires state agencies to report their improper payments to the Legislative Research Commission.<sup>68</sup> Neither the state agency nor the Legislative Research Commission is required to publicly disclose reported amounts of improper payments. Further, federal statutes governing corrective action plan mandates for state governments do not require states to publicly disclose their corrective action plans.

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<sup>66</sup> Wendy Morton-Huddleston, Calandra Layne, and Hudson Riehle. "Marching On! Sustaining Improper Payments Prevention Program." *Journal of Government Financial Management*, Winter 2016-2017. Page 13.

<sup>67</sup> Edward Sheen. "Eliminating Improper Payments: A Review, Framework for Action and Seven Fundamental Questions." *Journal of Government Financial Management*, Winter 2006. Page 46.

<sup>68</sup> KRS 45.237 (7). Establishment of internal controls and preaudit procedures for state agencies -- Collection of improper payments -- Referral of certified debts by agency or local government to Department of Revenue -- Information to be provided to State Treasurer.

## *Data Sharing Programs*

On November 20, 2009, President Barack Obama signed Executive Order 13520 – Reducing Improper Payments, which directed federal agencies to start the improper payment process of identifying and recovering improper payments.<sup>69</sup> He followed up this executive order on June 18, 2010 with a memorandum creating the Do Not Pay List that required the Office of Management and Budget to coordinate with other agencies to utilize current lists maintained by the federal government in order to reduce improper payments through pre-payment verifications.<sup>70</sup> The Do Not Pay List was codified as the Do Not Pay Program under the United States Treasury in the IPERIA of 2012. Most of the literature points to Do Not Pay as a resounding success and its use is a leading recommendation for combating improper payments.<sup>71</sup>

72 73

In February 2020, the State of Oregon released an audit of Oregon Health and Human Services Program’s use of the Do Not Pay program.<sup>74</sup> The audit report cited several positive outcomes of the state utilizing the Do Not Pay program:

- Generated a return on investment of \$286 in savings for every \$1 spent.
- Identified over \$790,000 in financial benefits.

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<sup>69</sup> Obama, Barack. “Executive Order 13520 – Reducing Improper Payments.” November 20, 2009.

<sup>70</sup> Obama, Barack. “Memorandum: Enhancing Payment Accuracy Through a “Do Not Pay List”. June 10, 2010.

<sup>71</sup> Bryan Reece Clark. “Kafkaesque Dangers: IPERIA, Do Not Pay, and the Government’s New Fight Against Improper Payments.” Iowa Law Review, Vol 102, 1719, Pages 1721, 1756.

<sup>72</sup> Danny Werfel and Jeffery C. Steinoff. “Are You Combat Ready to Win the War Against Improper Payments?” Journal of Government Financial Management, Summer 2014. Page 21.

<sup>73</sup> Elizabeth Owens and Carol Jessup. “Federal Improper Payments: An Overview.” Journal of Financial Management, Summer 2014. Page 14.

<sup>74</sup> Garber, Will, Furnish, Teresa, Green, Ian, and Faulkner, Sheila. “Using the U.S. Treasury’s Do Not Pay System for Health and Human services Programs Will Save Taxpayers Money.” Oregon Audits Division, Secretary of State, State of Oregon. February 2020.

- Reported it took ten days of staff time with a cost of \$2,750 in salary and benefits to generate the information.
- Identified data quality issues for the federal government and state government.
- Identified potential compliance issues.
- Identified internal control weaknesses.
- Verified effectiveness of state integrity programs.

The Do Not Pay program has great merit in helping subnational governments to reduce improper payments. Under PIIA of 2019, the Do Not Pay program was given expressed permission to coordinate with state governments. The Do Not Pay program requires the involvement of an interagency working group including input from state administered federal programs.

The Public Assistance Reporting Information System (PARIS) is a data analytics system administered by the Administration for Children and Families (ACF) in order to improve integrity within the Temporary Assistance to Needy Families (TANF) program, the Food Stamp

| <b>State</b> | <b>Number of Potential Avoidable Cases for SNAP, TANF &amp; Medicaid</b> | <b>Improper Payment Avoidance</b> | <b>Cost</b> | <b>Net Savings</b> |
|--------------|--|-----------------------------------|-------------|--------------------|
| Colorado     | 4715   | \$9,377,443                       | \$103,909   | \$9,273,534        |
| Kansas       | 1925   | \$1,986,284                       | \$66,725    | \$1,919,559        |
| Maine        | 800  | \$1,329,167                       | \$51,733    | \$1,277,432        |
| New Mexico   | 1870   | \$3,776,010                       | \$66,005    | \$3,710,005        |

*Figure 4: 2008 Annualized estimates of improper payment avoidance and net savings related to closing all potential SNAP, TANF and Medicaid avoidable cases.*

program (SNAP), and Medicaid.<sup>75</sup> PARIS is designed for data matching and information exchange between state governments and between the federal government and state governments. It is comprised of three matches: Interstate Match, VA Match, and Federal Match.<sup>76</sup> The Interstate Match uses social security numbers of public assistance consumers to determine if an individual is enrolled in multiple states.<sup>77</sup> The VA Match provides the states information from the United States Department of Veterans Affairs (VA) on state public assistance consumers, who are receiving income and medical assistance payments from the VA.<sup>78</sup> The Federal Match provides the states with data from the U.S. Department of Defense (DOD) and the Office of Personnel Management to verify if consumers are receiving payments or federal health coverage from the DOD or federal employment.<sup>79</sup> PARIS is a voluntary program and states can opt in one or all three of the data match systems.<sup>80</sup> When a state receives a match, the state is expected to send the match hits for follow up investigation to appropriate agency employees.<sup>81</sup> These match hits inform states of consumers who have not informed their former state of residence they have moved to a different state or cases of fraud when the consumer is deliberately attempting to receive government benefits from multiple states.<sup>82</sup> As of

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<sup>75</sup> "Evaluation to Determine the Effectiveness of the Public Assistance Reporting and Information System." Health Systems Research, Inc., an Altarum Company. June 30, 2007. Page 1.

<sup>76</sup> Evaluation to Determine the Effectiveness of the Public Assistance Reporting and Information System." Health Systems Research, Inc., an Altarum Company. June 30, 2007. Page 1.

<sup>77</sup> Evaluation to Determine the Effectiveness of the Public Assistance Reporting and Information System." Health Systems Research, Inc., an Altarum Company. June 30, 2007. Page 1.

<sup>78</sup> Evaluation to Determine the Effectiveness of the Public Assistance Reporting and Information System." Health Systems Research, Inc., an Altarum Company. June 30, 2007. Page 1.

<sup>79</sup> Evaluation to Determine the Effectiveness of the Public Assistance Reporting and Information System." Health Systems Research, Inc., an Altarum Company. June 30, 2007. Page 1.

<sup>80</sup> Evaluation to Determine the Effectiveness of the Public Assistance Reporting and Information System." Health Systems Research, Inc., an Altarum Company. June 30, 2007. Page 1.

<sup>81</sup> "Public Assistance: PARIS Project Can Help States Reduce Improper Benefit Payments." Report to the Ranking Minority Member, Committee on Governmental Affairs, U.S. Senate. U.S. General Accounting Office. September 2001. Page 5.

<sup>82</sup> "Public Assistance: PARIS Project Can Help States Reduce Improper Benefit Payments." Report to the Ranking Minority Member, Committee on Governmental Affairs, U.S. Senate. U.S. General Accounting Office. September 2001. Page 5.

February 2020, 38 states participate in the VA Match<sup>83</sup>, all 50 states participate in the Interstate Match,<sup>84</sup> and 45 states participate in the Federal Match<sup>85</sup>.

While the data points to the successes of PARIS, there also have been weaknesses of PARIS. For example, states are not completing the follow up case investigations, which means state governments are going through the expense of using PARIS for the data match, but they are not following up to resolve cases.<sup>86 87</sup> Another identified weakness is documenting follow up activities to capture outcomes and provide accountability to the program.<sup>88</sup>

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<sup>83</sup> <https://acf.hhs.gov/paris/veterans-affairs-match-2020>.

<sup>84</sup> <https://www.acf.hhs.gov/paris/interstate-match-2020>.

<sup>85</sup> <https://www.acf.hhs.gov/paris/federal-match-2020>.

<sup>86</sup> "Public Assistance: PARIS Project Can Help States Reduce Improper Benefit Payments." Report to the Ranking Minority Member, Committee on Governmental Affairs, U.S. Senate. U.S. General Accounting Office. September 2001. Pages 18-19.

<sup>87</sup> Evaluation to Determine the Effectiveness of the Public Assistance Reporting and Information System." Health Systems Research, Inc., an Altarum Company. June 30, 2007. Page 44.

<sup>88</sup> "Public Assistance Reporting Information System Cost-Benefit Analysis." Altarum Institute. 2008. Page 37.

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*“You will not be able to understand the performance of your company without good quality data to measure it.”*

Pearl Zhu

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## **Analysis and Findings**

This qualitative research paper was designed after a thorough review of federal improper payment laws, policies, and implementation strategies. The goal is to inform state policymakers on what federal improper payments entail and how they impact state governments. The concepts of this research paper focused on the historical development of federal improper payment laws, United States Government Accountability Office Reports (GAO) on improper payments and scholarly research.

Federal improper payment laws, while well intentioned and needed, push down enforcement and the responsibility of administering the laws to the managers of federal programs while creating financial liabilities for these same entities. The federal government, within the constructs of federal improper payment laws, has attempted to develop working groups with stakeholders to elevate the discussion and prioritize the reduction of improper payments at the subnational level. However, we have not seen a robust policy discussion of improper payments at the subnational level. Outside of state auditors or internal state agency discussions, state governments have not created or aligned policies to mitigate their financial risks or created a governance structure for state agencies to address and comply with federal improper payment requirements.

The development of substantial federal improper payment laws by Congress during the past decade reflects a change of policy from solely reporting improper payments to addressing root causes of improper payments as well as providing accuracy in calculating improper



payments. Through the statutory history of federal improper payment laws, transparency has always been at the forefront of legislative decisions to inform the public of the scope of improper payments and to ensure there is accountability in addressing improper payments. The development of improper payment laws also reflects the ability of federal agencies to better assess and calculate improper payments. While federal improper payments laws were originally developed under IPIA of 2002 as a government-wide approach, these laws were narrowed to high-risk programs as federal agencies and Congress realized that addressing billions of dollars in improper payments simultaneously throughout the entire federal government was impossible.

Research at the subnational level on improper payment policy and programs is lacking, especially since these entities face the requirements of administering federal programs and are recipients of billions of dollars in federal grants. Analyzing the effectiveness of public integrity programs at the state level will help inform policymakers and citizens about the effectiveness of federal improper payment laws and create a better understanding of federal and subnational interactions.

As reflected in the Minnesota case referred to earlier, state governments are liable for misappropriations by subrecipients that violate the provisions of federal laws and regulations. State governments have a fiduciary responsibility to ensure the subrecipients of federal dollars that have been allocated or awarded federal contracts or grants, use the funds according to federal guidance. The Minnesota and Jackson Memorial Hospital cases are reminders to state policymakers and subrecipients of federal dollars, that federal disallowances can have severe financial consequences.

Literature research demonstrates the success of data sharing programs between the federal agencies and between the federal government and state governments. Programs like

DNP and PARIS have shown success in uncovering improper payments, saving taxpayers' dollars, and verifying the success or failure of internal controls at the federal and state levels of government. Data sharing among the GAO reports and scholarly research reflects a universal recommendation for addressing improper payments throughout government. Data sharing helps clarify data issues between states and with the federal government. This ensures more accurate data which drives better outcomes.

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*“Sunlight is the best disinfectant.”*

Associate Justice William O. Douglas

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## **Recommendations**

Based on the literature review from the GAO reports and research, there are several recommendations for the federal government and state governments to adopt.

### ***Federal Government Recommendations***

Federal laws can recover federal dollars spent by subnational governments; the subnational governments reimburse the federal government using the tax revenues they collect. This is a large hammer, but it is a hammer the federal government rarely uses. The threat is real, however, for the federal government to utilize its disallowance capabilities. At some point, the federal government needs to either utilize all its tools or repeal them. At the same time, the federal government has provided shared savings policies when subnational governments save federal dollars as an incentive for the subnational governments to focus on reducing improper payments. The Federal False Claims Act (FCA) update in 1986 provided a ten percent increase in the state Federal Medical Assistance Percentage (FMAP) when calculating FCA settlements as an incentive for state governments to adopt a federally compliant state-level FCA<sup>89</sup>. The federal government also provides savings sharing provisions within the Food Stamp Program as an incentive for state governments to reduce improper payments and reduce costs. Federal Food Stamp Program is administered by states, but state governments currently do not have any financial stake in the program. These shared savings policies can easily be adopted within federal improper payment laws and within all federal programs administered by state

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<sup>89</sup> <https://oig.hhs.gov/fraud/state-false-claims-act-reviews/>.

governments to provide financial incentives to address improper payments and reduce costs. When revising improper payment laws, the federal government needs to apply the correct amount of incentives and disincentives for subnational governments to take federal improper payment laws seriously.

Federal data sharing programs like DNP and PARIS have been successful and low-cost solutions to improper payment reductions. Federal policymakers should work to have every state utilize these programs through outreach programs and outcomes assessments. Sharing successful results from data sharing programs will further encourage states to utilize the systems. As the PARIS program research indicates, the federal government must create uniform reporting criteria to track and calculate costs and benefits from these programs.

The federal government also must close audit gaps in the PERM reports. FFS is being phased out as a delivery system for Medicaid and is being replaced by managed care.<sup>90</sup> PERM reports need to expand their sampling to include payments made from MCOs to providers and not just from the state to MCOs. This will capture the real costs of Medicaid improper payments and close an audit gap.

### ***State Government Recommendations***

State governments are the key stakeholders in the federal government's efforts to curb improper payments. The federal government should continue its policy of establishing working groups with states and other stakeholders to improve improper payment reduction policies and programs.

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<sup>90</sup> Hinton, Elizabeth; Rudowitz, Robin; Stolyar, Lina; and Singer, Natalie. "10 Things to Know About Medicaid Managed Care. Kaiser Family Foundation. October 29, 2020.

### *State Improper Payment Statues*

State governments should align state laws with federal improper payment laws. State agencies that expend federal dollars are already under federal mandate to align with federal laws and policies. Therefore, it makes sense to align state-only dollars for improper payments as well. Further, state policies can better drive cost/benefit models. The literature for PARIS shows there needs to be a greater effort in calculating costs and savings. State level improper payment laws will allow states and the federal government to reduce recovery efforts by ensuring payments are accurate before they are made. Alignment of federal and state improper payment laws is a crucial step in reducing improper payments.

State improper payment laws can be adopted government wide. Alternatively, a state can begin with agencies already operating under federal improper payment laws and then expand the scope of a state improper payment law to capture all state agencies over time. Regardless of how a state implements its state improper payment laws, it should start with risk assessments and focus its efforts on the high-risk programs first. Current federal risk assessments on federal programs can assist states in determining which programs are high-risk.

State improper payment laws should also include a working group, at minimum, consisting of the state's budget officer, state treasurer, state auditor, state inspector general, bipartisan legislative appointments (preferably two from each chamber representing each political party), director of state internal auditors, chief information officer, representatives from subrecipients like hospitals, non-profits, local governments, school districts, and the auditing firm contracted to complete the state's Comprehensive Annual Financial Report (CAFR) and Single Audit. This working group should evaluate the effectiveness of internal controls, review annual and quarterly improper payment data, establish annual improper payment reduction

benchmarks for state agencies or specific programs, and analyze the effectiveness of data sharing between all levels of government.

### ***Internal Controls***

State governments should align their internal controls to the GAO's *Standards for Internal Control in the Federal Government* through executive action or codifying it in statute, which would be preferable. A unified internal control system between the federal government and state government will only help to inform decision makers on internal control weaknesses, that has been and will continue to be a leading cause of improper payments. Internal controls are key to implementing a successful improper payment reduction program. The goal of improper payments reduction laws is for government agencies to get the payments correct the first time.

### ***Data Sharing***

As the literature points out, PARIS and DNP are two of the most successful programs in addressing improper payments. State governments should ensure all state agencies that make expenditures using federal dollars are also utilizing DNP. State agencies which operate Medicaid programs should be using all data match functions of PARIS. Further, state governments should statutorily mandate state agencies follow up on outcomes of data sharing programs and should report on their effectiveness through annual cost-benefit analysis including recommendations to improve these programs.

State governments also collect substantial data including medical claims data, death certificates, and many other forms of data. State data sources should be used to develop data sharing programs at the state level modeled after DNP. This will further help to ensure accurate data and increased data resources available to expand on the successful federal data sharing programs.

### ***Subrecipient Contracts***

State governments are liable for federal dollars that pass-through state government to subrecipients. If there is a federal disallowance creating a financial liability, state governments need to ensure their contracts with subrecipients of federal dollars clearly document that the subrecipients are liable for disallowances created by their errors. This appropriately apportions financial risk of federal improper payments laws between the state governments and subrecipient entities receiving federal funds. Proper contracts increase the financial risk of subrecipients to ensure they are compliant with federal laws and regulations thereby providing additional accountability.

### ***Legislative Oversight***

The state legislative branch must engage in oversight operations of federal improper payment laws by holding agencies, especially those with corrective action plans, accountable and meeting federally established improper payment reduction targets. If state agencies know the legislative branch is invested in addressing improper payments, the agencies will escalate their interest as well. Legislative oversight also means there will be more transparency about improper payments created through public hearings, where the public will be more exposed to and better informed about improper payments. These efforts will help shape public support for improper payment policies.

### ***Transparency***

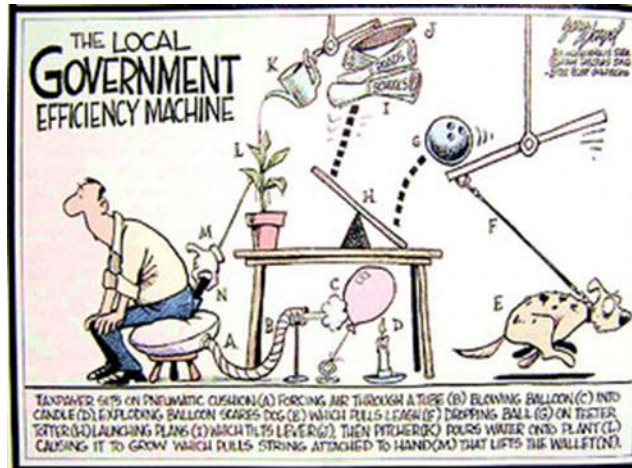
Transparency is the best cure for most government oversight problems. The federal government provides robust websites like [www.PaymentAccuracy.gov](http://www.PaymentAccuracy.gov) and the U.S. GAO websites where you can easily search for all reports on improper payments. State governments, however, are not posting their improper payment reports on their agency websites, excluding the

corrective action plans from their Single Audits. Not one Cycle 1 state posted their PERM report. Even the federal government has yet to formally release state PERM reports.

This lack of state government transparency around federal improper payment reports and data should not come as a surprise, but it shows the extent government agencies will go to not acknowledge a problem. Lack of transparency prevents state government from obtaining viable solutions to existing improper payment problems. While there may be numerous reasons why state agencies want to hide federal improper payment reports, state legislatures should adopt statutes requiring the public release of this information on state agency websites. Further, state budget offices should create a one-stop website for the collection and disclosure of agency improper payment reports, corrective action plans, and status of the corrective action plans.

As state governments have not even begun to contemplate improper payment policies or deployed comprehensive strategies for combatting improper payments, they are creating unnecessary financial risk for their taxpayers. Combined, these simple recommendations can put state governments on a path to reducing improper payments and ultimately reducing their financial risk. States must act quickly to catch up to the federal government on establishing appropriate policies, as the federal government continues its focus on reducing improper payments.





## Conclusion

An April 11, 2019 poll of Americans showed only 17 percent of the public say they trust the federal government to do what is right.<sup>91</sup> While public trust is up about ten percent since its low point on April 21, 2011, overall public trust in the federal government has declined since October 15, 1964 by 77 percent.<sup>92</sup> As the federal government reports on the estimated \$175 billion of improper payments made in FY 2019, the public trust decreases as the public sees inefficiencies and government waste. Governments must continue to work on internal controls to ensure government programs are as efficient and effective as possible.

As the literature has shown, there is no silver bullet that will magically eliminate improper payments. Governments, both the federal and subnational, must make their eradication of improper payments a priority and dedicate resources to implement the needed policy changes. Subnational government policymakers must understand their state’s financial liability created by federal improper payment laws and how those improper payments are created. This financial risk can create a budget busting financial liability that a state will have to pay requiring

<sup>91</sup> Pew Research Center. “Public Trust in Government.” April 11, 2019. <https://www.pewresearch.org/politics/2019/04/11/public-trust-in-government-1958-2019/>.

<sup>92</sup> Pew Research Center. “Public Trust in Government.” April 11, 2019. <https://www.pewresearch.org/politics/2019/04/11/public-trust-in-government-1958-2019/>.

policymakers to make draconian decisions on tax rates, expenditure reductions, and/or service delivery reductions. Subnational governments should establish sound improper payment policies now, before the federal government starts to utilize its claw back provisions as a revenue source.

Ultimately, improper payments are about doing it right the first time. Correcting mistakes always costs more time and money than doing it right from the beginning. Recovering public dollars pits the government against its citizens, which is not the ideal position for government to be in especially if the government is in error. Governments reducing improper payments means they will have less recovery costs and will mitigate its impact on the impact of improper payments on its own citizens.

Improper payments can also lead to increased fraudulent activity. If government internal controls are not detecting payment errors, those same flaws can be exploited to commit fraud against the taxpayers. Fraud in government programs means taxpayers must pay twice for the same services, one time for the fraud and one time for the actual services.

While this paper has identified several ways for governments to reduce improper payments, future research is needed in several areas:

- Statistical method the federal government has established to set audit samples.
- Cost/Benefit analysis of the Do Not Pay program.
- How the Do Not Pay program is being implemented in subnational governments.
- Cost/Benefit analysis of recovery efforts in the federal and subnational governments.
- Cost/Benefit analysis of recovery audits in the federal and subnational governments.
- Correlation of the increase of improper payments with the expansion of government services and programs.
- Effectiveness in PERM reports in reducing improper payments.

- Effectiveness of state corrective action plans in reducing improper payments.
- Analysis of the growth rate of improper payments and whether governments are improving their success in identifying improper payments.

These areas of research will better inform policymakers and citizens on improper payments.

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