

**PRESERVING INTEGRITY, PREVENTING
OVERPAYMENTS, AND ELIMINATING FRAUD
IN THE UNEMPLOYMENT INSURANCE SYSTEM**

HEARING

BEFORE THE

**COMMITTEE ON FINANCE
UNITED STATES SENATE**

ONE HUNDRED TWELFTH CONGRESS

FIRST SESSION

—————
JUNE 22, 2011
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**PRESERVING INTEGRITY, PREVENTING
OVERPAYMENTS, AND ELIMINATING FRAUD
IN THE UNEMPLOYMENT INSURANCE SYSTEM**

WEDNESDAY, JUNE 22, 2011

U.S. SENATE,
COMMITTEE ON FINANCE,
Washington, DC.

The hearing was convened, pursuant to notice, at 10:08 a.m., in room SD-215, Dirksen Senate Office Building, Hon. Max Baucus (chairman of the committee) presiding.

Also present: Senators Stabenow, Carper, Cardin, Hatch, and Burr.

Also present: Democratic Staff: Russ Sullivan, Staff Director; Amber Roberts, Tax-Exempt Policy Advisor and Research Assistant; and Diedra Henry-Spires, Professional Staff. Republican Staff: Bryan Hickman, Special Counsel; Jim Lyons, Tax Counsel; and Aaron Taylor, Professional Staff Member.

**OPENING STATEMENT OF HON. MAX BAUCUS, A U.S. SENATOR
FROM MONTANA, CHAIRMAN, COMMITTEE ON FINANCE**

The CHAIRMAN. The committee will come to order.

Clement Stone, the great American businessman and philanthropist, once said, "Have the courage to say 'no.' Have the courage to face the truth. Do the right thing because it is right. These are the magic keys to living your life with integrity."

These words provide helpful wisdom today as we face the truth and the challenges in our Nation's Unemployment Insurance program. In these difficult economic times, Unemployment Insurance, or UI, provides a critical lifeline to millions of Americans who lost jobs through no fault of their own. UI ensures that families can still put food on the table, gas in the car, and keep roofs over their heads while looking for the next job.

The beneficiaries of this program are workers. They have worked. They want to work, and they will work again. In a recession, Unemployment Insurance spending increases. This funding gives a temporary boost to the economy that helps keep both families and businesses afloat and helps stabilize our economy.

However, the substantial job losses of this Great Recession stretched Unemployment Insurance programs nationwide. The strain has led to an increase in improper UI payments due to errors, inefficiencies, and even fraud. To do the right thing and create solutions this program needs, we must first understand why these

overpayments occur, and that is why we are holding today's hearing.

In 2009, the Department of Labor reported \$11.4 billion in improper UI payments. Last year, that number spiked to more than \$17 billion. With leadership from this committee, Congress passed legislation last year to curb abuse and waste in the unemployment system. This law allows the Treasury Department to recover overpayments from those who do not report their earnings. It also eliminated the 10-year time limit the government had to collect overpayments.

The law requires employers to report the very first day new hires begin working. This helps determine whether workers are receiving improper unemployment compensation benefits. Although this legislation is helping curb these inefficiencies, we need to do more, clearly. The leading cause of UI overpayments is claimants who have returned to work, but continue to claim benefits.

The second-largest cause is errors verifying that unemployed workers meet all the requirements to be eligible for UI benefits. The third-largest cause of overpayments is workers who fail to fulfill State requirements. These requirements can include an active search for work or registration with the State Unemployment Service.

The UI program is too important for this money to be wasted. We need to work together to develop solutions to end these overpayments. This must be a combined effort. It includes beneficiaries, employers, States, the private sector, and the Federal Government. Right now everyone's budgets are tight, families are having trouble making ends meet, and we clearly need to fix our Federal budget problems. There is not a penny to waste.

The administration's most recent budget includes valuable ideas to address many of the program's issues. In this proposal, those who defraud the system will be required to pay a 15-percent penalty and return the wrongly collected funds. Employers would be held accountable for overpayments resulting from extremely untimely responses to inquiries about their employees' work history.

State governments will be encouraged to stop overpayments before they happen, not just to collect after the fact. And the Federal Government would have improved tools to recoup losses due to fraud and waste. While the administration's proposal contains some good ideas, there should also be a role for the private sector, including data processing upgrades and other private-sector ideas that seem to be quite efficient.

States and the private industry have devised systems to reduce overpayments and streamline the program. I also want to applaud Senator Coburn, who has worked in this area. I generally applaud my colleagues' efforts and look forward to working with each of them to develop solutions.

So, as we address these challenges, let us have courage, let us face the truth, and let us do right by the millions of Americans who are counting on us to preserve the integrity of our Unemployment Insurance system.

[The prepared statement of Chairman Baucus appears in the appendix.]

The CHAIRMAN. Senator Hatch?

**OPENING STATEMENT OF HON. ORRIN G. HATCH,
A U.S. SENATOR FROM UTAH**

Senator HATCH. Thank you, Mr. Chairman. I appreciate you having today's hearing on this very important topic.

The CHAIRMAN. Thanks.

Senator HATCH. Fourteen million Americans are unemployed. The official unemployment rate is 9.1 percent, but that actually understates how bad things really are. An article in *U.S. News and World Report* this week concludes that the unemployment rate is in fact closer to 16 percent if you include under-employment. The official numbers ignore people who have stopped looking for work or have not applied for a job in more than 4 weeks, or who have found only part-time work but who really want to work a full-time job.

You might think that, after the failure of its stimulus program, the administration would be doing everything within its power to help our private businesses to create jobs, but you would be wrong. In fact, the administration in some cases is actually eliminating jobs.

Consider what the administration just did in my State of Utah. The administration just announced that it is reneging on a long-standing bipartisan agreement to allow uranium mining in southern Utah and northern Arizona. By doing so, the administration is blocking 4,000 new jobs and \$30 billion in economic activity.

Now, think of that. A year has passed since the so-called Recovery Summer, and the economy is still on the ropes. We need all the jobs we can get. Yet, the administration is content to deny 4,000 jobs in Utah, and that is just in one corner of the State. This also means we have to obtain our uranium overseas.

Four thousand jobs. That is 4,000 families who would have seen their Great Recession come to an end. But not now. We have a President who says he wants to create jobs, but as I said Monday on the Senate floor, I have never seen a bigger disconnect between a President's stated goals and his actions.

Now, Mr. Chairman, I would like to have a copy of that floor statement included in the record.

The CHAIRMAN. Without objection.

[The statement appears in the appendix on p. 56.]

Senator HATCH. With high unemployment and an anti-business administration stifling job creation, the subject of Unemployment Insurance is before us again. Unfortunately, addressing these issues is more important than ever. As unemployment remains high, the amount of taxpayer dollars spent on Unemployment Insurance also remains high. In 2007, before the recession, we spent \$32 billion on Unemployment Insurance. In 2010, the figure was \$156 billion.

Now, here is the kicker: at a time of trillion-dollar deficits and with the country hurtling toward a full-blown debt crisis, the Department of Labor estimates that 11 cents of every unemployment dollar spent by the government is spent in error. Eleven cents. That means in 2010, over \$17 billion was simply wasted.

Now, we cannot afford this level of waste under any circumstances. Let us put this waste in this one program in perspective. Just last month, the CEOs of the five largest oil companies

were brought before this committee, with cameras rolling, over a tax subsidy for energy companies.

The proposal to eliminate that subsidy would have saved \$2.1 billion per year. Many on the other side of the aisle touted that as a significant proposal for bringing our trillion-dollar deficits to heel. Yet here in this case—Unemployment Insurance programs—we have \$17 billion in waste in 1 year alone.

That is why, today, we are here to discuss program integrity. When we talk about program integrity, we mean the management principles the Federal Government and the State governments employ, or should employ, to ensure that those who qualify for Unemployment Insurance receive it and that those who do not qualify for benefits do not receive it. In short, we are here to discuss ways to shrink an 11-percent payment error rate that is costing taxpayers \$17 billion every year.

One problem is the sheer complexity of the Unemployment Insurance system. Too many in Washington are masters of bureaucracy with little regard for the costs involved. The administration of Unemployment Insurance programs at the Federal and State level cost American taxpayers over \$5 billion in 2010. States need flexibility, not Washington mandates. States should be free to share their best practices, learn from one another, and adopt what works.

As is often the case, the Utah way has resulted in an error rate much lower than the national average. I look forward to hearing how that was achieved and what kind of improvements Utah plans to make for the future. Another problem that must be addressed is the substantial compliance costs the Unemployment Insurance system places on employers who are saddled with substantial paperwork and tax planning burdens.

For example, not every departing employee qualifies for Unemployment Insurance, but many file claims anyway because it costs nothing to file a claim, and they believe they have nothing to lose. But this puts the burden and the expense of fighting unjustified claims on the employer.

Then there is the problem posed by people who qualify initially for Unemployment Insurance, but then cease to remain qualified and continue receiving a check anyway. Maybe they have stopped looking for work as they are required to do, or maybe they have returned to work after a layoff and not reported it.

Indeed, there are many reasons why an unemployment check might be paid in error, and sometimes fraud is involved. But whatever the reason for an erroneous payment, given the millions of people in the system today and the billions of dollars being spent each year, we cannot tolerate an 11-percent error rate. We cannot continue to waste billions and billions of dollars every year.

Once again, I want to thank you, Mr. Chairman, for holding this hearing. That will conclude my remarks.

The CHAIRMAN. Thank you, Senator.

[The prepared statement of Senator Hatch appears in the appendix.]

The CHAIRMAN. We are fortunate today to have witnesses who have firsthand knowledge of the UI system and how it works. First we will hear from Jane Oates, Assistant Secretary for Employment and Training, U.S. Department of Labor. Our second witness is Ms.

Kristen Cox, who is Executive Director of the Utah Department of Workforce Services in Salt Lake City. Perhaps, Senator, you may want to say a few words about Ms. Cox at the appropriate moment.

Senator HATCH. I would be glad to do it.

The CHAIRMAN. And we will also hear from Commissioner Paul Trause, Washington Employment Security Department of Olympia, WA. Finally, we will hear from Mr. Mike Cullen, managing director of On Point Technology in Oak Brook, IL.

Senator Hatch may want to say a few words about Ms. Cox at this point.

Senator HATCH. Why don't I introduce Kristen Cox?

The CHAIRMAN. All right.

Senator HATCH. For the past 4 years, Kristen Cox has served as Utah's Executive Director of Workforce Services. Now, in this capacity, Ms. Cox is responsible for overseeing the operations of 12 divisions, which encompass Federal and State programs, including workforce development, public assistance, and of course Unemployment Insurance.

Under her leadership, Utah has been at the forefront of advancing new processes and technology in order to improve program integrity for Unemployment Insurance. And, most importantly, she has gotten results. Utah's improper payment rates consistently fall below the national average, and the State has been recognized by the Department of Labor as a top performer among medium-sized States.

So we want to welcome you, Ms. Cox. We appreciate your willingness to be here in Washington to testify here today, and we look forward to hearing from all of you. Certainly I look forward to hearing from everybody here, but especially you.

The CHAIRMAN. Thank you, Senator.

We will begin with Ms. Jane Oates.

Ms. Oates?

STATEMENT OF JANE OATES, M.Ed., ASSISTANT SECRETARY FOR EMPLOYMENT AND TRAINING, DEPARTMENT OF LABOR, WASHINGTON, DC

Ms. OATES. Thank you, Senator, very much. Good morning to you and to the ranking member. I do not see Senator Burr here, but I like him much better on our beloved other committee, and Senator Carper and Senator Cardin. Lovely to see you.

Thanks for this opportunity to talk to you a little bit about our legislative proposal to improve integrity in the UI system.

Senator Hatch, I could not agree with you more. Reducing the UI improper payment rate is getting our highest attention, not only at the Department of Labor but also with the administration. I applaud the committee. You could not have better witnesses than you have with the two Commissioners here. They represent real innovation in the States, and they are critical partners to us in this.

I want to thank the committee specifically for enacting improvements to the National Directory of New Hires and the Treasury Offset Program in the last Congress. These two important integrity proposals that we had advocated for and you supported so strongly are already giving States new tools to improve prevention, detection, and collection of improper payments.

I would like to just take a moment to say that some States have gotten some early success. Michigan, New York, and Wisconsin have already recovered approximately \$25 million, thanks to the TOP program.

Louisiana and South Carolina have substantially reduced their employment service registration errors—in Louisiana, a 90-percent reduction, and in South Carolina a reduction of more than 75 percent since you enacted those new provisions. Texas has improved its operational procedures, reducing benefit year earnings errors by nearly 50 percent.

Even though the UI program has a longstanding commitment to ensuring its financial integrity, unfortunately the UI improper payment rate has increased from 2009 to 2010. During the most recent reporting period, the improper payment rate was, as Senator Hatch said, 11.2 percent, of which 10.6 percent represents overpayments.

Based on our analysis of the cause of overpayments, we know that approximately one-half of the overpayments is controllable. The four main reasons for improper payments in the UI program are, one, payments are made to individuals who have returned to work and continue to claim benefits. We can fix that. The second is a failure of employers or their third-party administrators to provide timely and adequate information on the reason for an individual's separation. The third is claimants' failure to meet the State's work search requirements. The fourth is a failure to register claimants with the State's employment service pursuant to State law.

It is important to understand the impact that the recession has had on the UI improper payment rate. Entering the recession, the average UI claims increased by 3.2 million, or 120 percent, in only a 1-year period. Many State workforce agencies struggled to keep up with the increased workloads and were compelled to utilize integrity staff to process claims instead of focusing on improper payments.

Today, however, States are actively working with the Department to aggressively implement strategies to bring down the UI improper payment rate. While States are striving to improve their integrity functions—and the Department has many initiatives under way to support States' efforts to reduce the UI improper payment rate—additional statutory authority and resources are needed to enhance our collaborative efforts and to continue to improve the payment accuracy.

To this end, the Department sent the draft Unemployment Compensation Program Integrity Act of 2011, or lovingly, the Integrity Act, to Congress on June 11. Here are some of the key provisions.

It provides new dedicated resources by permitting States to use up to 5 percent of recovered overpayments and delinquent contributions for critical State integrity activities.

It requires a penalty of at least 15 percent on outstanding fraudulent benefit overpayments, similar to the penalty employers face for delinquent tax payments. States may use these funds for integrity activities or for the payment of benefits. Most States have these provisions in their State law but allow the funds to be used for other purposes frequently having nothing to do with UI purposes.

Third, it requires that employers' accounts be charged if an overpayment is the employer's fault due to failure to respond timely or adequately to a State's request for information.

Lastly, it improves the usefulness of the National Directory of New Hires for overpayment detection by requiring employers to report individuals who are rehired after being separated from employment for at least 60 days.

We believe that the Integrity Act provides a balanced approach with a huge benefit. Not only will UI integrity improve, it will save money. The Department estimates this legislative proposal would cut spending by \$2.5 billion over 10 years and, because that would lead to lower taxes for employers, produce net savings to the government of \$556 million over that same period. We think it is benefit-added.

Before closing, I would like to mention a few of the many integrity activities we are working on with our State partners. These activities include reducing improper payments through prevention and early detection of eligibility problems and speeding claimants' return to work by conducting Reemployment and Eligibility Assessments, REAs.

Number two, receiving more timely and accurate separation information from employers or their representatives through the use of an automated State Information Data Exchange System, SIDES. Finally, working with States to more efficiently combine the use of the National Directory of New Hires and automated claimant notification processes and other claimant messaging tools to prevent improper payments when a claimant has returned to work.

Again, let me thank you for this opportunity to talk to you. Thank you for your terrific partnership on UI, and we will certainly, after the rest of the testimony, appreciate any of your questions.

The CHAIRMAN. Thank you very much, Ms. Oates.

[The prepared statement of Ms. Oates appears in the appendix.]

The CHAIRMAN. Ms. Cox, you are next.

Ms. COX. Just a quick question. It is 5 minutes, and there is like a light that goes off or something?

The CHAIRMAN. That is what happens.

Ms. COX. So, can you do like an auditory cue?

The CHAIRMAN. You got it.

Ms. COX. All right. That is great. I could wax eloquent for hours.

The CHAIRMAN. What would you prefer? One minute before the five?

Ms. COX. Yes, about a minute. Just say a minute.

The CHAIRMAN. Right.

Senator HATCH. You can see how perspicacious we all are out here in Utah.

The CHAIRMAN. Perspicacious? That is a big word.

Ms. COX. I know. I will have to look it up.

Senator HATCH. For you Democrats, I guess. [Laughter.]

The CHAIRMAN. I am just as stunned that you know the word! [Laughter.]

Senator HATCH. I know a few others too, and I am going to use them in a minute. [Laughter.]

The CHAIRMAN. All right, Ms. Cox.

**STATEMENT OF KRISTEN COX, EXECUTIVE DIRECTOR, UTAH
DEPARTMENT OF WORKFORCE SERVICES, SALT LAKE CITY,
UT**

Ms. COX. We have a lot to cover in a short period of time, so I am going to focus specifically on some best practices in Utah. Let me just start off with, our ultimate goal in our division with UI is to get people back to work. Program integrity efforts, operational excellence, trust fund management, all of those we want to align to make sure people get the right benefits in a timely manner, but ultimately so we can move them into the workforce. That is critical because it drives a lot of our efforts. But today I know it is on program integrity, so I will limit my comments to that.

We have great return on investment with integrity efforts. For every dollar in investment, we return about \$5.50. We have great outcomes with that. A side note: with reemployment initiatives, if I can reduce my duration by 1 week, I can save \$20 million, so actually it is a bigger return on investment.

We have some concerns with the legislation. I have pointed out a couple in my written testimony. I will just say we certainly applaud the overall intent to enhance program integrity efforts. We have a great track record. It is a priority for us. This bill, though, does not provide a lot of value added and is actually, in a couple of areas, more restrictive. It would tie our hands from really using our resources in a way that would be most beneficial for our State. I will leave that for the written testimony for more detail, or questions.

Let me go through a few of our best practices. One starts with a very hard line around fraud in our State. The legislation talks about a 15-percent penalty for fraudulent overpayments; ours is 100 percent. It is never written off. Fraud overpayments can result in denial of future benefits for up to 49 weeks (13 weeks for the first week of fraud and 6 weeks for each additional week of fraud) and may also include criminal prosecution and publication of the convictions in the press and on our website. It starts with a very aggressive stance on fraud.

We probably have a higher fraud rate than other States because our laws around this are so regressive. We do take it very seriously. There is a lot of ambiguity on what fraud means because States define it very differently, and so that needs to begin with a hard stance on how you actually go after fraud.

Other best practices that we use—and the Assistant Secretary spoke to some of those—cross-matching is huge. Ninety-five percent of our prevention and detection activities come from automated cross-matching. We right now have 12 cross-matches in place. We will have another 6, with a total of 18 by next year. We have had huge success with that.

We automate a lot of our activities around red flags we get from wage data matching or New Hire Directory matches. We can automate that and send automated notices to employers about concerns or red flags. They can provide us with the information electronically. We can then run the rule and send a correspondence to the client so we can expedite detection very quickly.

New Hire Directory, both at the State and the national level, has been huge for us. We love it. We will say, though, that having it

nationally is great, but, at the State level, 60 to 70 percent of our new hires come from our State New Hire Registry, and it is really important for States to actually implement and have enforcement around employers using that system. You can have it, but, if employers do not engage, you cannot get the data you need. So that is really important for us.

We look at SIDES, which is big. We are the first State to actually operate SIDES, which is a way to get standard separation information, which can be a big cost, 20 percent in Utah, for overpayments. It has been a big success. We are actually going live on Tuesday with TALX, which represents 25 percent of the employers across the country. It has been a big advantage for us as well, so we certainly applaud the efforts around SIDES.

We are looking also at some pilots around looking at what we call automatic clearinghouses from banks, so we can look at debits or withdrawals or trends that may suggest somebody is getting dual benefits or also receiving a paycheck. We are in pilot mode and proof of concept, working with the Department of Labor. We think that is going to be a very promising concept as well.

And then finally, our worker profiling system. That tends to be a manual system for most States. We have made it all online, integrated it into our eligibility review system, so we can make sure people are compliant, looking for work, and looking at their work registration requirements.

Some challenges we have: what we call the TOP program, the Treasury Offset Program. Again, fantastic, but they are applying it differently to UI as compared to food stamps. We also run the food stamp program, and we have some flexibility in food stamps that we do not have in UI, and that is making it more difficult to execute that as well as we think we could.

The CHAIRMAN. You are doing just great. I will let you have an extra minute.

Ms. COX. Is that a minute?

The CHAIRMAN. I will let you have an extra minute. You have another minute.

Ms. COX. But now 10 more seconds because you ate into my time. [Laughter.]

The CHAIRMAN. Right. I can tell you are a good enforcement officer. [Laughter.]

Ms. COX. In a minute, I will be very quick.

But the most important thing for us in terms of challenges are around, how do you measure integrity? I would be happy to answer questions. I do not necessarily think that the Benefits Accuracy Measurement, or BAM, is the only measure you can really look at, and that is where the improper payment numbers are coming from right now.

The current overpayment protection rate that is currently used for a lot of States really incentivizes to detect and establish payments later because you use that in your denominator, and that can really skew how States are incentivized to do early detection. So some of the areas around, how do you measure quality and integrity, that will drive your system.

If the measurements are not relevant to a State, we will put them on a shelf and report them for compliance activities and use

our own measurements to drive our business. So to have measurement systems across the board, I know they are looking at it. I think the Department of Labor is going in a good direction. We do have some concerns around some of their proposed rules right now on this, but we do appreciate them trying to move with early detection in some areas like that.

So, I am happy to answer any other questions after the testimonies.

The CHAIRMAN. Thank you very much.

[The prepared statement of Ms. Cox appears in the appendix.]

The CHAIRMAN. Mr. Trause?

**STATEMENT OF PAUL TRAUSE, COMMISSIONER, WASHINGTON
EMPLOYMENT SECURITY DEPARTMENT, OLYMPIA, WA**

Mr. TRAUSE. Thank you, Chairman Baucus, Ranking Member Hatch, and members of the committee. I am Paul Trause, the Commissioner of Washington's Employment Security Department.

Washington State has one of the healthiest trust funds in the Nation. This results from the commitment of our Governor, State legislature, businesses, and workers to support that fund. Our experience in Washington State convinces me that preserving a level playing field for business and ensuring appropriate benefit payments for workers is essential to the credibility and health of our trust fund.

Today I would like to talk with you about three things: our efforts, first, to detect and deter fraud; second, to collect benefit overpayments and unpaid taxes; and third, but equally important, to prevent fraud. The vast majority of overpayments and unpaid taxes are due to errors and confusion, not fraud. Nevertheless, strong fraud detection is critical to integrity.

Washington State's legislature and Governor have worked to improve our laws and provide the framework required to pursue those employers and claimants who seek to defraud the system. We have established clearer definitions of employee fraud, as well as a graduated penalty structure for people who commit fraud. We have strengthened our laws regarding employer fraud, including establishing substantial penalties for employers who intentionally evade paying their tax.

We rely heavily on technology to detect claimant fraud. We regularly cross-match UI recipients against a wide variety of databases to identify individuals who are ineligible, concealing wages, or not engaging in a legitimate job search. These matches are responsible for uncovering half of all the fraud-related claims. For this reason, we strongly support expanding the New Hire Database to include rehires.

We also mine the data available to us to uncover organized fraud. For example, we identify instances where the same phone is used to file multiple claims, multiple claimants are claiming from a single address or post office box, or the same Social Security number is being used in different claims. We aggressively promote toll-free hotlines on our website to solicit tips.

Our investigative efforts have been very successful, with just under \$16 million in fraud overpayments detected in 2010, and we have also brought a number of prosecutions. We uncover employer

fraud primarily through audits. Again, just as with workers, the vast majority of employers acts responsibly. The department has a very active audit program to identify employers who are not paying their share.

In 2006, we moved from scheduling employers randomly for audits to using database comparisons, unexplained changes in information reported to us, past audit experience, and staff knowledge, to schedule our audits. We also have forged close working relationships with other State taxing agencies to identify unregistered businesses or businesses operating underground.

As a result of Washington's enhanced audit program, we found 270 percent more misclassified workers and 345 percent more unreported taxes in 2010 than in 2006. We believe actively publicizing successful fraud prosecutions can deter future fraud, and we work very closely with the news media to ensure that these cases do get publicized.

But collection provides meaning to detection. We work aggressively to collect overpayments using existing databases to locate debtors, payment plans to encourage voluntary compliance, and where that fails, legal tools such as liens and garnishment to compel payment. We also have a waiver process to forgive debts where the claimant is not at fault and collection would be against equity and good conscience. We have recently created a dedicated skip-tracing unit that appears to be very successful in finding debtors. Over the past 10 years, we have increased our recoveries by more than 300 percent. Each of our collectors returns over \$30 for each dollar we spend.

I also agree, however, that prevention is as important, if not more important, than detection and collection. We believe that there are three keys to prevention. First, we need better technology. Our benefits computer system is more than 20 years old—we still use COBOL—and our Internet claim system is 11 years old. They interface poorly with each other, lack the ability to catch errors in advance, and frustrate claimants, businesses, and our staff. We urge including technology infrastructure investment in the use of funds reserved for integrity efforts.

The second is education for both employers and claimants. We engage in extensive outreach efforts and offer a voluntary audit review to employers so they can make sure that they are paying the right amount of tax. We closely review all benefit claims to identify common errors, and to educate claimants about what they must do. But again, our ability to change our systems is limited because our technology is so outmoded. Technology infrastructure funding is, for us, absolutely critical.

The third key to preventing fraud is returning people to work quickly. We recognize we will never have the resources available to provide the optimal level of attention to each person. We are working to improve the methods we use to review claimants' job searches, assess their skills within the context of their labor market, and help them better target and carry out their job search.

From a 2009 study, we know that job seekers who use our reemployment services returned to work more quickly and at better wages. It is a highly effective investment, and I would like to thank the Department for its continued support.

In conclusion, we recognize that the integrity of our fund is critical to its solvency. We believe the efforts I described today to detect and deter fraud, to collect benefit overpayments and unpaid taxes, and to prevent fraud are essential to guaranteeing the health of our fund.

Thank you. Of course, I am available for questions.

The CHAIRMAN. Yes. Thank you. Thank you, Mr. Trause.

[The prepared statement of Mr. Trause appears in the appendix.]

The CHAIRMAN. Mr. Cullen?

**STATEMENT OF MIKE CULLEN, MANAGING DIRECTOR,
ON POINT TECHNOLOGY, INC., OAK BROOK, IL**

Mr. CULLEN. Thank you, Chairman Baucus, Ranking Member Hatch, distinguished members of the committee. Thank you for your continued interest in this important topic and the opportunity to testify before you again today.

I am Mike Cullen, managing director of On Point Technology, a company focused entirely on Unemployment Insurance technology solutions. For over 15 years, On Point solutions have enabled 17 States to find and collect improperly paid benefits.

Over the past year, On Point has visited nearly half the State workforce agencies in the country. What we have seen is a core of professionals dedicated to protecting the critical program, but lacking the tools required to do the job. Today, 90 percent of the Unemployment Insurance systems operate on technology created before the personal computer was invented. Imagine that! Investigators are pursuing over \$17 billion in overpayments from last year alone using pen and paper, scissors, and glue sticks.

It should surprise no one that such a system has produced an improper payment rate that stands as the worst ever recorded by the Department of Labor. To put this in perspective, since the beginning of the recession approximately \$40 billion has been lost through improperly paid benefits. Interestingly, this \$40 billion is roughly equivalent to the total outstanding trust fund debt owed by all State workforce agencies, debt that has yet to be repaid.

We propose four specific initiatives to increase the transparency of the integrity problem and enhance the accountability of the program's stakeholders, including employers, State workforce agencies, and the Department of Labor.

Importantly, each of our proposals can be implemented without increasing budgets at either the State or Federal level. Foremost, we must provide professionals modern technology and productivity-enhancing tools. Based upon our experience, one-time investments in software for State integrity programs can easily return \$10 for each dollar invested.

The Department of Labor has designed a sophisticated integrity strategy that offers a tremendous potential return on investment. The strategy cannot succeed unless States first increase their capacity to investigate improper payments. Installing better software for investigation operations will yield the greatest gains in minimizing fraud, reducing waste, and saving money.

Second, we endorse recommendation by the State Chamber of Commerce and the National Employer Group that the Department dedicate \$30 million annually from existing administrative funding

toward a competitive integrity grant process. We believe Congress should require the Department of Labor to report annually on the results of each integrity investment. In addition, we believe 10 percent of administrative dollars should be reserved for integrity activities that protect the Federal dollars from waste, fraud, and abuse should Congress ever adopt another extension of Federal UI benefits.

Third, we urge the creation of a public/private partnership with the sole focus of examining and recommending tools to detect and stop overpayments earlier. This initiative must leverage existing organizations and focus on ideas which can yield an immediate impact by reducing improper payments within 6 months. Too often, strategic plans have been adopted that reference multi-year project strategies. The historical mind-set needs to change from long-term studies to short-term solutions.

Finally, in concert with the U.S. Department of Labor and State workforce agencies, we encourage Congress to consider a long-term legislative solution. In this context, the proposed Unemployment Compensation Program Integrity Act sets forth a number of excellent ideas. In particular, we endorse the use of 5 percent of recovered overpayments to support integrity operations. Critically, these funds must augment existing integrity funding rather than providing States funds to divert to other uses.

Providing a consistent self-supporting funding stream rather than occasional supplemental grant opportunities establishes UI system integrity as a true priority. This is the third Congress that will consider this legislation. With a \$40-billion problem, the time to act is now.

In closing, we must act to preserve the integrity of the UI system to ensure its continued viability for those in need. Fortunately, we are in a position to strengthen UI trust funds and to help ease tax burdens employers across America are facing today. Aligning funding priorities and investing in proven solutions will return precious dollars to the UI system to ensure it remains a vital lifeline for millions of American workers.

Thank you again for the opportunity to testify. Of course, I am available for any questions that you might have.

The CHAIRMAN. Thank you, Mr. Cullen.

[The prepared statement of Mr. Cullen appears in the appendix.]

The CHAIRMAN. Thank you, Mr. Cullen. Your first statement was a bit stunning. Could you repeat it, please? The one you said about, 90 percent—if I understood it correctly—of UI work is done—

Mr. CULLEN. I will repeat it.

The CHAIRMAN. Repeat the statement, please.

Mr. CULLEN. Yes, I will. The statement I made was that today 90 percent of the Unemployment Insurance systems operate on technology created before the personal computer was invented. We just heard from Washington that they are on old COBOL programs. Can I elaborate just a little bit?

The CHAIRMAN. Yes, please.

Mr. CULLEN. In July of 2010, the National Association of State Workforce Agencies did a study on the age of the Unemployment Insurance technology systems. They found that, in the benefits system, the average age is 22 years old. The oldest system out there

is 42 years old. They found tax systems where the average age was 21 years old, and the oldest system out there was 41 years old. These systems are old, they are aging, and they have been stressed beyond belief in the current recession.

The CHAIRMAN. I would like to ask Ms. Oates, do you agree with Mr. Cullen's assessment?

Ms. OATES. I would not argue about the—I do not know the accuracy of the facts. I am sure they are accurate; Mark, you are terrific at this. But this is the number-one problem for States. I think everyone would agree—

The CHAIRMAN. But do you think that is basically accurate, his first statement that he gave? Is that basically correct?

Ms. OATES. I think it is basically correct. Yes, sir.

The CHAIRMAN. Ms. Cox, do you think it is basically correct?

Ms. COX. Not in my State.

The CHAIRMAN. But other States. Maybe not Utah, but—

Ms. COX. I do hear there are problems, and hopefully we can talk about that and talk about the funding. More money is not always the answer. Part of it is how States design their systems, if they are centralized or they are still very manual.

The CHAIRMAN. All right. I appreciate that.

Mr. Trause, do you basically agree?

Mr. TRAUSE. Yes, I do.

The CHAIRMAN. All right. Do you all agree that is a problem?

Ms. COX. It is a problem.

The CHAIRMAN. All right. Now we have to find the solution. Frankly, I am a bit stunned at that statement. I am a bit surprised that we do not have a program—Mr. Cullen has one generally—to address the problem, find a solution, with dates, benchmarks, and targets for getting the job done. The error rate is much lower than our current, say, 10 percent or 11 percent, whatever it is. You said that half of the problem is controllable. That means about half of, what, \$17 billion? So we have \$8 billion that is controllable.

Ms. OATES. Is controllable. Yes, sir.

The CHAIRMAN. So my one question is, do you have benchmarks and data and a time frame within which to get that half that is controllable? If so, what are they? That is, what are the dates and what is the plan, in addition to the legislation that you have described? Essentially, how are you going to get that \$8 billion, and what is a reasonable date?

Ms. OATES. Well, we already have started, and I would be happy—

The CHAIRMAN. What is a reasonable date to get that \$8 billion?

Ms. OATES. Well, it is up to the States, Senator, so it is very difficult—

The CHAIRMAN. I am asking you, what is your program?

Ms. OATES. We have an aggressive plan to reduce it with the 11 largest States. That has already started. We have, as we said, begun to recapture using TOP—

The CHAIRMAN. If you could give us a date. Is it 1 year? Two years? What is a reasonable time frame?

Ms. OATES. I think we could get close to the \$8 million figure in 2 years.

The CHAIRMAN. Two years.

Ms. OATES. I hope that we will do it faster than that.

The CHAIRMAN. All right.

What about the other half that is not controllable? Why is that not controllable?

Ms. OATES. Well, there are factors that are out of the ability for us to control. I mean, the things that are controllable, Senator, are things like people who continue to claim after they have been re-employed. We can put work together, and we have already started doing that with States.

The pie chart that each of you got attached to my testimony, each of our States has gotten that same pie chart to talk about, in the whole world of their overpayments, what percent would be work search, what percent would be folks who are returning to work and still claiming, what are slow or inaccurate responses by employers? Those are the things that we think we can control.

Work search, of course, is much more difficult because, how do you, in a world where we no longer do face-to-face claims, where we have gone to online and telephonic claims, make sure when someone tells us that they have searched for a job that they really have?

The CHAIRMAN. I would just like to ask a bit of the different approaches here.

Ms. OATES. Yes.

The CHAIRMAN. As I understand it, Ms. Cox, Utah has a 100-percent penalty provision for fraud, whereas Washington basically requires the person who commits fraud to forfeit 26 weeks of benefits. I think those are different approaches. I would just like a little discussion of which of the two seems to work. They both work apparently, because I think both of your States have done a pretty good job. But if you were to recommend to other States, which of those two, or some combination, or a third approach they should pursue, what would that be? I will start with you, Ms. Cox. We do not have a lot of time here, but if you could, very briefly.

Ms. COX. Sure. I think that the larger the penalty when it is fraud—not necessarily just an overpayment if no fault—the higher the better from our stance. This has also lined up with some of our Supreme Court decision rulings and State statute, so a lot of it is governed by State statute, obviously, and where the legislature wants to take this. But 15 percent, or 10 percent, or zero for me just is not stringent enough if it is true fraud, and we have to send a very strong and clear message, really creating a culture that does not tolerate that in our State.

The CHAIRMAN. All right. Mr. Trause, do you think 26-week forfeiture works as well?

Mr. TRAUSE. We use a graduated approach, Senator, where the first time a person is responsible for fraud, it is a 26-week disqualification. The second time it is 52 weeks and a 25-percent penalty. The third time it is 52 weeks and, I believe, a 50-percent penalty.

The CHAIRMAN. All right.

Mr. TRAUSE. That works very well for us. We prefer that to a harsher original penalty.

The CHAIRMAN. I appreciate that.

I probably missed it, but what is the error rate or overpayment rate in your two States?

Ms. COX. Our operational rate is about 5.3 and—

The CHAIRMAN. I am sorry. A little closer to the microphone, please.

Ms. COX. Our operational rate is 5.3, and our BAM rate is 8.1 percent. But again, if you look at your BAM rate compared to your Benefit Payment Control rate, our BPC detects twice as much as our actual BAM rate. I think that is a point of discussion. But the BAM rate that DOL uses may, on fraud issues, underestimate—at least in Utah, it underestimates what we are actually detecting.

The CHAIRMAN. All right.

Mr. Trause?

Mr. TRAUSE. We are very similar. We also have our collection ratio, like hers, that would indicate that there are issues with the way the BAM rate is working for us.

The CHAIRMAN. All right. My time has expired.

Senator Hatch?

Senator HATCH. I want to thank you, Mr. Chairman.

Ms. Cox, States address UI program integrity with varying degrees of success. Some States simply do not go far enough in identifying fraud and overpayments. I am sure that in some States it is a question of resources, in others it is likely a question of priorities.

Utah, it seems, has taken advantage of almost every opportunity to improve the program integrity in its UI system. Now, you mentioned in your testimony that Utah was the first State to implement the State Information Data Exchange System, or SIDES, program. Please tell the committee about Utah's experience with SIDES and what you think of its potential to prevent benefit overpayments.

Ms. COX. Well, ambiguity around separation issues for Utah accounted for 20 percent of our overpayments. That was largely due to employers submitting either inaccurate information or information that was not complete. So SIDES was developed, and the Department of Labor obviously was instrumental in this, to ensure that there is a standard template for submitting separation information, primarily geared for large employers, although small employers can access it as well. I think that is an opportunity to move forward.

Our experience to date is about almost 100 percent of the separation information that we get from SIDES is accurate, and our rework time is down by 50 percent because we are not having to follow up with the employers and collect information. So overall, in terms of really utilizing that and reducing overpayments because of separation issues and expediting the process, it has been fantastic. It is one of those things in infrastructure and technology that, if we use our resources correctly, we can get a lot of bang for our buck.

Senator HATCH. Thank you.

Mr. Cullen, in your testimony you have outlined the need to improve the use of technology in the UI system. I agree with many of your observations. I note that Utah has taken advantage of many of the options that you have noted in your testimony. In your estimation, how many States are using outdated and inefficient systems both to process UI payments and to enforce program integrity requirements, and what specific differences have you observed

between those States that use outdated processes and those that use more advanced technology?

Mr. CULLEN. I would say that probably a good 80 percent of the States are using outdated technology, even though I said 90 percent was based on technology such as COBOL, mainframe, old technology that has been around for years. Some States have done some improvements to the front end of the process to give them better access to the data, but I would say a good 80 percent are well out of date.

The differences that we see between those that have either tried to improve the technology systems that they have or have not done anything is the use of automation to handle the large workload that sits out there. We go to visit a State, they talk about the increasing claims we have heard about here this morning. With the increasing claims is a concurrent increase in overpayments, even if they stay relatively the same.

The ability of the staff to handle that large volume of work manually is limited by the number of resources they can throw against it. But when you use technology and you are able to automate some of those processes and you are able to automate them in line with the State's law and regulation, you see dramatic improvement in terms of the volume of work handled, the consistency of the decisions that come out of it, and the accuracy of the work.

Senator HATCH. Thank you.

Section 4 of the Department of Labor's proposed legislation would prevent States from removing charges to an employer's UI account that resulted from overpayments if the overpayments were the result of the employer's failure to provide accurate and timely information requested by the State.

Now, it seems to me that employers have a built-in motivation to avoid charges to their UI accounts. That being the case, additional penalties, particularly penalties imposed at the Federal level, may be unnecessary. It is my understanding that in many States, information collection is extremely inefficient.

I have heard of examples where some States require employers to provide documents within 10 calendar days after the agency sends a request, yet the requests are sent by regular mail, leaving employers with very little time once they have received the request to provide a timely response. Are there newer technological innovations that can streamline information submission, and would this not be a better way to approach the problem of untimely data?

Mr. CULLEN. Yes, I think there are. I have to say that the integrity legislation has been sent to Congress for a number of years, and so some of the original provisions are still in there. The Department of Labor has worked hard on the SIDES project to resolve exactly that problem.

Let me defend the States really quickly for just a second. I mean, they are under pressure to make payments in a timely fashion to those who are unemployed and get that money to them, and so they have to restrict the time period that employers do have to respond. They try to be very reasonable about it, but they do have timeliness gauges that they have to meet.

SIDES is intended to address that other issue, and that is, can you get the information more quickly to the State so they can take

action on it, can you get it more accurately, and can you avoid the situation where an employer provides an incomplete or an incorrect response by adding edits into that automated system? So, can we get past the mailing dilemma? Yes. Is SIDES one of the ways on the separation information to get past it? It certainly is. But what it takes, though, is participation by all States and participation by employers to make it economically effective.

Senator HATCH. Thank you, Mr. Chairman.

Ms. COX. Senator, may I add one comment to that?

Senator HATCH. Sure.

Ms. COX. Right now, we started doing electronic notifications and really creating transparency on our customer side, and almost 75 percent of them are opting in to electronic correspondence. We are doing the same now for employers so we do not have to rely on snail mail. We have only 1,500 employers up right now. We have not marketed it broadly yet because we are finishing converting all of our additional correspondence. But that way we can immediately send it. We can actually go in to see if they have read it or not so we are not concerned if it has been lost. That gives them much more lead time in meeting any requirements.

Senator HATCH. Thank you.

The CHAIRMAN. Thank you very much. Thank you, Senator.

Senator Carper?

Senator CARPER. Thank you. And to our witnesses, thanks a lot for joining us, and for your testimony and your responses today.

Just to put this in context, \$17 billion is a lot of money. The improper payments reported last year throughout the Federal Government, not including parts of the Department of Defense, not including parts of Medicare, were \$125 billion, mostly overpayments. It is a big problem throughout our government, and certainly is here.

In Medicaid, which the States and Federal Government participate in almost evenly, equally, the potential savings are significant not just for the Federal Government, but also for the States.

Ms. Oates, it is nice to see you. Thanks for your work. Let me ask a question of the other witnesses. I think the administration has laid out a number of steps, additional steps, that the administration thinks should be taken. To the other three witnesses, do you have any comments, pro or con? Do you like what they have suggested? Is there anything you especially like or that you have concerns about that is in the administration's proposal?

Ms. COX. There is a lot of stuff we are already doing that this bill would not really have an impact on, but there is one provision we are concerned with—I think it is in section 3—that talks about, if we collect penalties from an overpayment or fraud, that we would put that into a sub-account around integrity efforts exclusively rather than be able to deposit that currently into our penalties and interest fund. Right now we have flexibility in our P&I fund, and we work with our legislature and Governor to decide at the local level what the local solutions need to be and how those funds should be directed.

As I mentioned earlier, reemployment initiatives are really key for us, so we are now able to use some of those funds to get people back to work, to build infrastructure in those areas, to really sup-

port economic development in our State. Penalties from fraud are a big contributor to our P&I fund, and to limit that and to force us to use it for integrity efforts when we could already pay for integrity efforts and infrastructure through our UI grant really does not work for us and actually penalizes us and ties our hands.

Now, if other States want to do that, that is great, but let it be decided by each State how they want to use those funds. But an overall mandate is actually a disincentive for us.

Senator CARPER. All right. Thank you.

Gentlemen?

Mr. TRAUSE. Three things very quickly, Senator. First, we strongly support the New Hire expansion to include re-hires. We think that that is extremely important. Second, we believe that, if you are going to restrict the 5-percent override, you will clarify that it can be used for basic technology infrastructure. The biggest issue that we face, the biggest problem that we face in detecting overpayments, really is basic computer systems. Third, we would request that you make sure that we continue funding reemployment services. They are the key to prevention and I think will make a tremendous difference. Thank you.

Senator CARPER. Good. Thank you.

Mr. Cullen?

Mr. CULLEN. I think I stated earlier that we believe that the 5-percent use of recovered payments to help with integrity operations is the one portion of this bill that we really support, but we do believe—and I am going to have to disagree with Ms. Cox just a little bit—that it should be mandated in some fashion that States use this for integrity operations.

I think we have seen throughout the current recession that, when pressure is on an agency to make payments, they will transfer staff from integrity operations to get those payments out the door. We can argue whether that is right or wrong, but it happens. I think we need to, in the future, always keep the focus and the priority on integrity that it deserves, and the only way to do that is to ensure that we are dedicating the resources to it that need to be.

Senator CARPER. All right. Thank you.

Earlier this month I chaired a subcommittee hearing with the Federal Financial Management Subcommittee, and we looked at a technology solution that is being implemented across the government—we already talked about it a little bit here today—called the Do Not Pay list. The idea is to use information to prevent payments to those who should not be getting them in the first place. The most basic information is up-to-date listing of people who passed away, to avoid giving payments to people who are ineligible because they are dead. Accessing the Social Security Administration's death master file is what agencies do to avoid that kind of error.

Mr. Cullen, if I could just come back to you for a moment and say, I think in your testimony you mentioned the National Directory of New Hires. You mentioned it a couple of times, and correctly indicated that making this directory as up-to-date and as timely and reliable as possible is paramount to preventing improper payments in the Unemployment Insurance program. I

agree. Are there any other data systems or sources that would be useful to the Unemployment Insurance program to start preventing more of these improper payments from occurring in the first place? Also, are there other Federal programs that would be helped by access to the National Directory of New Hires, maybe the Social Security Disability Insurance program, or others?

Mr. CULLEN. I believe, yes, there are. I was surprised Ms. Cox mentioned 18 cross-matches that Utah is under way to complete. I think that is very impressive, that there are systems out there. In many cases, for unemployment it comes under "able and available for work," and so we should be looking at prison cross-matches, possible hospital cross-matches, the death registry cross-match. Anything that a State can look at that says this person who is drawing a benefit is not able and available for work, should be considered a source of information that States can use. As far as other agencies that can use the National Directory of New Hires, I apologize, it is just not my expertise, so I cannot comment on that.

Senator CARPER. All right. Thanks.

Ms. OATES. Senator, if I may.

Senator CARPER. Yes, please. Ms. Oates?

Ms. OATES. I just want to tell you, we are piloting, through our partnership fund, using bank data—and actually have been involved in some of the discussions with other agencies about the Do Not Pay list. We think it would be very, very helpful for our States to be able to cross-match incarcerations, death, and also this banking data so that, as I think Kristen said in her testimony, as they do in Utah, we could watch for anomalies of people making large-scale deposits who are allegedly unemployed.

Senator CARPER. All right. That is a good point.

My time has expired. Let me just conclude by saying, as former State treasurer and as a recovering Governor, I am mindful of the fact that States really are laboratories of democracy, and we have centers for best practices in different States doing different things. It sounds like Utah is pretty good especially in this area. The NGA, the National Governors Association, has a Center for Best Practices where we can go, the States can go, to see who is really doing a good job at this stuff. I am pleased that Senator Hatch's State has been represented here today to share with us some of the good work that is going on there, and we applaud very much the efforts of the administration in this regard. This is important work. Thank you.

I would just say to our friend from Washington, if you would tell Governor Gregoire that a recovering Governor sends his best.

Mr. TRAUSE. I shall do so.

Senator CARPER. Thank you.

The CHAIRMAN. Thank you, Senator.

I have this BAM report, and I know it has problems. But it still is a bit stunning, the disparity among States, even given the problems with the BAM report. Like, some States have overpayment rates of 40 percent, another State has 28 percent, another State has 33 percent. Some States are very low, according to the BAM. One of the lowest States is 3 percent. Another of the lower is 2 per-

cent, that is Kentucky. The other one is Connecticut. Vermont is 3.5 percent.

It just seems to me that there has to be some effort undertaken to deal with the irregularities, the problems with the BAM. I think it is important to know what each State is doing, and that gets to technology and so there is some commonality here. States can still have their own programs, but at least we have to know what is up.

So, what is your best advice, any of the four of you, as to how to make this thing quite useful? I think it is somewhat useful now. I mean, to see disparities between 48 percent and 3 percent, that is somewhat useful. So how do we make it even more useful so we know what we are doing, and we know where the problems are and where they are not? How do we make this report work?

Ms. OATES. Senator, if I could start out. I am sure my friends here will have better information to put forward. But it begins with partnership. It begins, for us, working with the National Association of State Workforce Agencies, which is the organization that represents all the States and the individuals here at the table. It starts with setting up groups. The visual that we gave you, the pie chart, that was the first attempt for us to really visualize the problem for all the States.

Our effort to bring the top 11, the biggest 11 instead of the people with the biggest problems, was to make sure that we establish beacons of good practice, of best practice, so that Utah, which has really done some remarkable work, could partner and mentor other States in that. We really think that the Federal Government has a convening role and a role to really put forward those best practices. But States talking to States is where they can really make the biggest improvement.

The CHAIRMAN. All right. Ms. Cox, your thoughts on the subject?

Ms. COX. She is right, so ditto. Give me clear instructions and a couple of measures of what you want me to do. I feel like I am chasing a few measures. BAM is one, but there is a lot of variability in BAM. There is the BAM operational rate, there is the over-detection payment rate, there is a new regulation that is coming out, there is my BPC measure in terms of detected and established. I feel like I am chasing a few measures. You have to look at all of them, really, to get a qualitative and quantitative piece.

But if you guys are going to be looking at the BAM measure as the way of comparative data, I have some concerns around that. You are never going to keep everyone happy with the measure, I get that. You are never going to be perfect. But there needs to be clarity around maybe two, three, four measures that we all agree on that you guys are going to look at.

The CHAIRMAN. What do you think they should be, those two or three?

Ms. COX. I do not think it should be BAM.

The CHAIRMAN. What should it be?

Ms. COX. Maybe BAM operational. I think BPC measure, in terms of actually established collections and as it compares to appeals and adjudication, do those detections actually stand up? And I would have an early detection measure, a little different than the one they are proposing, that looks not at just fraud, but fraud and

overpayment. We do not really have any early detection measures. So an early detection one, perhaps operational, and maybe BPC.

The CHAIRMAN. All right. Thank you.

Mr. Trause?

Mr. TRAUSE. I would agree. I think it is important to simplify. I think three measures are critical. BAM operational is one that I would like to see us focus on.

The second that I believe is really very important is a prevention measure, because I agree that early detection is critical, and that what you want to look at is how early in the claim are you catching fraud. We have one that we use that we are quite comfortable with.

The third thing I would say, though, is that part of this is on us as States and what use do we make of the information. I think it is incumbent upon us as States to look at what comes out of BAM and what is it in our system that we need to change to bring that BAM rate down. It is a process of continuous improvement. So I do not think—without wanting to pander too much—I do not think it is fair to look at the Department of Labor alone. I think part of it rests with us.

The CHAIRMAN. All right.

Mr. Cullen?

Mr. CULLEN. I have made my pitch for technology.

The CHAIRMAN. Right.

Mr. CULLEN. And so I think the same thing I would focus on is this concept of a public/private partnership. I mean, I sat here writing notes about the National Governors Association Center for Best Practices, the 18 cross-matches that the State of Utah is doing, and we are going to follow up on that because those are ideas that we have not necessarily thought of or that we have not tapped into.

So I agree that States and the U.S. DOL have responsibility for the administration of the program, but employers, through taxes, pay for it, and we should be involved as employers in that conversation too to say we have some ideas also. So I think the idea of a public/private partnership that gets everybody's voice involved in the discussion, finds a way to get a clearinghouse for information, that addresses this particular problem, is critical.

Mr. TRAUSE. Senator, the one thing I would add, very quickly, is that I believe whatever approach we adopt has to be balanced. We have to look at both sides of the equation. What are we doing to detect unregistered businesses? What are we doing to make sure that employers are paying their fair share, as well as making sure that employees are getting only appropriate benefits?

The CHAIRMAN. I am trying to figure out how we accomplish this objective. The first thing that comes to my mind is to have you all back here a year from now and charge you, if that is the correct word, with finding a solution together over the next year, or 6 months, or whatever the appropriate period of time is. You are the experts. I mean, we talked about State governments, Federal Government, private sector, and so forth. But clearly we have a problem here. Seventeen billion is a problem. I would like your thoughts right now off the top of your head on what process would you suggest so we are not just wasting our time talking about all

this, but we find some solutions here? Do you have an idea on process? Ms. Oates?

Ms. OATES. I think it would be important for you to hold our feet to the fire, and I think that certainly NASWA and the Department could work collectively to give you quarterly updates so you could determine when you wanted to pull us in front of you again. I am interested in Mr. Cullen's idea about how we engage business in that, and quite frankly, Senator, I do not have a clear answer to that. But I would love to think about how we get employers engaged at a national level. I mean, I know States are already engaging them, but I would have to come back to you on what I thought was a reasonable way to get that employer involvement.

The CHAIRMAN. Does anybody else have an idea on process and how we get some results here?

Ms. COX. Can I ask a question?

The CHAIRMAN. Sure.

Ms. COX. In your mind, what are the top two or three things you would want as a deliverable in a year?

The CHAIRMAN. I would like to see definite progress in getting the rates down much lower than they currently are. I am interested in the bottom line. I think that probably the things you have talked about, the various kinds of reporting, can be improved upon. That is probably correct.

I think better technology is probably part of the solution. Working with employers, that is part of it, too. But I am more concerned about the bottom line, and that is making sure that we do not have a \$17-billion loss next year. I would like to get down to \$8 billion in a reasonable period of time. Ms. Oates said getting down to \$8 billion in a couple of years sounds reasonable. But I am interested in that bottom line. You are the experts to know how to help get to that bottom line.

Ms. COX. Well, for me, it is so different from State to State.

The CHAIRMAN. Right.

Ms. COX. So I am always cognizant about that. But I would have a clear understanding of what we are measuring, a clear plan for automation and technology. I do not know if it is necessarily in new funds or if it is redistribution or UI administrative flexibility. Part of that measurement would be around reemployment. It is not an emphasis right now.

For my mind, making sure people are compliant is part of program integrity with the specific targets for each State, but not a generic one. Not everyone is 35 percent or 50 percent, which is in the proposed rule, so we need a target that makes sense for each State, and maybe that is negotiated. We negotiate a lot of our measures right now with the Department of Labor at the regional level. We should have that same flexibility, because current direction is a one-size-fits-all approach. Some States need to be much more aggressive, and other States are pretty close and may need smaller improvements.

The CHAIRMAN. All right. I just do not want to let this opportunity slide by, so I am going to still think about it.

Senator Hatch?

Senator HATCH. Well, thank you, Mr. Chairman. I am just going to finish with a couple of questions.

Secretary Oates, I do appreciate your willingness to be here today and the apparent willingness of the Department of Labor to address the growing problem of fraud and overpayment in the Unemployment Insurance system.

However, I want to ask you about the status of a program Congress already authorized. Legislation we passed in 2008 allows States to collect Unemployment Insurance overpayments due to fraud under the Treasury Offset Program. Congress authorized States to use the offset program to intercept Federal tax refunds to collect overpayments.

Now, the program is being set up by the Department of Labor, Treasury, and IRS, as I understand it, and you mentioned it in your testimony. Could you please give the committee just a little more information about the status of the implementation of the offset program, and tell us how much money could potentially be recovered by the States in the future?

Ms. OATES. Well, in the 2010 tax year, as I said in my statement, Senator, three States were able to collect \$25 million. We think that more States will come on for the 2011 year. Depending on which States those are, looking at the States this year, there were three rather large States. But if California and Texas were to come on next year, we could probably quadruple that \$25 million. So I think we are trying to give guidance.

It took a little bit of time to get Treasury to get the guidance out. They did get it out in time for the 2010 year. We are very optimistic. States are very interested in pursuing that. Probably the two Commissioners here would give you their read on what they thought they could collect, but we think \$25 million in 1 year is very promising.

Senator HATCH. All right. Now, as I read it, section 3 of the administration proposal seems to prevent the States from using penalties collected for fraudulent unemployment claims for anything other than integrity activities.

Ms. OATES. Integrity.

Senator HATCH. Now, currently States impose a wide variety of penalties for Unemployment Insurance fraud, and many of them greater than 15 percent. Under current law, there are no such restrictions as to how States can use these funds collected as penalties.

Now, the funds collected under these penalties are in every respect State funds. Even if there is a Federal requirement to impose a penalty, should the States not be able to determine for themselves the best way to spend those funds, whether it be for integrity programs or job training programs or additional benefits or whatever? Then, Ms. Cox, if you would give us your opinion on it as well. Go ahead.

Ms. OATES. Well, Senator, the 15 percent that we are proposing would not prohibit a State from charging more. So, in a State like Utah where they do 100 percent, there would be no prohibition on that. It would instead establish a floor that every State was at least charging a 15-percent penalty.

In terms of the use of funds, I mean, clearly this is a discussion draft that we are going to have lots of discussion with the States and with this committee about. But these are employer funds, and

I think we at the Department had lots of rich conversations about, what is the responsibility of this? Should we put some parameters around it? We do not want to be a nanny here.

We know that some States are doing really wonderful things. But we are called before you when States do silly things with this money, so we want to achieve a balance that says this is employer money, tax money that is being paid, how should it be used? If we need to widen the uses of those funds, we will certainly work with your staff on something that we are all comfortable with. But saying they can use it for everything assumes that every State will be as responsible as Utah has been in this, and I am not sure any of us feel that same comfort level. We want a little bit of protection for this money.

Senator HATCH. All right.

Ms. Cox?

Ms. COX. The Assistant Secretary is great to work with, so I am confident we will have a good dialogue around this. Two points. One, most States, I would assume—we have it in Utah—work with an oversight group that we go to for “permission” on how to use the P&I fund. We also have to get permission from our legislature. They actually have to appropriate that, and they get feedback from employers. So it is not as if we are making these decisions in isolation. We go to our employer groups and say, here is where the funds are, and actually get approval from them before we even take it to the legislature.

And, two, the idea around program integrity, I know, has become emphasized during the recession because so much went out from the Federal Government around EUC and EB funds. But it is important to recognize, I have to go in front of my State legislature and talk about program integrity around the State benefits for 26 weeks. So States, even though they may be struggling in different areas, still have to be accountable to their State legislature face-to-face.

Where you have to be responsible to this whole body, we are still going in front of our legislatures. So these issues are still important for us, but the legislature, in tandem with the employer community and the benefits community, needs to make the decisions around where the priorities are, where we are deficient. If we are really good in program integrity and I need to resource some other priorities, I need that flexibility.

Senator HATCH. Well, thank you.

Mr. Chairman, this has been an excellent hearing, and I really appreciate all four of you. Each of you has been particularly articulate, and we are very grateful to you for helping us to understand this a little bit better. Thank you for being here.

The CHAIRMAN. I second that. I am still trying to figure out an efficient process here.

Ms. OATES. Senator, with your permission, if we could send to the members of the committee and your staff, through the chair, our strategic plan, we would love to get your feedback on it, and we would love to have a real discussion with you about things that you think we could be tougher on and things that maybe we have overlooked. So, with your permission, we will send you that this afternoon, and we will wait for questions.

The CHAIRMAN. That is an excellent idea. In fact, I was going to suggest something similar to that.

Ms. COX. Great minds.

The CHAIRMAN. I am going to ask each of the four of you to give your recommendation of how we undertake the next steps to address the overall problem here. I have a hunch we may see each other again.

Thank you very much. The hearing is adjourned.

[Whereupon, at 11:25 a.m., the hearing was concluded.]

APPENDIX

ADDITIONAL MATERIAL SUBMITTED FOR THE RECORD

Hearing Statement of Senator Max Baucus (D-Mont.) Regarding Unemployment Insurance Program Integrity

Clement Stone, a great American businessman and philanthropist, once said, "Have the courage to say no. Have the courage to face the truth. Do the right thing because it is right. These are the magic keys to living your life with integrity."

These words provide helpful wisdom today as we face the truth and the challenges in our nation's Unemployment Insurance program.

In these difficult economic times, Unemployment Insurance, or UI, provides a critical lifeline to millions of Americans who lost jobs through no fault of their own. UI ensures that families can still put food on the table, gas in the car and keep roofs over their heads while looking for their next job. The beneficiaries of this program are workers. They have worked, they want to work and they will work again.

In a recession, Unemployment Insurance spending increases. This funding gives a temporary boost to the economy that helps keep both families and businesses afloat. This helps stabilize our economy.

However, the substantial job losses of the Great Recession stretched UI programs nationwide. This strain has led to an increase in improper UI payments due to errors, inefficiencies, and even fraud.

To do the right thing and create the solutions this program needs, we must first understand why these overpayments occur. That is why we are holding today's hearing.

In 2009, the Department of Labor reported \$11.4 billion in improper UI payments. Last year, that number spiked to more than \$17 billion.

With leadership from this Committee, Congress passed legislation last year to curb abuse and waste in the unemployment system. This law allows the Treasury Department to recover overpayments from those who don't report their earnings. It also eliminated the ten-year time limit the government had to collect overpayments.

The law requires employers to report the very first day new hires begin working. This helps determine whether workers were receiving improper Unemployment Compensation benefits. Although this legislation is helping curb these inefficiencies, we need to do more.

The leading cause of UI overpayments is claimants who have returned to work, but continue to claim benefits. The second-largest cause is errors verifying that unemployed workers meet all the requirements to be eligible for UI benefits. The third-largest cause of overpayments is workers who fail to fulfill state requirements. These requirements can include an active search for work or registration with the state employment service.

The UI program is too important for this money to be wasted. We need to work together to develop solutions to end these overpayments. This must be a combined effort that includes beneficiaries, employers, States, the private sector and the Federal government.

Right now, everyone's budgets are tight. Families are having trouble making ends meet, and we clearly need to fix our federal budget problems. There is not a penny to waste.

The Administration's most recent budget includes valuable ideas to address many of the program's issues. In this proposal, those who defraud the system would be required to pay a 15 percent penalty and return the wrongly-collected funds. Employers would be held accountable for overpayments resulting from extremely untimely responses to inquiries about their employees' work history. State governments would be encouraged to stop overpayments before they happen -- not just to collect after the fact. The federal government would have improved tools to recoup losses due to fraud and waste.

While the Administration's proposal contains some good ideas, there should also be a role for private-sector solutions in UI's future. These ideas may be the key to lasting administrative and data processing upgrades the system needs. States and private industry have also devised systems to reduce overpayments and streamline the program. We should examine all of these plans.

Senators have also come to the table with new ideas. I applaud my colleagues' efforts and look forward to working with each of them to develop solutions.

We will discuss with our witnesses today the challenges and opportunities for improvement in the UI system. So as we address these challenges, let us have courage. Let us face the truth. And let us do right by the millions of Americans that are counting on us to preserve the integrity of our Unemployment Insurance system.

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Written Testimony of
Kristen Cox, Executive Director
Utah Department of Workforce Services
before the Senate Finance Committee on
“Preserving Integrity, Preventing Overpayments, and Eliminating Fraud
in the Unemployment Insurance System”

Chairman Baucus, Members of the Senate Finance Committee, and Ranking Committee Member Hatch:

I appreciate the opportunity to provide the Senate Finance Committee with a short overview of some of the strategies deployed in Utah to help ensure the integrity of the UI trust fund, corresponding challenges, and my observations on proposed legislative and regulatory changes. Ultimately, our goal is to help unemployed Utah citizens find employment. When properly aligned, program integrity efforts, re-employment initiatives, operational efficiencies, and trust fund management should ensure that limited resources are maximized and directed to those who are eligible for benefits and re-employment activities.

INTRODUCTION

Program integrity is a priority for us and is reflected in the fact that for the third year running, the Department of Labor has recognized Utah as the top performer among medium-sized states for issuing timely payments while employing effective safeguards to stop improper payments and for issuing timely and quality appeal decisions. We estimate that for every \$1.00 invested in integrity efforts, we collect \$5.50 in benefit overpayments. Re-employment activities can also have a very positive impact on the UI trust fund—a one-week reduction in the average duration equates to a \$20 million dollar savings to the fund. Clearly, strategic and aggressive program integrity activities have a high return on investment.

Utah’s approach is founded on core values which include:

- We align UI fundamentals (such as trust fund management and program integrity) in a seamless system to support people going back to work.
- We direct maximum resources to the customers rather than to overhead and bureaucracy.
- We design policy in tandem with operations and a clear understanding of the costs and impact.
- We keep the system transparent and governed by limited and clear outcomes rather than a multitude of compliance activities.
- We keep public policy consistent across programs that include an interface with common customers.
- We strive for simplicity and common sense as our standard rather than complexity.
- We seek local solutions to local challenges.

Unemployment Compensation Program Integrity Act of 2011

In general, Utah supports the proposed requirements contained in the UC Program Integrity Act of 2011 to reduce overpayments and improve collections. However, Section 3 requires states to assess a minimum 15 percent penalty to any fraud overpayment with all collections placed in a restricted account for integrity activities or the payment of benefits. If Congress is serious about deterring fraud, setting the amount at 15 percent is inadequate. In addition, requiring states to use collected funds on integrity activities or benefit payments would actually be more restrictive than our current process which allows states the flexibility to determine how UI penalty and interest funds are used, particularly in states that already have administrative grants adequate to fund integrity efforts. Utah currently uses a portion of these funds for other activities such as re-employment initiatives that may have an even greater long-term, positive impact on our UI trust fund.

UTAH'S INTEGRITY INITIATIVE AND BEST PRACTICES

Utah, like other states, faces the challenges of ensuring timely UI payments to eligible individuals while employing effective safeguards to stop improper payments. The combination of customer education and aggressive strategies to combat fraud and overpayments is requisite to a robust program integrity approach. Utah is committed to transparency and on-going customer education in addressing these strategies.

Fraud and Overpayments

- Utah takes a very hard line when it comes to unemployment fraud. The fraud penalty is equal to 100 percent of the benefit amount paid as a result of fraud. Fraud overpayments can result in denial of future benefits for up to 49 weeks (13 weeks for the first week of fraud and 6 weeks for each additional week of fraud) and may also include criminal prosecution and publication of the convictions in the press and on our web site. We do not write off fraud overpayments and we do not allow debtors to draw future benefits until the debt is repaid. Utah's fraud overpayment rate is .88 percent of total benefits paid or about 55 percent less than the U.S. average.
- Most fraudulent overpayments are the result of claimants working while receiving UI benefits. Utah currently has 12 data cross-match programs that identify potential overpayments and, by next year, the number will increase to 18. These programs currently include:
 - UI wage data
 - Utah's New Hire Registry
 - Interstate Cross-match
 - National Directory New Hires
 - Jail and Corrections
 - National Guard and Reserves
 - Social Security

- State Employees
 - Address (multiple claims from same address)
 - Phone (multiple claims from same phone #)
 - IRS (data sharing with Treasury Inspector General Office)
 - Foreign Internet IP Address
-
- Utah was recently awarded a DOL grant for \$153,000 to further automate the process for identifying overpayments by automatically faxing, e-mailing, or mailing requests for information to employers to confirm work and earnings information based on leads from the New Hire Registry and wage data cross-match programs. This system will allow employers to respond electronically by interfacing with a web site, enabling the system to process the comparison, identify potential overpayments, and generate notices to claimants. The system will be fully implemented by July 1, 2012.
 - Utah was one of the original four pilot states to implement the National Directory of New Hires (NDNH) cross-match program that is now used by most states. The new hire cross-match system is the second largest tool for detecting UI benefit overpayments in Utah and is instrumental in the earlier detection of UI overpayments.
 - In 2005, Utah was one of five states to form a consortium (aka the State Information Data Exchange or SIDES) to develop a standardized format for exchanging separation data electronically (SIDES). SIDES provides a mechanism for states, large employers, and third party administrators to improve timeliness, accuracy, and reduce costs associated with separation decisions that account for 20 percent of all UI overpayments. Utah was the first state to implement SIDES in February 2010. The additional four states are now operational and another 18 states are now in the developmental stages. Initial results indicate that Utah has 50 percent less follow-up calls, with almost 100 percent accuracy and timeliness on all SIDES transactions. Future enhancements and additional modules are underway.
 - Utah, along with Texas, Maryland, and the Department of Labor are reviewing the value of matching ACH transactions against UI claimants' direct deposits and debit card transactions. The process would provide another opportunity for early detection of fraud and potential overpayments. The project is in a proof of concept phase but does appear promising.
 - Utah's innovative worker profiling and reemployment services function was recently updated and integrated into our on-line eligibility review program. This process requires a mandatory online UI eligibility review, orientation, and self-assessment for those UI claimants that are most likely to exhaust their UI benefits. This on-line system allowed Utah to obtain a five-fold increase in eligibility reviews that now reach 500-750 claimants weekly or almost one-third of our current weekly initial claims. The program allows Utah to ensure claimants are completing their weekly work search requirements and provides on-line information about other services, including job search workshops, training, supportive services, on-line job openings,

and labor market information and is very cost effective. Early engagement of UI claimants in re-employment activities has proven to be an effective tool for reducing the duration of claimants receiving benefits and ensuring program compliance.

- Effective collections of overpayments and contributions are also integral to the integrity of the trust fund. Utah's ratio of accounts receivable to tax due is one percent which is the 6th lowest in the nation according to the Department of Labor. Utah's automated collections case management system allows the electronic filing of liens with the court via the eFLEX system and reduces processing time and the associated costs. The system also provides collectors with real-time case management tools that reduces monitoring time, skips tracing time, and includes electronic work flows to help ensure collections are maximized to the fullest extent possible.
- In addition to penalties, Utah employers who are not compliant or current in filing UI taxes may face penalties from other state agencies. Agreements with partnering state government agencies may include revoking liquor and contractor licenses if the employer's UI account is not in good standing. In other cases, state vendor payments and state tax returns may be intercepted based on an outstanding UI tax debt.

Misclassification of Workers

Fifteen percent of collection activities are a result of misclassified workers. Utah has implemented an innovative approach to try to address this issue and we are beginning to see some positive results. However, a state's ability to fully address the complexity around this topic is limited by the IRS definitions that drive the policy.

- Utah was one of the first states to use IRS Form-1099 data to target employers for audit for potentially misclassifying workers. Since 2005, the Utah 1099 audit program has been continually expanding. The Department of Labor recently established new performance standards for states which place more emphasis on focusing compliance resources on more cost effective audits. In 2009, Utah had the highest effective audit score per Department of Labor performance reports. Utah uncovered over \$100 million in unreported wages during the last three years as a result of this program. Effective compliance is instrumental for providing a "level playing field" as well as helping to ensure the health of the UI trust fund.

CURRENT CHALLENGES

Federal legislation was recently passed that allows states to begin intercepting federal income tax refunds from individuals with UI benefit overpayment debts through the Treasury Offset Program (TOP). While we applaud the legislation, we have found that excessive Treasury regulations make it difficult and time consuming to implement. Utah, like many states, employs IT contractors to develop and maintain our IT systems. Current regulations and guidance do not permit the sharing of federal tax information with contractors even though no such restriction

applies to the Food Stamp TOP program which we have also been running successfully for many years. IT contractors are held to the same confidentiality requirements and background checks as our employees. We estimate an additional 600 hours of programming to accommodate this requirement.

A current Department of Labor core performance measurement for determining the effectiveness of a state's UI program integrity efforts is the "Overpayment Detection Rate." This rate is the ratio of established overpayments as compared to the overpayment amounts estimated by the Benefits Accuracy Measurement (BAM) program. One of the primary deficiencies of this measure is that the longer it takes for a state to discover and establish the overpayment, the larger the overpayment. Even though it is obviously better to discover overpayments earlier rather than later, this practice tends to improve performance outcomes. We understand future performance measurements are currently being discussed and we do have concerns about the draft language and look forward to the opportunity to provide further input. However, we support the concept of measuring the early detection of fraud overpayments in terms of reducing overpayments of five weeks or more. A focus on the actual collection of these overpayments is equally important to UI trust fund integrity.

With the enactment of the Improper Payments Elimination and Recovery Act (IPERA) of 2010 (P.L. 111-204), the Department of Labor has required state workforce agencies to report planned activities to prevent, detect, reduce, and recover improper UI payments as part of their future State Quality Service Plan (SQSP) submission. Utah supports giving states the flexibility to develop strategies and associated actions to reduce root causes, including the recovery of improper payments. Holding a state accountable, while providing maximum flexibility is reasonable and responsible.

CONCLUSION

I appreciate the opportunity to address the Senate Finance Committee. Program integrity, like re-employment strategies, is integral to the long-term health and viability of the unemployment program and I look forward to additional opportunities to work with this committee and the Department of Labor in finding real solutions for improving UI integrity.

United States Senate Committee on Finance
Public Hearing
“Preserving Integrity, Preventing Overpayments and Eliminating Fraud in the
Unemployment Insurance System”
June 22, 2011
Responses of Ms. Kristen Cox to
Questions Submitted for the Record

Senator Max Baucus:
Questions for the Witness:

Re-employment Activities

Providing reemployment services to claimants yields a reduction in the duration of UI claims. Most importantly, re-employment activities keep beneficiaries engaged in the workforce. In July 2010, there were 5 unemployed workers for every job opening. The current labor market means that an unemployed worker who loses benefits faces a serious challenge in securing new employment. Re-employment activities are a crucial connection for unemployed individuals who want to remain engaged in the labor market.

Re-employment activities can also have a positive impact on the UI trust fund – a one-week reduction in the average duration equates to a \$20 million in savings to the fund. Strategic and aggressive program integrity activities have a high return on investment.

Re-employment activities may also have an impact on preventing desperate acts by people who have run out of benefits.

1. Ms. Cox, I understand that re-employment activities have a positive impact on the trust fund. Will you please explain in greater detail?

Utah has found that engaging UI claimants early in their claim may reduce the average duration (number of weeks) the claimant remains on unemployment benefits, thus saving the UI trust fund (both state and federal) potentially millions in benefits. Despite having a relatively high average weekly benefit amount, Utah's average duration for state benefits is 16 weeks (for the 12 months ending March 31, 2011) which is one of the lowest in the country. Clearly, strategic and aggressive re-employment activities compliment integrity activities for ensuring the overall integrity of the UI system. Utah has a motto, "the claimant's full-time job should be devoted to becoming re-employed." Ideally, we would like to see every claimant become re-employed in suitable work in the shortest time possible. However, it is also essential that claimants are provided with a clear understanding of what is expected from them as a condition of receiving benefits and providing appropriate oversight to help ensure the claimants are actively engaged in becoming re-employed. Utah has employed several strategies for helping to ensure this through a fully automated worker profiling and eligibility review system, mandatory employee workshops and employer job fairs, mandatory re-employment meetings with employment counselors, and a more robust re-employment labor exchange system. Attachment #1 provides a

detailed description of these Utah re-employment initiatives. While many claimants have barriers to becoming re-employed rapidly, it is imperative that the unemployment division work with the workforce system to provide an integrated and seamless pathway for helping all claimants identify their barriers and helping them overcome them. Utah is currently looking at designing a truly integrated re-employment system for all claimants that will provide cost effective delivery through on-line portals, wherever possible, while ensuring program compliance with continued eligibility requirements.

Senator Ron Wyden:

Questions for the Witness:

1. In April of last year, the New York Times ran an investigative front page story on TALX (“Contesting Jobless Claims Become a Boon Industry” April 3, 2010), a business which challenges UI claims and appeals on behalf of other employers, covering almost 30% of all the claims filed in the U.S. Based on interviews and a sample of state data collected by the U.S. Department of Labor, it found that this company -- which contracts with many \ of the nation’s largest employers – is often responsible for filing late and frivolous appeals, unfairly triggering overpayment determinations for workers and backing-up the strained state unemployment programs. Does your state have any problems with TALX or other third-party representatives?

Utah has not experienced an unusually high number of frivolous and late appeals from TALX or other third-party administrators (TPAs). TPAs by their very existence, add another layer of complexity to obtaining timely first-hand separation information. While Utah has experienced untimely appeals from TALX and others in the past, we have been able to successfully resolve the issue with them at a state level. Utah and TALX recently began handling unemployment separation notices through the State Information Data Exchange System (SIDES), preliminary feedback using the new electronic exchange suggests the responses are timelier and more complete using SIDES thus we are encouraged that this could potentially be beneficial to other states as they implement SIDES.

If so, how do you address those problems? Does the Administration’s proposed Program Integrity Act go far enough to prevent these abuses (the act allows the states to “charge” the EMPLOYER for the overpaid benefits but only if the state can show there’s a “PATTERN” of failing to provide the necessary employer information on time). Should there be additional measures to prevent these abusive practices that contribute to UI overpayments? For example, should there be (or is there already) any requirement that third-party firms be separately regulated? Should they be required to register with the state, meet acceptable rules of conduct, and impose penalties for those that abuse the system? Should all charges that directly result from late-filed information be charged to the employers, especially given the limited resources of the states to go up against companies like TALX and prove that a given situation rose to the level of a “pattern” of abuse? In cases where an employer or third party representative fails to respond to your office in a timely matter, do you initiate payments to the claimant in the meantime or wait for employer verification?

Utah has had a provision in their law for several years that we feel is adequate for addressing the issue of an employer (or TPA) failing to provide timely separation information. Utah charges (benefit costs) employer's accounts for failure to provide timely separation information, without "good cause" and they essentially become a disinterested party without further appeal rights. An Administrative Law Judge (ALJ) may exercise discretion and choose to take continuing jurisdiction; however, even if they do take jurisdiction and reverse the eligibility and establish an overpayment the employer is not relieved of charges. The ALJ looks at 3 factors when deciding to take continuing jurisdiction:

- *The flagrancy of the refusal to provide complete and accurate information.*
- *The employers past record to provide complete and accurate information.*
- *Whether the employer is represented by counsel or a professional representative.*

Obviously, the proposed provision would be more administratively burdensome if we had to "track a pattern of non-responsiveness" and define "responding adequately" before we were able to charge employers. Utah is concerned this would effectively make our current law less relevant thus we would recommend the current language "if the employer has established a pattern" and the word "adequately" be removed from the proposed legislation. Utah does not feel that third party administrators need further federal regulation, if a state has an issue with any particular employer or third party administrator they should be able to address it at a state level and impose consequences/penalties that the state deems appropriate. Utah initiates an eligibility decision to the claimant based on the evidence provided by both parties. If the information provided justifies eligibility, the claimant is awarded benefits. Failure to respond to requested information can negatively impact either party. Utah, like all states, are bound by the "JAVA" supreme court decision, that prohibits withholding of UI benefits upon an employer's appeal from the initial eligibility determination.

2. With all the serious and important focus on recovering overpayments, what more could the federal government and the states be doing to ensure that workers are not innocently swept up in non-fraud or fraud overpayment determinations, and ensure there's a balanced approach toward program integrity? For example, the vast majority of states require that non-fraud overpayment determinations be waived in appropriate cases? Should all states have similar provisions to help workers who are already financially destitute and have done nothing to contribute to the overpayment?

Educating claimants regarding their responsibilities is critical to minimizing improper payments. Utah provides a 25 page claimant guide that provides an overview of their responsibilities, it is communicated to every claimant that they will be held responsible for provisions within the guide; we believe personal accountability is sound public policy. If the claimant is not responsible and an overpayment is created because of an agency error, the overpayment is considered a non-fault overpayment and no collection activity is established. While this action seems reasonable appropriate for our state, I believe it should be left up to individual states how they handle these types of situations.

3. The Obama Administration and the states have taken steps to address employer fraud in the UI program, going after employers who fail to pay their fair share of taxes by not reporting

workers on their payroll, by underreporting their payroll, or misclassifying workers as independent contractors. Various government-funded studies have estimated that as many as 15-30% of employers misclassifying workers as independent contractors to avoid paying unemployment taxes, workers' compensation or deny workers their basic rights under employment and labor laws.

Yet, when it comes to employers who commit UI fraud, the financial and criminal penalties are often very limited, more limited in many cases than the penalties that apply to workers who commit UI fraud. For example, in your state, workers are subject to a maximum prison term of 15 year years when they commit UI fraud, compared to 5 years for employers. In most states, the fines and penalties on employers for committing fraud are far below the proposed 15% penalty imposed on workers by \ the Administration's Program Integrity Act (they are usually a flat fee, not a percent of the unpaid taxes, ranging from about \$50 to \$2,000 or so).

Why shouldn't the penalties for employers who commit fraud be comparable to the penalties for workers who commit fraud? What more could be done in the Program Integrity Act or other federal or state policies to ensure that employers that intentionally defraud the unemployment system are effectively penalized?

Utah's criminal penalties for unemployment insurance fraud are governed by Section 76-8-1301 of the Utah Code. The maximum penalties for UI fraud for both claimant fraud and employer fraud are equal, each violation results in a second degree felony when the value of the money obtained or sought to be obtained is equal to or greater than \$5,000. As mentioned in my written testimony, Utah takes a hard line when it comes to unemployment fraud; the civil fraud penalty is equal to 100 percent of the benefit amount received. Fraud overpayments also will result in denial of future benefits for up to 49 weeks. If Congress is serious about deterring fraud, setting the amount at 15 percent is inadequate. Establishing penalties on the books is not enough, aggressive compliance programs to enforce the law are necessary, otherwise the law is meaningless. As mentioned in my written testimony, Utah was one of the first states to use IRS Form-1099 data to target employers for audit for potentially misclassifying workers. Utah is also partnering with other state and federal agencies to more effectively leverage our resources and share information on employers that misclassify workers.

Senator Tom Coburn:
Questions for the Witness:

I have attached a copy of a letter that I sent to the Department of Labor, April 2011, for your consideration.

1. The State of Utah has a lower than U.S. average fraud rate and has no outstanding unemployment insurance loans with the federal government. Your testimony seems to indicate that Utah has chosen to invest in program integrity efforts. Why do you think Utah is having such success compared to other states that are struggling to implement unemployment programs with robust safeguards against waste, fraud and abuse?

Utah has had a long standing commitment to establishing high performance standards; this is established in everyone's individual performance plan from the line worker to the director. Holding people accountable for their performance and productivity is a sound business practice for any government operation. Utah also invested heavily in automation beginning in the mid-1990s – we modernized both our UI tax and benefits systems between 1999 and 2006 and made work processes more efficient. The system is much easier to adapt to additional programs such as the Emergency Unemployment Compensation program which positioned us well during the economic downturn. We had adequate systems to help manage the tripling of the workload while maintaining our focus on integrity activities. I believe many states had to divert integrity resources to the massive increase in claims workload. Resources devoted to integrity activities was probably not increased commensurate with the increased level of claims activity. Additionally, DOL has provided numerous opportunities for states, through supplemental budget request (SBR) grants to enhance their programs and Utah has taken advantage of many of these opportunities and this has allowed us to continually enhance all of our UI programs, including our integrity programs. Finally, we have a very functional and cooperative relationship with the state's Department of Technology Services that has allowed us to develop and manage our own IT projects much more efficiently and successfully than most vendor-contracted projects.

2. In your testimony, you note concerns about the Administration's proposal to improve program integrity in the Unemployment Insurance program. Can you expand on this point and how state flexibility may be hindered if The Unemployment Compensation Program Integrity Act of 2011 were enacted as currently drafted?

The integrity act proposal requires the states to use the fraud overpayment penalties collected on UI integrity related activities. Current laws allow a state to use monies collected from penalties and interest on anything the state chooses. Utah's administrative grant provides us with adequate funding to cover our integrity related activities thus we would like to continue to use all penalties and interest monies on whatever purpose we (with legislative approval) deem is most appropriate for Utah. Utah currently uses these monies on re-employment activities, economic development incentives, training opportunities, etc., that may have an even greater long-term, positive impact on our UI trust fund.

3. In your testimony, you point out a deficiency in the federal overpayment calculation. Can you expand on this point in detail?

Basically, a state's improper payment rate comes from the Benefit Accuracy Measurement (BAM) program. Each state pulls a random sample of both paid and denied claims and audits these claims to determine whether the claimants were properly paid or whether the denials were appropriate. The improper payment rate and the improper denial rate are added together to establish the overall improper payment rate. Each state has different laws with respect to eligibility, thus what might be considered an overpayment in one states law may not be in another state, and thus it is difficult to compare rates between states. Additionally, one of the largest causes of overpayments is work-search issues. Utah recently required all non-deferred claimants to now complete a minimum of four work search applications per week (previously it was two per week); these are difficult to verify, and again, vary considerably between states.

States could effectively reduce their overpayment rates by simply relaxing the work-search requirements, however this would undermine the integrity of the UI system. While the BAM overpayment rate has some flaws, it also provides an individual state a baseline from which to reasonably attempt to measure program compliance and the overall impact of integrity efforts.

4. In your testimony, you note that Utah's unemployment benefit data is currently cross-matched to 12 registries and next year the number of registries will increase to 18. How difficult and costly has this effort been in Utah, and what you believe the return on the investment will be?

The additional six cross-matches are not anticipated to derive as much potential fraud overpayments as many of the original twelve since they are focused on a much smaller projected number of positive "hits". We anticipate the initial one-time cost to develop the additional six cross-matches to be less than \$100,000 and we should recover more than this amount in three months, on-going program costs will be less than \$100,000 per year also. It is difficult to project the return on investment until we see how much is generated when it is placed into production. Utah recently implemented a program to identify claimants who filed continued claims on-line using a foreign IP address (outside the US or Canada). This resulted in the establishment of over \$3.3 million in overpayments and penalties. This only took about a month to create this program, it proved to be so successful that we now have changed the program to create an issue and deny payment at the time the claim is filed to hopefully prevent the payment altogether.

Attachment 1

Utah's Initiatives to Re-employ UI Claimants Utah's pro-active re-employment initiatives have contributed to one of the country's lowest UI duration rates of 16 weeks (45th lowest) despite having one of the highest average weekly benefit amounts (as a percentage of average weekly wages).

- Utah implemented a "Back to Work" (BTW) wage subsidy program in July 2010 that was designed to assist eligible UI claimants and eligible youth. The program offers qualified employers an incentive up to \$2,000 for each eligible job seeker that is hired for a full-time position and remains for at least 90 days. To date 5,900 individuals and 814 employers have enrolled in the program, 1,100 have been hired by 370 different employers. The estimated savings to the Utah UI trust has been \$2.6 million to date and approximately \$6 million savings to the federal Emergency Unemployment Compensation (EUC) program.
- Utah's UI Worker Profiling and Re-Employment Services (WPRS) program was integrated with our UI Eligibility Review (ER) system in 2009. This process requires a mandatory online UI eligibility review and orientation and self-assessment to UI claimants that are profiled to be most likely to exhaust their UI benefits. This on-line system allowed Utah to obtain a five-fold increase in eligibility review that now reach 500 claimants weekly or almost 25% of our current weekly initial claims. This program allows a state to ensure claimants are completing their weekly work search requirements as well as provide on-line information on other DWS services, such as workshops, training, supportive services, on-line job openings, and labor market information in a very cost effective delivery. Failure to participate in this program results in denial of benefits. Utah received the American Institute of Full Employment's 2010 Best Practices Award for this innovative program.
- Using a \$1.3 million federal Re-employment and Eligibility Assessment (REA) grant, the Department has implemented an REA program. This program focuses on providing re-employment support to 10,000 unattached UI claimants who are most likely to exhaust their UI benefits. The REA program is similar to the current WPRS system, with the addition of a mandatory staff assisted interview to provide counseling, more in-depth assessments, and the development of a work plan. Preliminary results indicate 28% of claimants selected to participate in the program are no longer collecting UI benefits. Comparison reports with a similar control group are still forthcoming. Year 2 will expand the program to include follow-up contact, mandatory attendance to workshops, and pilot an on-line workshop.
- About \$440,000 of ARRA Stimulus funding was devoted to integrating Utah's current job match system with our UI benefits system. The integrated systems gather more accurate and complete data from job seekers (UI claimants) and eliminate redundant data collection. New AutoCoder software assigns ONET codes to job seekers and employer job orders, and these assigned ONET codes are transferred to Labor market Information (LMI). LMI provides individually relevant job market information to claimants on their personalized My UI Account web page.
- DWS has also worked with employers to identify occupations in which employment opportunities exist and for which a pool of occupationally qualified UI claimants is available. An example of this focused reemployment effort is bringing trucking companies together with UI claimants who are trained truckers. Claimants are notified that attendance is mandatory and failure to attend will result in denial of further benefits. Initial results indicate that about 30% of the unemployed truck drivers failed to attend and were subsequently denied benefits.
- Utah piloted a program in one of our economic service areas where we require claimants to come into one of our one-stop employment centers and attend a workshop (resume writing, interviewing skills, job searching, networking, etc). Of the 887 required to attend, almost 29%

are no longer receiving benefits compared with only about 1% of a similar sized control group that were not required to attend. We are currently expanding this pilot to include directing REA claimants to an on-line electronic workshop with multiple modules for helping claimants become re-employed. This pilot began in June 2011 and preliminary results should be provided by midsummer.

STATEMENT OF MICHAEL CULLEN
MANAGING DIRECTOR
ON POINT TECHNOLOGY, INC.
BEFORE THE
COMMITTEE ON FINANCE
UNITED STATES SENATE

Hearing on Reducing Overpayments and Increasing Quality in the Unemployment System

June 22, 2011

Chairman Baucus, Ranking Member Hatch, and distinguished members of the committee, thank you for the opportunity to testify this morning.

I am Mike Cullen, Managing Director at On Point Technology. On Point Technology's entire focus is Unemployment Insurance, and as a company we take pride in our employees' experience and expertise in this arena. Prior to joining On Point, I spent 14 years with the Colorado Department of Labor and Employment, serving six years as the State's Unemployment Insurance Program Director – our staff possesses similar backgrounds as career state unemployment insurance professionals. For over 15 years, On Point's solutions have enabled 17 states to find and collect improperly paid UI benefits, returning hundreds of millions of dollars to their state trust funds. We are proud to provide more efficient management systems that strengthen UI programs and help minimize tax burdens on employers and now with multiple federally funded extensions, return improperly paid dollars to the US treasury.

Background

The Unemployment Insurance system continues to face its greatest set of challenges in a generation. The recession's impact on state and federal UI trust funds is clear and stark as millions of unemployed continue to look for work in an economy that struggles to regain its feet. A year ago, before this committee, I testified that state trust funds have been forced to borrow a combined \$38 billion. As of June 16, 2011 state trust funds have an outstanding balance of \$41 billion in loans. The President's 2012 budget addresses the continuing increase in state borrowing; "Heavy borrowing from the Federal Unemployment Account (FUA) is projected to continue over the next few years. The aggregate loan balance is projected to increase from \$40.2 billion at the end of FY 2010 to a peak end-of-year balance of \$68.3 billion in FY 2013. Up to 40 states are projected to borrow".

We also testified that the problem was not exclusive to the states as Federal UI accounts had borrowed an additional \$37 billion from the United States Treasury to support the numerous federal unemployment insurance programs. The Department of Labor FY 2011 Mid-session Budget Review indicates that a combined additional \$42 billion will have to be borrowed in 2010 and 2011 from the general fund to support the extended

federal programs. Over the last year, despite the focus on improper payments, the rate of improperly paid benefits has gone from 9.6% in 2009 to 10.6% in 2010 and is currently at 11.51%.

Extended payment of benefits to the unemployed, bankrupt trust funds, unparalleled borrowing, and unprecedented levels of improperly paid benefits means that we are placing the future ability of the unemployment insurance program to act as an economic stabilizer at risk. Employers, who are struggling to keep their business afloat, are increasingly bearing the burden of rebuilding the trust funds through repetitive tax increases. In 2010, employers in 24 states saw UI tax increases. In 2011, employers in 35 states saw UI tax increases. If the trend continues, tens of thousands of employers will face additional tax increases in 2012. Employers are now experiencing not only the burden of increased taxes to replenish trust funds, but to pay interest on the debt the program has accumulated. The cumulative effect of this situation is that employers are now forced to bear the UI tax burden rather than use the money to create jobs. It is imperative we bring the improper payment problem under control because we are headed in the wrong direction.

Since the beginning of the recession in December 2007, more than \$370 billion in unemployment benefits have been paid. Moreover, the Administration projects that an additional \$430 billion of UI will be paid from 2011-2016. In 2010 alone \$18 billion in benefits were improperly paid. Yet, additional funding to combat the problem was only \$18 million. That's \$1 dedicated to combating the problem for every \$1000 improperly paid. This is unacceptable and does not begin to address the problem. If we continue at today's rate an additional \$50 billion will be improperly paid over the next 6 years with that number likely to increase if we do not take action now.

The current outdated systems create a tension between timely processing of benefits and ensuring the integrity of these payments. However, this dilemma ultimately represents a false choice. With an investment in technology systems and improvements in the use of the data available to us, we can both improve states' capacity to process benefits while dramatically enhancing the integrity of these payments.

Administrative Funding

Since 1992, administrative funding for the UI program has remained static. State agencies have been required to cut service levels or compete for other state dollars to administer their UI programs. During the Great Recession administrative funding was provided to deal with the significant increase in workload resulting from the huge increase in claims volume and to support the administration of the federal extensions and federal additional compensation. As the economy recovers the additional funding will begin to dry up and state UI programs will return to pre-recessionary levels; levels barely able to sustain program administration. However, the improper payment collection problem will continue and there is no additional funding to help pay for the activities associated with the lingering collection requirements. Because the focus to this point has been the payment of claims; improved processes, staff hiring, automation, etc. has

revolved around getting the money in the hands of the unemployed. Integrity has largely remained an under-staffed, manual activity. Post-recession funding for integrity has not been a focus.

National Directory of New Hires

Access to the National Directory of New Hires (NDNH) has been available to state workforce agencies since 2004. Use of the directory data has been mandated since 2007. In Unemployment Insurance Program Letter 19-11, issued June 10, 2011, the Department of Labor has directed that all state UI programs begin using NDNH cross-match data no later than December 2011. This is a positive step forward. Our experience has been that states who use NDNH cross-matching are able to reduce the size of the overpayment by about 50%. It is this early detection that has the potential to bring significant, immediate improvement to addressing the improper payment problem.

However, the challenge we see in relying solely on the NDNH is the unknown participation level by employers. We find that in states where both an NDNH cross-match and a quarterly benefit / wage cross-match are run, each finds about 50% of the total overpayments detected around claimants who were working while collecting UI benefits (The USDOL refers to this as a benefit year earnings overpayment).

Automating the Prevention, Detection and Recovery of Improper Payments

The issue faced by most agencies is what to do with the results of cross-matches or other processes that produce mass volumes of potential improper payment data. The majority of states rely upon manual processing to recoup wrongly paid benefits. Performing calculations, interfacing with state systems, and creating documents for employers and claimants are labor intensive processes. Resolving any question regarding a case, generally requires searching through file cabinets to secure the required information. These manual processes prevented states from addressing the overpayment problem before the recession and have proven impossible to ramp up with the increase in workload.

Adapting existing technology to eliminate this paper processing will dramatically increase productivity. States should store information in a web-accessible system to enable automated reports, letters, and interfaces thereby increasing productivity. Most states adjudicate every overpayment manually based on state statutes and UI case law. However, technology enables states to translate state law and precedents into business rules in order to issue automated determinations. Using these techniques we have seen states automate over 85% of overpayment decisions. This approach ensures consistency of approach and outcomes. It is our experience that implementing software incorporating these processes improves the overall detection and processing of UI overpayments by at least 300%. One state has had a return on investment of more than 100 times the original cost.

Reward High-Performing State Workforce Agencies

UIPL 19-11 which set the strategy for addressing the improper payment problem has also identified 10 “high impact” states, to pilot “cross-functional task forces”. In general the directive focused on those states with the largest populations. We believe this approach is mis-guided. Small and medium population states also possess good ideas and success stories from which everyone would benefit. Rather than focus on population, we believe the Department should support any state that can clearly demonstrate a comprehensive plan to address the improper payment issue. It is critical that we take steps to improve processes in the states and take advantage of every innovative idea.

Implement a National Effort to Combat Organized Fraud

Organized fraud exists. States that are armed with software to find organized fraud can avoid significant losses to their trust funds. In June of 2005, the U.S. Department of Labor’s Office of Inspector General testified before Congress about a single organized fraud ring that stole 15,000 identities and committed \$58 million of UI fraud. Other cases have been found. A proactive approach could have identified this organized fraud earlier, saved millions of UI dollars, and prevented identity theft for thousands of individuals. The use of automated software to search disparate databases for known patterns of fraud can detect and stop these illegal activities.

Unfortunately the nature of the UI federal-state partnership and the legal processes involved with prosecuting fraudulent activities has often left state agencies isolated and has precluded the sharing of information. States often are unaware of schemes that are perpetrated in other neighboring states or other regions of the country. A focused effort on the part of the Department of Labor to address fraud and share information is needed.

Recommendations

Improper payments represent a large and growing threat to the integrity of the UI system and require an immediate solution. We believe there are several ways that Congress can dedicate a comparatively small amount of what it currently invests in the management of these program yet yield substantial results to both the U.S. Treasury and state UI trust funds.

1. Provide a level of funding to the states that is appropriate to the problem.
 - Lacking a dedicated funding mechanism for integrity operations, we support the proposal of the National Foundation for Unemployment and Workers Compensation (UWC) and State Chambers of Commerce that a continued annual investment of \$30 million for integrity be part of a competitive grant process. Funding must be based on a clear demonstration of dramatic improvement by a state agency using the investment.

- Congress should provide dedicated administrative funding for software to support effective integrity activities with each UI extension. Purposing 10% of the administrative funds for integrity technology to protect the dollars from fraud and abuse could return significant multiples of the investment in the first year of implementation alone. Both the Congressional Budget Office and the Department of Labor have recognized that dedicated integrity funding produces net revenue increases for the unemployment trust funds and the federal budget. Based upon our experience, investments in software for state integrity programs can easily return \$10 every year for each dollar spent in the first year.
2. Convene a task force that involves the public and private sector, with the sole focus of examining and recommending tools that can be used to detect and stop overpayments earlier and recover any previously lost funds. If there is an opportunity that can be served by a government and business partnership, this is it. A clear plan and strong action with an emphasis on tools and employer cooperation could result in hundreds of millions if not billions of dollars in savings for employers and the US treasury. The task force should be given the direction to report back with specific tools and processes that will have an immediate impact on the improper payment issue within six months. Let us not forget the huge dollars here, \$18 billion improperly paid in 2010 alone; a number that continues to grow at an unprecedented pace. The Department of Labor has laid out their strategic plan but action needs to be taken now on process improvement.
 3. Good strategic vision must be met with operational improvements. We support the USDOL's mandate of the National Directory of New Hire, the soon-to-be-introduced SIDES transaction for discovering earnings overpayments and the integrity proposal for longer range integrity funding. Yet, we have an expression at On Point Technology: "There is a river of fraud – just dip in your bucket". States cannot process the cases that they could find now, so they dial down the discovery process. Detecting more overpayments will widen the river. What is first needed is a bigger bucket. Success in dealing with the improper payment issue cannot come until states have automated processes to handle the load. USDOL should require the use of automated tools to handle the tremendous volume of improper payments that should be collected and to provide for early detection and prevention.
 4. In concert with the Department of Labor and the states, we encourage Congress to consider a long-term legislative solution to the Unemployment Insurance integrity problem. In this context, the proposed Unemployment Compensation Integrity Act is a much needed first step towards a thoughtful legislative process. In particular we support the use of 5% of recovered overpayments to support integrity operations. We recommend this investment be mandated and that it augment and not replace current administrative funding used by the state for

integrity purposes. The concept of a consistent, self-supporting funding stream rather than occasional supplemental grant opportunities just makes sense.

Our unemployment insurance system is a vital lifeline for millions of Americans especially during times of economic turmoil like we face today. We must act to preserve the integrity of the system to ensure its continued viability for those in need. Fortunately, we are in a position to strengthen the UI trust funds and to help ease the tax burdens our employers will soon face. A modest investment in integrity technology will yield significant savings for the government, our employers and our taxpayers.

Thank you for the opportunity to testify. I am available for any questions you might have.

Mike Cullen
 On Point Technology
 Responses to Senate Finance Committee Questions

National Directory of New Hires

The NDNH is a database that contains personal and financial data on nearly every working American as well as those receiving unemployment compensation. The NDNH database includes information on: 1) all newly hired employees, compiled from state reports as well as reports from federal employers, 2) the quarterly wage reports of existing employees, and 3) unemployment compensation claims.

You mentioned that states that relying on NDNH depends on the employer and whether or not they are entering the information that is needed. You testified that when the information is properly used, about 50% of the total overpayments were prevented.

1. How can Congress encourage employers to participate in the National Directory of New Hires?

As a first step, On Point Technology believes Congress should require the Department of Labor to measure and report annually the participation by employers with the National Directory of New Hires. That report should also identify reasons for any low participation rate. Without knowing the extent and cause of the problem it is difficult to develop a solution.

We would also encourage an approach whereby a state UI agency automatically notifies employers when large overpayments are detected through a wage cross-match that could have been found earlier through the New Hire Directory cross-match. This will serve to remind and enforce state laws requiring usage of the national directory of new hires. The proposed notification would include language that cites state law informing the employer of their requirement to report new hires to the state and advising of any penalty if they continue to fail to comply.

2. Would imposing a penalty for not participating, or rewards for participation, work to encourage employers to use the National Directory of New Hires?

We believe imposing a penalty would have a positive compliance impact on employers who fail to participate in New Hire reporting and should be included in any state law or directive.

However we believe penalties should be reserved for egregious offenders who have been previously warned and yet fail to comply.

Adopting an incentive in the form of a tax credit for employers who consistently meet the reporting standards equally effective as a penalty, yet the cost and CBO scoring implications may be problematic.

Mike Cullen
 On Point Technology
 Responses to Senate Finance Committee Questions

Investing in Technology

You testified that, "Adapting existing technology to eliminate this paper processing will dramatically increase productivity. States should store information in a web-accessible system to enable automated reports, and letters - thereby increasing productivity. Most states adjudicate every overpayment manually based on state statutes and UI case law. However, technology enables states to translate state law and precedents into business rules in order to issue automated determinations. It is our experience that implementing software processes improves the overall detection of UI overpayments by at least 300%. One state has had a return on investment of more than 100 times the original cost."

1. How would the technology investment assist states' recoupment efforts?

If states were able to handle all cases presented to them, a greater share of overpayments could be established and collected. Without increasing state UI staff, automating adjudication and collection of overpayments can provide each state agency the ability to increase productivity and collection dramatically.

Much of the recent discussion within the Unemployment Insurance Program has focused on increasing the number, types and frequency of data cross matches to identify more fraud. On Point Technology believes these efforts ignore the heart of the problem within the states. The vast majority of states are not interested in identifying more sources of fraud as they do not have the investigative capacity to handle current case volumes. In fact many states have elected to turn off cross matches because of a growing backlog of cases. Commercially available technology has the ability to increase the "number of cops on the beat" by 1,000% and can address the workflow issues that State systems currently encounter

Many state UI processes are manual. Because of the large number of overpayments and lack of staff resources, agencies are able to process only a small portion of the cases. Through software, driven by business rules reflecting individual state law, regulation, and policy, the majority of cases can be handled through automated notification and decision-making. Proper notification of claimants at the appropriate times with complete case information that allows a proper response period protects their due process.

2. How much would it cost to invest in technology to help save the over \$17 billion in overpayments?

A one-time investment of \$100-\$150 million and an annual competitive integrity grant program of \$30 million can result in a significant reduction in the improper payment rate. It is critical, however, that Congress ensure that the state agencies be compelled to use these funds for integrity technology, as past investments have been used for a wide variance of activities with differing rates of return on investment. Funding for integrity should be reserved specifically for integrity activities.

Congress, the Department of Labor and the State UI agencies should model their investments on the best practices established by the private sector.

Mike Cullen
 On Point Technology
 Responses to Senate Finance Committee Questions

Program Successes

The national improper payment rate is currently at 11.5%. In your testimony, you mentioned that the rate of improperly paid benefits has increased from 9.6% in 2009 to 10.6% in 2010. You seem to suggest that investing in technology can solve this problem.

I would like to know how effective your company's efforts have been.

1. Mr. Cullen, in which states does your company currently operate? What are the percentages of overpayments in those states?

We currently have products installed in 14 State Workforce Agencies; Alabama, Alaska, Arizona, Arkansas, Colorado, District of Columbia, Illinois, Kentucky, Nevada, New Jersey, North Carolina, Ohio, Tennessee, and Washington. In addition, five other State Workforce Agencies have recently selected our products and should have them operational in the near future. These are Georgia, Massachusetts, Michigan, New Hampshire and South Carolina.

Success depends not only on the tool, but the willingness of the agency to build and use procedures that most effectively use that tool. As a company we have focused on solving the benefit year earnings issue, automating the collections activities, and detecting fraud. Here is what we have seen some state agencies do when they change their internal process and rely on automation.

Alabama for the past two years has been able to automate over 85% of their overpayments associated with claimants who continue to claim while working. Their staff has been removed from handling repetitive work and been allowed to focus on the complex cases. They increased their collection amounts from 45% to over 60% the first year they moved to an automated collection process.

The State of Alaska recently made a push to take advantage of our automated software and established 75% of the benefit year earnings overpayments in the first quarter. The USDOL standard is 55%. They recently told us they had to explain how they made such a dramatic improvement.

On Point Technology's Barts application specifically increases the investigative capability of State Workforce Agencies Benefit Payment Control (BPC) activities. In 2010, the following Barts customers were able to establish overpayments utilizing our automated adjudication features.

| State | 2010 BPC Established \$ |
|----------------------|-------------------------|
| Alabama | \$26,881,750 |
| Kentucky | \$11,275,186 |
| North Carolina | \$32,236,127 |
| New Jersey | \$203,150,284 |
| Illinois | \$107,418,162 |
| Arkansas | \$9,387,077 |
| District of Columbia | \$9,437,832 |
| Alaska | \$7,573,515 |
| Arizona | \$38,194,613 |
| Washington | \$89,771,282 |

Mike Cullen
 On Point Technology
 Responses to Senate Finance Committee Questions

We would also like to compare and contrast some of On Point Technology's Barts customers with the State of Michigan. Michigan's State Workforce Agency was recently audited by the Auditor General. Their report is available at <http://audgen.michigan.gov/comprpt/docs/ap641031510.pdf> and provides some rare public information which allows us to benchmark the performance of State Workforce Agencies BPC activities. The benchmark comparison is based on a ratio of the fraud dollars established as a result of the cross match process relative to the benefits paid. The following table shows how On Point Technology's customers are using the same type of cross match data sources to identify significantly more fraudulent overpayment dollars.

| | 2010 Benefits Paid (000's) | Annual Cross match Fraud Case Investigations | \$ Established | Benchmark Comparison |
|----------------|----------------------------|--|-----------------|----------------------|
| Michigan | 5,734,598 | 676 | \$1,089,954.67 | 19 |
| North Carolina | 4,846,322 | 2,604 | \$5,167,055.00 | 107 |
| Washington | 4,209,860 | 2,278 | \$7,908,659.00 | 188 |
| Alabama | 1,830,249 | 9,803 | \$9,147,433.00 | 500 |
| Arkansas | 874,761 | 3,504 | \$5,311,513.00 | 607 |
| Arizona | 987,125 | 11,737 | \$10,714,307.00 | 1085 |
| DC | 480,549 | 2,716 | \$8,967,088.00 | 1866 |

2. What innovative practices have you come across in different states that you think are worthy of expansion and investment on a national level?

We believe the Separation Information Data Exchange System (SIDES) and Interstate Connection (ICON) models of providing states a platform to exchange and use data has great potential. SIDES requires a large amount of cooperation between state agencies and employers that may take years to build. It is an intermediate/long term strategy and deserves support. However, SIDES is highly likely to have little impact in the short run and will not help in reclaiming previously overpaid dollars.

Another idea worthy of expansion is the adoption of hosted or cloud solutions. These generally provide lower costs and quicker deployment times by deploying a single solution rather than 53 individual approaches. It makes sense economically and also promotes sharing of data and adoption of best practices among states. It is also favored by multi-state employers.

Lastly, some states have started using magnetic card readers to authenticate state identification cards and drivers licenses. This significantly decreases the use of stolen identities when establishing unemployment insurance claims.

Statement of Senator Michael B. Enzi**Senate Committee on Finance
June 22, 2011****“Preserving Integrity, Preventing Overpayments, and
Eliminating Fraud in the Unemployment Insurance System”**

Thank you, Mr. Chairman, for holding this hearing on the unemployment insurance system. Since our last hearing on unemployment over a year ago, our economy has stagnated. The unemployment rate increased again last month to over 9 percent and almost 14 million people remain unemployed. But the so-called true unemployment rate, or U-6 rate, has reached almost 18 percent. This figure includes “underemployed” individuals who are working part time but would like to work full time and those who have left the labor force entirely because they simply have given up the search for employment. All of this demand is straining state unemployment insurance trust funds, and they are falling deeper into debt.

Many states have found it economically necessary to change the structure of their unemployment insurance programs. Budgetary constraints caused several states to shorten the number of weeks unemployment compensation benefits are available. Twenty-nine states have had to borrow over \$40 billion from the federal government to finance benefits, and these loan balances are expected to increase by over \$10 billion in the next 6 months. If these loans are not repaid within a specified time frame, employers and employees face an increased federal payroll tax. Employers and employees in three states were subjected to this increased tax in 2010, and with the repayment date nearing on many loans, more states will face increased taxes in upcoming years.

Over the past 36 months, unemployment insurance has provided some unemployed people almost two years of benefits. Studies have shown that these lengthy benefit periods correspond to longer periods of unemployment, and they have certainly caused major deficits in the federal and state unemployment trust funds.

I appreciate you holding this important hearing on fraud and abuse in the unemployment insurance system and support efforts to reduce fraud and abuse. However, it is equally important to discuss the huge deficits the recent mandates are causing for state unemployment trust funds. We need to find a balance that will support those that have paid into the system while maintaining an atmosphere conducive to job growth and creation.

Mr. Chairman, I look forward to working with you in the future to promote employment and improve our unemployment insurance system. Part of this improvement will come from efforts to reduce overpayments in the UI system through improved technology and low tolerance for fraud, and I look forward to hearing testimony in this area.

**STATEMENT OF HON. ORRIN G. HATCH, RANKING MEMBER
U.S. SENATE COMMITTEE ON FINANCE HEARING OF JUNE 22, 2011
PRESERVING INTEGRITY, PREVENTING OVERPAYMENTS, AND
ELIMINATING FRAUD IN THE UNEMPLOYMENT INSURANCE SYSTEM**

WASHINGTON – U.S. Senator Orrin Hatch (R-Utah), Ranking Member of the Senate Finance Committee, today delivered the following opening statement at a committee hearing examining the waste, fraud and abuse within the federal unemployment insurance system:

I often begin my opening statements with a light-hearted comment or a joke, but not today. Not when the subject is unemployment. It's just not funny. It's not an occasion for jokes.

Fourteen million Americans are unemployed. The official unemployment rate is 9.1 percent, but that actually understates how bad things are. An article in *U.S. News and World Report* this week concludes that the unemployment rate is in fact closer to 16 percent because the official numbers ignore people who have stopped looking for work, or haven't applied for a job in more than four weeks, or who have found only part-time work but who really want a full-time job.

One might think that after the failure of its stimulus program, the Administration would be doing everything within its power to help private businesses create jobs.

But you would be wrong. In fact, the Administration in some cases is actually eliminating jobs. Consider what the Administration just did in my state of Utah. The Administration has just announced that it is renegeing on a longstanding, bipartisan agreement to allow uranium mining in Southern Utah and Northern Arizona. By doing so, the Administration is blocking 4,000 new jobs and \$30 billion in economic activity.

Think of that. A year has passed since so-called Recovery Summer, and the economy is still on the ropes. We need all the jobs we can get. But the Administration is content to deny 4,000 jobs in Utah. And that's just in one corner of one state.

Four thousand jobs. That's 4,000 families that would have seen their Great Recession come to an end. But not now. We have a President who says he wants to create jobs. But as I said Monday, *I have never seen a bigger disconnect between a President's stated goals and his actions.*

With high unemployment, and an anti-business Administration stifling job creation, the subject of Unemployment Insurance program operation is before us again and, unfortunately, addressing these issues is more important than ever. As unemployment remains high, the amount of taxpayer dollars spent on Unemployment Insurance also remains high. In 2007, before the recession, we spent \$32 billion on Unemployment Insurance. In 2010, the figure was \$156 billion.

Now here is the kicker.

At a time of trillion dollar deficits —and with the country hurtling toward a full blown debt crisis — the Department of Labor estimates that 11 cents of every unemployment dollar spent by government is spent in error.

That means in 2010 over \$17 billion was simply wasted. We can't afford this level of waste under any circumstances.

Let's put this waste in this one program in perspective. Just last month the CEOs of the five largest oil companies were brought before this Committee, with cameras rolling, over a tax subsidy for energy companies. The proposal to eliminate that subsidy would have saved \$2.1 billion per year. Many on the other side of the aisle touted that as a significant proposal for bringing our trillion dollar deficits to heel. Yet, here in the Unemployment Insurance programs we have \$17 billion in waste in one year alone.

Well, that is why today we are here to discuss *Program Integrity*. When we talk about *Program Integrity* we mean the management principles the Federal government and the State governments employ, or should employ, to ensure that those who qualify for Unemployment Insurance receive it, but that those who do not qualify for benefits do not receive them. We are here to discuss ways to shrink an 11 percent payment error rate that is costing taxpayers \$17 billion every year.

One problem is the sheer complexity of the Unemployment Insurance system. Too many in Washington are masters of bureaucracy with little regard for the costs imposed. Administration of Unemployment Insurance programs at the Federal and State level cost American taxpayers over \$5 billion in 2010. States need flexibility, not Washington mandates. States should be free to share their best practices, learn from one another, and adopt what works.

As is often the case, the Utah Way has resulted in an error rate much lower than the national average. I look forward to hearing how that was achieved and what kind of improvements Utah plans to make for the future.

Another problem that must be addressed is the substantial compliance costs the Unemployment Insurance system places on employers who are saddled with substantial paperwork and tax planning burdens. For example, not every departing employee qualifies for Unemployment Insurance, but many file claims anyway because it costs them nothing, and they believe they have nothing to lose. But this puts the burden, and the expense, of fighting unjustified claims on the employer.

Then there is the problem posed by people that qualify initially for Unemployment Insurance, but then cease to remain qualified and continue receiving a check anyway. Maybe they have stopped looking for work as they are required to do, or maybe they have returned to work after a layoff and not reported it.

There are many reasons why an Unemployment check might be paid in error, and sometimes fraud is involved. But whatever the reason for an erroneous payment, given the millions of people in the system today and the billions of dollars being spent each year, we cannot tolerate an 11 percent error rate. We cannot continue to waste billions and billions of dollars every year.

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SUBMITTED BY SENATOR HATCH

June 20, 2011 Press Release

Hatch Lambastes Obama's Latest Job and Energy Killing Move
Administration Puts Hold on 4,000 Clean Energy Jobs in Utah, Arizona

WASHINGTON – Sen. Orrin Hatch (R-Utah) today lambasted President Obama's move to put thousands of uranium mining jobs on hold in southern Utah and northern Arizona, site of some of America's richest uranium reserves.

Interior Secretary Ken Salazar announced today that the Obama administration will continue to stall uranium mining activity in the region. The current two-year moratorium on 1 million acres is set to expire in July.

"Once again we have a Democratic administration using the rim of the Grand Canyon as a backdrop to killing jobs in Southern Utah," Hatch said. "If any further proof was required about this Administration's war on energy development in the West, this should put any lingering doubt to rest. With this decision, the President is putting 4,000 jobs and \$30 billion worth of economic activity on hold. He is also breaking faith with southern Utah and northern Arizona by breaching a longstanding bipartisan agreement to allow uranium mining in the area. This is unconscionable.

"We have a president who says he wants to create jobs and attack climate change, but then puts our nation's best source of uranium off-limits, thus killing thousands of high-paying rural jobs," Hatch continued. "I have never seen a bigger disconnect between a President's stated goals and his actions. As was the case with the establishment of the Grand Staircase-Escalante National Monument in 1996, this Administration is killing jobs for Utahns, without input from Congress or from the stakeholders who will be impacted the most."

Hatch noted that wind and solar power, while carbon free, do not provide enough power that utilities or distribution can use to meet customers' minimum demands. Nuclear energy, distributed by more than 100 commercial plants in 30 states, is one of a few sources of carbon-free base power that can be increased to meet customers' requirements.

"We were hoping for some certainty for the uranium industry and its stakeholders so that this important work could go forward in a safe and environmentally sound manner," Hatch said. "Instead, we now have more uncertainty than ever, and a very confused energy policy coming out of the Obama administration. I was under the impression that the President was for green energy jobs. Well, these projects would have created about 4,000 green energy jobs in southern Utah and led to the reopening of an existing uranium mill in Garfield County. This decision effectively sabotages that. It also increases our near-total reliance on uranium from foreign nations.

STATEMENT OF JANE OATES
ASSISTANT SECRETARY FOR EMPLOYMENT AND TRAINING
U.S. DEPARTMENT OF LABOR
BEFORE THE
COMMITTEE ON FINANCE
UNITED STATES SENATE

June 22, 2011

Good morning. Chairman Baucus, Ranking Member Hatch, and distinguished members of the Committee. Thank you for this opportunity to discuss the Unemployment Insurance (UI) program and the Administration's legislative proposal to improve integrity in the UI program. I also want to thank you for enacting improvements to the National Directory of New Hires (NDNH) and the Treasury Offset Program (TOP) in the last Congress - two important integrity proposals we have advocated for in the past that will provide new tools to states to improve prevention, detection, and collection of improper payments.

Reducing improper payments and strengthening program integrity are priorities for the Administration government-wide. They are equally a priority within the Department of Labor (Department). We are aggressively working to identify new strategies and tools to support our state partners in addressing the rising UI improper payment rate. I might also add that addressing improper payments relates to UI trust fund solvency. Particularly now, when trust funds are under extreme pressure and states are borrowing at near record levels, it is essential to ensure that UI benefit

payments are made properly and that all employers pay their fair share of unemployment contributions.

I appreciate the Committee's interest in this critical issue.

BACKGROUND

I am pleased to report that the UI program has a longstanding commitment to ensuring its financial integrity. The program uses highly sophisticated sampling and auditing methods and other tools to prevent, detect, and recover overpayments. As you know, the UI program operates as a federal-state partnership, which means that state action is key to addressing the UI improper payment rate. Every state operates a UI Benefit Payment Control unit that utilizes a wide variety of tools to detect, establish, and collect overpayments. When potential overpayments are detected, individuals are given the opportunity to demonstrate that the payment was not made in error before collection efforts begin. All states also operate a quality control system to identify claims errors and support corrective action in the state's UI system. Using the Benefit Accuracy Measurement (BAM) survey, states sample approximately 24,000 paid and denied claims each year, nationwide. Each state thoroughly investigates its own benefit payments for accuracy. For claims that were improperly paid, the investigation determines the cause of, and the party responsible for, the error and the amounts over (or under) paid. The UI improper payment rate is estimated from the resulting data for this nationally representative random sample.

The Employment and Training Administration (ETA) routinely reports an annual improper payment rate based upon data collected from very thorough BAM audits that detect many errors that are not within the control of the state agency. As a result, we report two rates for the UI program: the overall annual rate based on all sources of error; and the operational rate, which represents those improper payments we believe are more readily controlled – that is, identified and addressed – under normal state operations. Unfortunately, the UI improper payment rate has increased during the most recent reporting period (July 2009 to June 2010) required under the Improper Payments Information Act. During this reporting period the rate was 11.2 percent, of which 10.6 percent represents overpayments. The operational rate for the same period was 5.7 percent. As explained below, that increase may, in large part, be due to the strains put on the UI system from the large increase in claims as we entered the recession.

As you review improper payment statistics for the UI program, there are several things to keep in mind. States are required by the Social Security Act as interpreted by a U.S. Supreme Court decision, California Human Resources Development Department v. Java, 402 U.S. 121 (1971), to pay benefits as soon as administratively feasible. States constantly struggle with getting timely, sufficient information from the individual's prior employer to make an accurate eligibility determination. Errors result from this structural challenge.

The four main reasons for improper payments in the UI program, listed in order of importance, are: (1) payments are made to individuals who have returned to work

and continue to claim benefits; (2) information regarding the claimant's separation from work is received after a determination of eligibility is made and the claim is paid, often due to failure of employers or their third-party administrators to provide timely and adequate information on the reason for an individual's separation from employment; (3) claimants fail to meet the state's work search requirements; and (4) claimants fail to register with the state's Employment Service pursuant to state law. Attachment A is a graphic display of the root causes for UI improper payments.

The recession has had an impact on the UI improper payment rate. Entering the recession, average UI claims increased by 3.2 million, or 120 percent, in only a one-year period. Although additional federal support helped, many state workforce agencies struggled to keep up with increased workloads and were compelled to utilize integrity staff to process claims instead of focusing on improper payments. In addition, a significant number of UI improper payments are not within the control of the state to prevent, such as when decisions awarding benefits are reversed on appeal. Other root causes of UI improper payments are very challenging and expensive to address, such as those due to the lack of documentation of a claimant's work search efforts. Today, however, states are actively working with the Department to aggressively implement strategies to bring down the UI improper payment rate, which is discussed in more detail below.

States also carry out integrity activities for state collection of employer UI contributions. Similar to the BAM survey, the Tax Performance System evaluates the quality of state UI tax operations. A sample of activity for each major tax function is

examined, including the collections operation and the field audit unit. Tax operations in the states employ a variety of tools including information sharing with the IRS under the Questionable Employment Tax Practice program, and targeting audits to detect and recover unreported contributions. All states audit one percent of their contributory employers to determine if they are properly reporting their employees and paying the correct amount of contributions. In addition, several states have enacted laws penalizing employers for misclassifying employees as independent contractors.

On November 20, 2009, President Obama signed Executive Order 13520: "Reducing Improper Payments and Eliminating Waste in Federal Programs". This Executive Order requires identification of the Federal programs with the highest dollar value or majority of government-wide improper payments, which are called high-priority programs. Due to its size, the UI program has been identified as a high-priority program. While states are striving to improve their integrity functions and the Department has many initiatives under way to support states' efforts to reduce the UI improper payment rate, additional statutory authority and resources are needed to enhance our collaborative efforts and to continue to improve payment accuracy. To this end, the Department sent the draft Unemployment Compensation Program Integrity Act of 2011, or as we call it, the Integrity Act, to Congress on June 11, 2011. The Department estimates this legislative proposal would cut spending by 2.5 billion over ten years. Much of this decline in spending would lead to lower taxes for employers, with 556 million in net savings to the government over that period. These estimates include budgetary savings in the form of further reductions in improper UC payments

and higher state unemployment tax collections, which do not score under budgetary rules. Much of the savings resulting from these measures will go straight back to employers in the form of lower tax rates. By making the system more fair for everyone we can lower the costs for this vital national program.

UNEMPLOYMENT COMPENSATION PROGRAM INTEGRITY ACT OF 2011

The Integrity Act consists of several provisions that will reduce UI overpayments, underpayment of employer taxes, and misclassification of employees as independent contractors; it will also improve the collection of overpayments and delinquent contributions.

Specifically, the legislative proposal would provide flexibility to states that want to augment their resources for integrity activities by permitting them to use a portion of recovered overpayments and delinquent contributions specifically for integrity purposes. Under current Federal law, all overpayments of UI benefits and all delinquent payments of UI contributions by employers that are collected by a state must be deposited in the state's unemployment fund where they may be used only for the payment of UI benefits and not for administrative costs. The Integrity Act would permit states to use up to 5 percent of each overpayment recovered to augment administrative funding for preventing, detecting, and recovering benefit overpayments. Similarly, states would be permitted to use up to 5 percent of delinquent contributions collected for preventing and detecting employer fraud and evasion, and recovering required employer contributions, including the misclassification of employees as

independent contractors and the identification of employers who attempt to manipulate the taxing provisions to pay less than their fair share of contributions. Having dedicated resources to support integrity activities is critical to ensuring that states are engaging in these crucial activities. When states are faced with large numbers of claimants as in the current recession, they often divert integrity resources to other mission-critical functions, such as timely benefit payments to unemployed workers. However, the combination of lower resources for integrity activities and a higher volume of claims inevitably lead to more improper payments. By creating resources dedicated to tackling improper payments we can preserve the integrity of the system and keep costs down for employers.

Currently, every state assesses penalties on employers who are delinquent in tax payments. The Integrity Act would apply a similar penalty on UI claimants with outstanding fraudulent overpayments and boost resources for integrity activities. It would require states to assess a penalty of not less than 15 percent of the amount overpaid on any claim for benefits that is determined to be due to the claimant's fraud. States would be required to place the penalties collected in a subaccount of the state's account in the Unemployment Trust Fund and only withdraw these funds for integrity activities.

This would ensure that individuals who have defrauded the system — who are frequently required to do no more than repay the fraudulently received benefits — will be penalized and that the penalty will be used in a way that will result in improved program integrity. While many states currently have these penalty provisions, the

amounts received are often used for non-UI purposes. If the state decides that any amounts it deposits in this special fund are not needed for the designated purposes, the state may use these amounts for the payment of benefits. At the same time, it is important to ensure that claimants accused of fraud are afforded appropriate due process, and the Department plans to issue policy guidance and provide technical assistance to states to ensure that is the case.

The Integrity Act would help prevent overpayments as well by giving employers an incentive to respond timely and adequately to an agency's request for information. In determining whether an individual is eligible for UI, states rely on information provided by employers. When this information is not received in a timely manner, is inaccurate, or is incomplete, an ineligible individual may receive benefits. To encourage employers to provide complete, timely, and accurate information about their former employees, this legislative proposal would provide that if the state determines that an overpayment was the employer's fault due to failure to respond timely or adequately to an agency request for information, and that the employer has a pattern of failing to respond timely or adequately to such requests, the state may not relieve the employer's account of the benefit charges.

Lastly, the Integrity Act would help states identify overpayments by requiring that rehires be reported by all employers to the NDNH. State UC agencies have found their state directories and the NDNH to be extremely useful in identifying individuals who claim UC benefits after they have returned to work and, under amendments enacted in 2004 and 2010, states are using the NDNH for this purpose. The NDNH

allows states access to a wider universe of employers, including federal agencies and multi-state employers who report all new hires to a single state.

However, the effectiveness of this system is limited because employers do not currently report the rehire of individuals who have not been separated from employment for at least a year, which limits a state's ability to determine whether individuals were improperly receiving UC benefits. This amendment would require employers to report individuals who were rehired after being separated from employment for at least 60 days. This reporting requirement will benefit these employers directly by ensuring that they are not inappropriately charged for UI payments to current employees.

EXISTING INTEGRITY EFFORTS

The provisions I have outlined above in the Integrity Act will bolster existing integrity efforts already in place at the state and Federal levels. The Department, working with our state partners, has been focused on the issue of improper payments for many years. A number of robust strategies are under way, new strategies are in the process of being rolled out, and we have been working collaboratively with our state partners to identify additional strategies that concentrate on the prevention of overpayments focusing on the root causes which will yield the highest impact. These strategies include:

(1) preventing claimants from continuing to claim benefits after they return to work through state workforce agencies' use of the NDNH;

(2) reducing improper payments through prevention and early detection of eligibility problems and speeding claimants' return to work by conducting Reemployment and Eligibility Assessments (REAs);

(3) receiving more timely and accurate separation information from employers or their representatives through use of the State Information Data Exchange System (SIDES), an automated separation information exchange;

(4) recovering outstanding overpayments by intercepting Federal income tax refunds using the U.S. Department of the Treasury's TOP; and

(5) providing tools, resources, and intensive technical assistance to states, and initiating innovative pilots to improve prevention in order to bring the improper payment rate down.

I will elaborate on each of these strategies.

National Directory of New Hires

To address the issue of individuals continuing to claim benefits after returning to work, one of the most effective tools for detecting improper payments, as mentioned previously, is the use of NDNH, a database maintained by the Department of Health and Human Services for child support enforcement purposes. The database contains quarterly wage and unemployment compensation benefit payment information, and information on new hires reported by employers. The Department has, under current authority, mandated expanded use of the NDNH for both detection and prevention activities and provided new protocols to states for using the NDNH most effectively. States will also be provided funding opportunities to implement these new protocols

and to put in place automated processes to immediately alert claimants that the state understands they have returned to work to prevent continued claiming and more improper payments.

Reemployment and Eligibility Assessments

The Reemployment and Eligibility Assessment (REA) initiative also has been an important investment in UI integrity. This initiative provides funds to states to perform in-person reemployment assessments typically conducted in a One-Stop Career Center. When an REA is conducted, individuals' UI eligibility is reassessed, the individual is provided with labor market and career information, and a reemployment plan is developed that includes referrals to One-Stop services. These REA activities reduce improper payments through early detection and prevention of eligibility problems and speed claimants' return to work.

During FY 2011, Congress provided nearly \$60 million in funding to states to support REA and integrity activities, for which we thank you. Currently 38 states, Puerto Rico, and the District of Columbia have REA programs. The FY 2012 budget requests \$70 million, which will fund 980,000 claimant REAs and save state unemployment trust fund accounts an estimated \$237 million. Another integrity proposal contained in the President's FY 2012 Budget is a request for \$10 million for incentive awards to states to improve their UI integrity activities related to improper payments.

A program evaluation for REAs has been completed and a report to Congress will be submitted this month. We were pleased to learn that the findings of the

independent review show the benefits resulting from the program substantially exceed the cost of providing REAs and that the program helped claimants get jobs quicker than they otherwise would have. By helping to speed the return to work REAs help both the claimant and the UI system. Individuals participating in REAs had a lower duration of benefits and were less likely to exhaust their regular UI benefits during a difficult economic period. Fewer benefits paid improves trust fund solvency, and quicker re-employment improves people's lives. REAs are a win for everyone.

State Information Data Exchange System (SIDES)

Another key initiative that addresses one of the top root causes of UI improper payments is the SIDES. This initiative is designed to help employers provide the information required to determine a claimant's eligibility to states more quickly by providing a secure electronic data exchange between states and employers or their third party administrators. In addition to speeding up the process, the SIDES system includes prompts and edits to improve completeness and accuracy of the information. Implementation of SIDES slowed during the recession due to other technology demands on the UI system; however, the Department is working with states, employers, and employers' representatives to rapidly accelerate implementation.

Treasury Offset Program

I am pleased to report that as of February 2011, the necessary regulation and system are in place for states to implement use of the Treasury Offset Program, which enables states to recover UI overpayments by offsetting Federal income tax refunds against UI debts. States that were ready to implement this system are already showing

impressive recovery numbers as a result. State UI agencies gained access to the TOP in February 2011. Between that time and June 1, 2011, three states (Michigan, New York and Wisconsin) have collected approximately \$25 million in overpayments.

Collaboration with States

We have engaged eleven states whose improper payments have the highest impact on the national UI improper payment rate in a collaborative effort to aggressively bring down the rate and to provide leadership to other states. Each state has formed a task force and developed a state-specific strategic plan with support and technical assistance from the Department of Labor. The Department is providing other tools and resources to support state efforts including implementing a campaign to target messages to claimants designed to prevent improper reporting of work/earnings while filing for UI benefits, messages to employers on the importance of responding timely and adequately to state requests for separation information, and adopting an additional state performance measure focused on improper payments that more effectively targets prevention. We are also working with states with the highest improper payments resulting from issues associated with registration of claimants with the state's Employment Service to analyze the state-specific challenges and develop strategies to address them.

RESULTS

Working with the states, we have seen a reduction in error rates and improper payments, and an increase in collections, through REAs, TOP, and other efforts. System

changes in Louisiana and South Carolina have resulted in substantial reduction of Employment Security registration errors. Louisiana's corrective actions have reduced the registration error rate 90 percent -- from 47.13% in 2010-Q1 to 4.76% in 2011-Q1. Similarly, South Carolina's actions have reduced the registration error rate by more than 75 percent -- from 15.94% in 2009-Q1 to 3.72% in 2011-Q1.

Work flow changes in Texas resulted in reduction in benefit year earnings errors. In fact, Texas reduced the benefit year earnings error rate from 4.37% in 2006 to 2.64 in 2010.

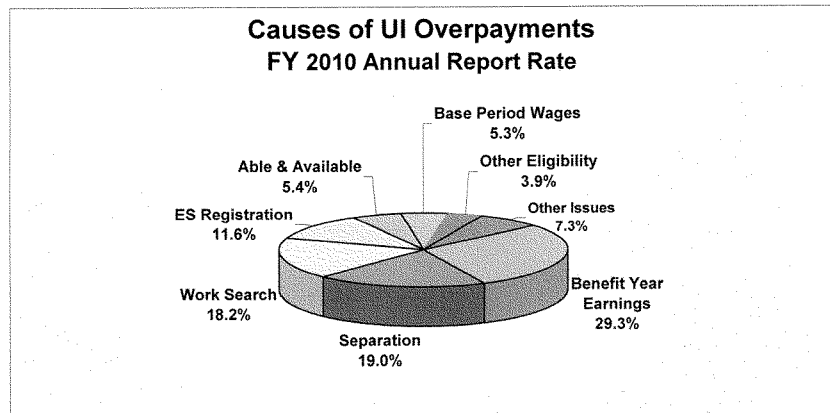
CONCLUSION

Again, let me thank you for the opportunity to talk to you about the integrity of the UI program. I look forward to working further with the Committee as you consider ways to enhance Federal and state efforts to reduce improper payments in the UI program, including passage of the Integrity Act. I will be glad to respond to any questions you may have.

Attachment A

Root Causes of Improper Payments

- ❖ Improper UI payments are classified into several causes.
 - 1) Benefit Year Earnings (BYE) (29.3%) - the claimant continues to claim and receive benefits after returning to work;
 - 2) Separation Issues (19.0%) - information regarding the claimant's separation from work is received after a claim is paid that disqualifies the claimant from being eligible for benefits and creates an overpayment (employer sends inaccurate or late information or a ruling is made on appeal);
 - 3) Work Search (18.2%) - inability to validate that the individual has met the state's work search requirements, which disqualifies the claimant from being eligible for benefits;
 - 4) Employment Service (ES) Registration (11.6%) - the claimant is not registered with the state's Employment Service or job bank as required by state statute, disqualifying the claimant from being eligible for benefits;
 - 5) Able and Available (5.4%) - the claimant is later determined to be unable or unavailable for work (in the hospital, in jail, etc.), disqualifying the claimant from being eligible for benefits;
 - 6) Base Period Wages (5.3%) - it is later determined that the claimant's base period wages were over-reported (due to employer error or an automation error), and the claimant is determined to be eligible for fewer benefits than they have received.



U.S. Department of LaborAssistant Secretary for
Employment and Training
Washington, D.C. 20210

JUN 22 2011

MEMORANDUM FOR THE SENATE FINANCE COMMITTEE

FROM: JANE OATES
Assistant Secretary *Jane Oates*

SUBJECT: Department of Labor's Strategic Plan to Reduce Unemployment
Insurance (UI) Improper Payments

Thank you for the opportunity today to testify today before the Senate Finance Committee in the hearing on Preserving Integrity, Preventing Overpayments, and Eliminating Fraud in the UI System. As I shared in my testimony, the Department of Labor is aggressively working with states to reduce UI improper payments and to bring the improper payment rate down. In order to give you a more complete picture of our efforts, I would like to share with the Committee the Department's UI Improper Payment Strategic Plan. I am pleased to report that we are on track to complete all of our strategies as identified. We would welcome your feedback and ideas to expand the plan.

We look forward to continued work with the Committee to address this important issue.

GETTING THE RATE DOWN: A STRATEGIC APPROACH

PREVENTION

TARGETING

METRICS

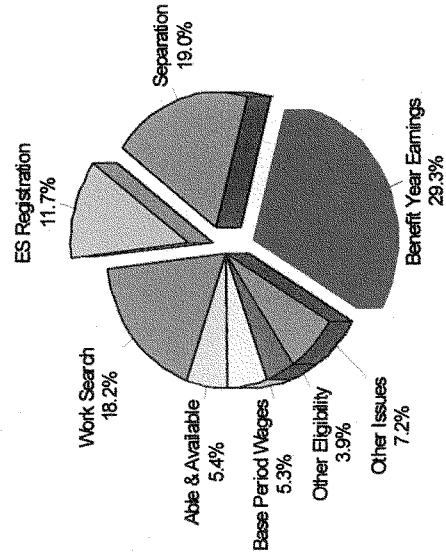
STATE FOCUS

Strategic Framework:

- 1) Prevention strategies for three of the largest and controllable root causes:
 - ◆ Claimants continuing to claim benefits after returning to work (Benefit Year Earnings or BYE);
 - ◆ Untimely or inaccurate separation information from employers or their third party administrators; and
 - ◆ Employment Service registration.
- 2) Targeting states with greatest impact on the rate.
- 3) State focus through incentives, new Performance measures, targeted funding, new tools and technology, and technical assistance.

Causes of UI Overpayments

FY 2010 Annual Report Rate



| STRATEGIES | ACTIONS | MILESTONES | METRICS |
|---|--|---|--|
| Benefit Year Earnings (BYE) Strategies | | | |
| <p>#1 Implement New State Performance Measure Focused on Prevention (50% reduction in BYE errors of 5 weeks or more)</p> | <ul style="list-style-type: none"> ✓ Analyze potential measure and develop clear definition and methodology for calculating it ✓ Develop roll-out strategy to include development of policy guidance, identification of new reporting requirement, securing OMB clearance for new reporting requirements, identification of implementation timing, and development of technical assistance strategies. | <ul style="list-style-type: none"> ✓ Performance measure fully defined by April 30, 2011 ✓ Reporting requirements defined and OMB clearance received by December 31, 2011 ✓ UI Program Letter to states announcing new measure by January 31, 2012 ✓ Full implementation of the measure through the State Quality Service Plan (SQSP) process for FY 2013 | <p>100% states in compliance with the standard for the measure resulting in an estimated reduction of the Annual Report overpayment rate by 0.90 percentage points by FY 2015.</p> <p>Note: The metric applies to strategies #1 and #2 and will be re-evaluated in one year.</p> |
| <p>#2 Mandate State Use Of National Directory Of New Hires (NDNH) for Benefit Payment Control (BPC) and Develop Model Standard Operating Procedures (SOP)</p> | <ul style="list-style-type: none"> ✓ Develop model sop for how to utilize NDNH most effectively for prevention ✓ Draft and publish policy guidance ✓ Schedule webinars to | <ul style="list-style-type: none"> ✓ SOP and policy guidance published by May 31, 2011 | <p>100% of states use NDNH as part of BPC by December 31, 2011</p> <p>100% of states use NDNH in accordance with the sop by</p> |

| | | | |
|---|---|--|---|
| | review guidance and feature states best practices for using NDNH for prevention | | June 30, 2012 Notes: • The metric as noted in strategy #1 also applies to #2 and will be re-evaluated in one year after issuance of the policy guidance. |
| #3 Claimant Messaging Campaign to Deter Continued Claims Filing After Return to Work | <ul style="list-style-type: none"> ✓ Work with information technology support center (ITSC) to secure contract support ✓ Inventory current state practices ✓ Develop messaging tools and products for state use ✓ Disseminate tools and products and provide technical assistance | Messaging products/tools developed by September 30, 2011 | 100% of states implement at least on of the products by March 31, 2012 |
| #4 Work Collaboratively with the Partnership Fund for Integrity Innovation to Explore More Timely Data Sources Indicating Claimant's Return to Work | <ul style="list-style-type: none"> ✓ Pilot the use banking information that could help detect when payroll checks are deposited in bank accounts, indicating a claimant has returned to work | <ul style="list-style-type: none"> ✓ Pilot to run for 12 months. Funding received in June 2011. | The pilot is a value test to determine if the information improves how soon states can detect possible return to work by a claimant and the quality of the data for this purpose. |

| Separation Issue Strategies | |
|--|---|
| <p>#5 Significantly Increase State Take Up of the State Information Data Exchange System Implementation (SIDES). SIDES enables Electronic Communication between States and Employers or their Third Party Administrators (TPAs) to Improve Timeliness and Quality of Separation Information.</p> | <p>✓ Aggressively outreach to states and employers to promote implementation</p> <ul style="list-style-type: none"> ✓ Support state development, testing and implementation ✓ Mandate state implementation of SIDES by December 31, 2014 (will require regulation and funding) ✓ Provide Supplemental Budget Request opportunity to states that have not yet committed to SIDES implementation |
| | <p>3 new states fully implemented by July 1, 2011</p> <p>TALX fully implemented by July 1, 2011</p> <p>8 additional states fully implemented by December 30, 2011</p> <p>NOTE: Projected targets are based on state identified target dates for implementation.</p> |
| | <p>70% of states implement SIDES by FY 2015</p> <p>Percentage of improper payments due to separation issues reduced by at least 20% resulting in an estimated reduction in the Annual report overpayment rate by 0.45 percentage points by FY 2016.</p> |
| Employment Service (ES) Registration Strategies | |
| <p>#6 Aggressive and Targeted Technical Assistance and Monitoring of States with the Highest Percentage of ES Registration Improper Payments (TN, AL, NM, OH, FL, CA, TX)</p> | <ul style="list-style-type: none"> ✓ Targeted states informed by letter of plans for ETA to work with them aggressively to lower this portion of their improper payment rate ✓ Targeted states contacted |
| | <ul style="list-style-type: none"> ✓ Letters to states by March 15, 2011 ✓ Calls to 10 targeted states by April 15, 2011 ✓ State specific plans submitted by May 15, 2011 |
| | <p>75% reduction of improper payments due to ES registration in targeted states resulting in an overall reduction of the Annual Report overpayment rate by 0.78 percentage points by</p> |

| | | | |
|---|---|---|----------|
| | personally by UI Administrator and ETA Regional Administrator to examine state specific cause for the problem and to request a formal plan from the state to address it. | | FY 2014. |
| Resource Targeting | | | |
| #7 Integrity Legislation to Provide Additional Resources for States to Perform Integrity Functions and Improve Tools for States to Address Improper Payments. | <ul style="list-style-type: none"> ✓ New FY 2012 budget provision added to require reporting of individuals rehired within 60 days | <ul style="list-style-type: none"> ✓ Legislative language transmitted to OMB on February 11, 2011 ✓ Transmission to Congress by June 13, 2011 | Complete |
| #8 Explore requiring Dedicated Percentage of State UI Administrative Grants for Integrity Activities | <ul style="list-style-type: none"> ✓ Analyze state spending for integrity activities ✓ Identify minimum amount states should spend on integrity from their administrative grants ✓ Consult with states | <ul style="list-style-type: none"> ✓ Decision to proceed made no later than August 31, 2011. | N/A |
| State Focus/Technical Assistance Supporting All Strategies | | | |
| #9 Federal/State | <ul style="list-style-type: none"> ✓ Convene workgroup | <ul style="list-style-type: none"> ✓ Workgroup convened in | |

| | | | |
|---|---|---|--|
| <p>Workgroup to Identify State Improper Payment Prevention Strategies.</p> | <ul style="list-style-type: none"> ✓ Review recommendations for potential implementation ✓ Implementation of most impactful recommendations pending approval and funding | <p>December 2010</p> <ul style="list-style-type: none"> ✓ Initial recommendations identified in January 2011 ✓ Final workgroup report due September 30, 2011 | |
| <p>#10 Support Targeted High Impact States Convening Cross-Agency Task Forces on UI Improper Payments (CA, PA, TX, IL, NJ, NY, MI, WI, NC, OH, and FL)</p> | <ul style="list-style-type: none"> ✓ Identify and notify targeted states ✓ Convene virtual institute with state task forces to support strategic planning for reducing each state's improper payment rate based on their root causes ✓ Provide on going technical assistance to help states implement their improper payment reduction strategies. | <ul style="list-style-type: none"> ✓ Targeted states identified and notified by May 31, 2011 ✓ Virtual Institute scheduled by October 2011 ✓ States finalize state plans by December 31, 2011 ✓ Technical assistance by ETA - ongoing | <p>Reduction in state improper payment rates (actual metric pending further state specific analysis and acquiring baseline data)</p> |
| <p>#11 Enhanced State Quality Service Planning (SQSP) Process To Incorporate New Elements Related to Prevention of Improper Payments</p> | <ul style="list-style-type: none"> ✓ Draft new section of SQSP requiring states to identify state specific root causes and to provide strategies for addressing them ✓ Incorporate the new performance measure | <ul style="list-style-type: none"> ✓ New section focused on reduction of improper payments implemented for FY 2012 SQSP process ✓ Requirement that states identify specific resources for corrective action plans associated with improper | <p>100% states provide strategies for reducing improper payments in their FY 2012 SQSP</p> <p>100% of states failing to meet the new performance standard focused on</p> |

| | focused on prevention into the FY 2013 SQSP process by requiring states to provide corrective action plans if they fail to meet the performance standard | payments implemented for FY 2013 SQSP process | prevention will provide corrective action plans in the FY 2013 |
|---|--|--|--|
| #12 Assist Targeted States in Taking Advantage of Supplemental Budget Reductions in the State's Improper Payment Rate | <ul style="list-style-type: none"> ✓ Identify targeted states ✓ Encourage targeted state submission of SBR requests ✓ Execute grant modifications ✓ Monitor project implementation | <ul style="list-style-type: none"> ✓ States provided SBR funds to improve targeted integrity activities by September 30, 2011 | TBD based on state strategies |
| #13 Ongoing Technical Assistance | <ul style="list-style-type: none"> ✓ Targeted collection of integrity best practices ✓ Best practices disseminated system-wide ✓ Series of integrity webinars featuring best practices during calendar year 2011 ✓ Bi-annual Integrity Conference held in April 2012 (pending approval and funding availability) | <ul style="list-style-type: none"> ✓ Integrity best practices identified by September 30, 2011 and disseminated by December 31, 2011 ✓ Series of Integrity Webinars throughout Calendar Year 2011 ✓ Integrity Conference held in April 2012 with 100% state attendance (Pending Approval/Funding) | |

**Responses of Assistant Secretary of Labor Jane Oates to Questions for the Record
of the Committee on Finance of the United States Senate, June 22, 2011**

Senator Max Baucus:

Questions for the Witness:

Difficulty Recovering Overpayments

The Treasury Offset Program (TOP) was created by legislation in 2008 and amended federal law to permit states to recover certain UI debts due to fraud from federal income tax refunds. Last year, we passed the Claims Resettlement Act of 2010, which expanded the TOP to recover non-fraud overpayments, uncollected employer contributions, and associated penalties and interest. Yet, even with these enhancements to recovery efforts, we only received a savings score of \$2.6 Billion with the Congressional Budget Office.

1. *Why have we not been able to recover more of the funds that went to overpayments?*

The Department is very pleased to have the enhanced authority to use TOP to recover Unemployment Insurance (UI) overpayments as well as the work start date for the National Directory of New Hires. CBO in fact scored these provisions as saving \$4.9 billion in outlays over ten years, offset by \$2.2 billion in decreased revenues as States responded by lowering their UI taxes.

In order to recover overpayments, states must invest significant manpower to detect and validate that an overpayment has occurred. As I mentioned in my testimony, during the course of the recession, many state integrity staff were needed to process the overwhelming numbers of UI claims. As a result, fewer overpayments were formally established and ultimately set up for collection during the course of the recession.

The tools states have to recover overpayments include setting up voluntary payment plans with the claimant, offsetting future UI benefit payments, putting liens on property, and garnishing wages. All of these activities are workload intensive. In addition, some states offset state income tax returns and lottery winnings as a recovery strategy.

We are pleased that states now have the ability to offset UI debts against Federal income tax refunds through the TOP, which has been collecting delinquent debts on behalf of Federal and State agencies since 1996. All the necessary regulations and processes were in place for states to begin offsetting starting in February 2011. Three states—Michigan, New York, and Wisconsin—were positioned to quickly implement TOP during the 2011 tax season and successfully recovered \$25 million. Several states have changed their laws to authorize them to use the TOP, and others may have to do so before taking advantage of the program to collect overpayments. In addition, states must comply with Internal Revenue Service processes for submitting debts,

which requires time and resources for states to accomplish. For three states, Georgia, Texas and Virginia, this is particularly problematic and may not allow them to utilize the TOP program because the information technology systems of those states are totally supported by private contractors; Internal Revenue Code (IRC) Section 6103 prohibits the sharing or disclosure of tax returns and return information prepared or received pursuant to Title 26 to non-state staff unless a specific exception applies under IRC Section 6103. The Department is aggressively promoting state implementation of TOP as soon as feasible, including the provision of funds to states for their implementation costs.

It is important to note that not all overpayments are controllable. In addition to an overall improper payment rate for all causes, the Department identifies an operational rate, which represents the overpayments states could be reasonably expected to detect and establish for recovery. The operational overpayment rate is around 6 percent.

2. *Given that over 10 percent of UI funds are going to overpayments, should states be allowed to use recovered funds for purposes outside of integrity activities?*

Under current Federal law, states are prohibited from using recovered overpayments for anything except payment of UI benefits. The only program integrity funding available to states is from the Federal UI administrative grants, special Reed Act distributions, and the supplemental UI funding that has been provided to states.

Having resources to support integrity activities is important to ensure that states are engaging in these critical activities. The Integrity Act proposed by the Department includes provisions permitting states to use up to five percent of each overpayment recovered to augment administrative funding for preventing, detecting, and recovering benefit overpayments. Similarly, states would be permitted to use up to five percent of delinquent contributions collected for preventing and detecting employer fraud and evasion, and recovering required employer contributions, including the misclassification of employees as independent contractors and the identification of employers who attempt to manipulate the taxing provisions to pay less than their fair share of contributions. We do think that, other than for benefits, the use of recovered funds should be limited to integrity activities; however, we would construe these activities broadly to encompass other good ideas.

I would note that other federal programs permit retention of up to 50 percent of recovered funds. That high a percentage would not be appropriate for the UI program, given that employer payroll taxes are the source of the funding. Returning most of the monies recovered to the states' accounts in the UTF increases states' solvency which, in turn, may affect employers' taxes and surcharges.

3. *What, in your opinion, is the best approach?*

The provision in the Integrity Act that will allow states to use up to five percent of the recovered funds due to overpayments, delinquent taxes, and those employers who

willfully misclassify workers or otherwise engage in illegal tax avoidance, will provide more resources to support prevention and recovery activities and generally will be an incentive to states to improve their recovery efforts.

The UI program was designed as a federal-state partnership under which states were afforded flexibility to implement program details within broad federal requirements; that approach has served as the foundation upon which the present UI system is built. Over the history of the program, the federal government has provided incentives and guidance to states to achieve policy objectives but allowed states to decide how to structure their programs. We believe that approach is still valid.

Senator Ron Wyden:
Questions for the Witness:

1. *In April of last year, the New York Times ran an investigative front page story on TALX (“Contesting Jobless Claims Become a Boon Industry” April 3, 2010), a business which challenges UI claims and appeals on behalf of other employers, covering almost 30 percent of all the claims filed in the U.S. Based on interviews and a sample of state data collected by the U.S. Department of Labor, it found that this company -- which contracts with many of the nation’s largest employers – is often responsible for filing late and frivolous appeals, unfairly triggering overpayment determinations for workers and backing-up the strained state unemployment programs. Would you agree that there is a serious issue with TALX and other third-party representatives?*

States have reported that third-party representatives have in the past been responsible for the failure by many employers to provide timely and adequate information to state UI agencies to permit the agencies to correctly determine eligibility for benefits. However, they are not solely responsible for the lack of timely or adequate information to determine claimant entitlement to benefits. Individual employers are frequently responsible by ignoring the separation report when it comes in, setting it aside and failing to return it, or failing to provide the state UI agency with a correct address to which documents should be mailed.

We note that TALX has been an active partner in the implementation of the State Information Data Exchange System (SIDES) and went live with SIDES on June 28, 2011. SIDES is designed to improve timeliness and adequacy of information provided by employers and their third parties, which will avert filing of appeals and help prevent improper payments.

If so, does the Administration’s proposed Program Integrity Act go far enough to prevent these abuses (the act allows the states to “charge” the EMPLOYER for the overpaid benefits but only if the state can show there’s a “PATTERN” of failing to provide the necessary employer information on time)? Would the Administration consider additional measures to prevent these abusive practices

that contribute to UI overpayments? For example, shouldn't the third-party firms be separately regulated? Why not require them to register with the state, meet acceptable rules of conduct, and impose penalties for those that abuse the system? And why shouldn't all charges that directly result from late-filed information be charged to the employers, especially given the limited resources of the states to go up against companies like TALX and prove that a given situation rose to the level of a "pattern" of abuse. That's a very high burden for states to prove, and it may substantially dilute the provision.

Some states have enacted laws to regulate the third-party entities. Those laws may require that the third-party representative register with the state UI agency, and generally provide for penalties against either or both third-party representatives and employers for failing to provide timely or adequate separation information. Those penalties may include a provision that would require benefits paid erroneously due to the employer's failure to participate or to participate meaningfully at the initial determination stage be charged against that employer's account. We believe the matter of third-party entities is best left to the states under the federal-state partnership.

The term "pattern of abuse" as used in the Integrity Act would establish a minimum standard states would have to use to determine whether to assess penalties against third-party representatives and/or the employers they represent. States could impose stricter standards. States are now, and would be under the Integrity Act provision, free to assess penalties against any employer or third-party representative who fails to show good cause for failing to provide timely or adequate separation information.

The "pattern of abuse" provision also was included in order to avoid penalizing a small "mom and pop" business for a single mistake due to misunderstanding the reporting requirement.

It is my understanding that the Department of Labor is concerned about overpayments in Oregon, but often the overpayments are a result of delays on the part of the employer or third party and the judgment call that in the case of delays, UI applicants should receive their benefits while waiting. Would you agree that in these cases, it is unfair to punish a laid off employee through delay or denial of benefits when the delay is caused by their former employer?

Yes, we agree that delaying benefits to a laid-off employee because the employer failed to provide information on the reason for the separation from employment would be unfair to the individual. The U.S. Supreme Court, in California Human Resources Development Department v. Java, 402 U.S. 121 (1971), addressed the issue of delayed benefits when employers filed appeals. There the issue was whether California could suspend payment of benefits when the employer filed an appeal from an agency adjudication of eligibility. The Court held that suspending benefits under these circumstances was impermissible, and that states were

required to pay benefits as soon as administratively feasible. The failure of employers and third-party entities to respond timely and adequately to the states' request for separation information may result in states' being forced to make an eligibility determination that may subsequently lead to an employer appeal of a finding of eligibility for benefits, and a reversal based on new information made available to the state agency.

As a result of that decision, the Department developed standards, found at 20 CFR Part 640, for making the first payment on a claim following the date the claim was filed. The regulations also provide standards for determining the timeliness of subsequent payments when an issue arises that raises a question of the individual's eligibility. States must balance the requirement that they meet timeliness standards for payment of benefits against the need for additional information from employers and third-party entities and must use the best information available to them while meeting the requirement to make payment when due.

2. *I appreciate the Department's efforts in the proposed program integrity legislation, but am concerned over the requirement that the State agency determine that the employer or agent has engaged in a pattern of untimely or inadequate responses to requests for information. This is a very high burden for states to be able to prove. Would you consider requiring that the burden of proof be placed on the employer or third party representative?*

We agree that the evidentiary burden of proving a pattern of delay may increase the administrative burden for states. However, SIDES will help provide information on patterns of delay to help states prove a pattern exists. The policy behind requiring a pattern of behavior is to avoid penalizing employers who make a one-time mistake. Requiring that all employers who fail to provide timely information be penalized is likely to adversely impact small businesses more than large businesses with personnel departments and/or third party administrators. Shifting the burden to employers or third-party administrators does not appear to be a viable option because it would still require verification by the state agency.

3. *With all the serious and important focus on recovering overpayments, what more could the federal government and the states be doing to ensure that workers are not innocently swept up in non-fraud or fraud overpayment determinations, and ensure there's a balanced approach toward program integrity? For example, the vast majority of states require that non-fraud overpayment determinations be waived in appropriate cases? Should all states have similar provisions to help workers who are already financially destitute and have done nothing to contribute to the overpayment?*

Many states differentiate between fraud and non-fraud overpayments. For example, some states prohibit individuals determined to have engaged in fraud from receiving benefits for a period of time and, in at least one state until the

overpayment is repaid. This penalty does not apply to non-fraud overpayments. Nearly all states currently provide some measure of relief from non-fraud overpayment liability depending on the individual's circumstances and the reason for the overpayment, based on an "equity and good conscience" standard, which we believe is a sound practice. We believe that whether to relieve individuals of overpayments in some circumstances is a decision generally best left to states.

Senator Tom Coburn:
Questions for the Witness:

I have attached a copy of a letter that I sent to the Department of Labor, April 2011, for your consideration.

1. *The rising level of improper payments in the Unemployment Insurance program – \$17.5 billion in 2010 alone – is concerning. A September 2010 report of the Inspector General (IG) reported on shortcomings of the Department's efforts to combat improper payments.¹ More specifically, the IG found that the Department's reduction plan did not include specific targets for reducing Improper Payments; sufficient details regarding meeting the targets; and supporting analysis related to the implementation initiatives and expected impact. What's more, the IG found the Department's methodology did not evaluate the entire population of Unemployment Insurance programs and may not have identified the total extent of individually significant improper payments. What actions has the Department taken since the issuance of this report to address the specific concerns of the IG? If concerns of the IG have not been addressed or recommendations fulfilled, please explain why.*

The four main reasons for UI overpayments are:

1. Payments made to individuals who continue to claim benefits after they have returned to work;
2. Information about the claimant's separation from work is received after a claim is paid, often due to failure of employers or their representatives to provide timely and adequate information on the reason for an individual's separation from employment;
3. The inability to validate that the individual has met the state's work search requirements; and
4. The failure to register the claimant with the state's employment service pursuant to the state's law.

Collectively these causes account for over 78 percent of all overpayments.

¹ U.S. Department of Labor, Office of Inspector General, "Review of Report on Improper Payments in the Unemployment Insurance Program," Report Number 22-10-020-03-315, September 30, 2010.

In response to these unacceptable levels of improper payments, the Department has developed a Strategic Plan that focuses on the major root causes of improper payments. This comprehensive plan provides specific strategies, actions, milestones and metrics that the Department is aggressively implementing and tracking. The goal is to reduce UI improper payments as quickly and as to as low a level as possible to meet the requirements of the Improper Payments Information Act of 2002 (IPIA), as amended by the Improper Payments Elimination and Recovery Act of 2010. The Department's reduction targets – which are driving our efforts to reduce improper payments in UI – are as follows:

| Measure | FY 2011 | FY 2012 | FY 2013 |
|----------------------|---------|---------|---------|
| Annual Rate | 9.80% | 9.70% | 9.60% |
| Operational Rate | 5.10% | 5.10% | 5.10% |
| ES Registration Rate | 1.15% | 1.15% | 1.15% |

Improper payments are estimated from the Benefit Accuracy Measurement (BAM) survey, which includes the three largest permanently authorized UC programs – state UI, Unemployment Compensation for Federal Employees (UCFE), and Unemployment Compensation for Ex-Servicemembers (UCX). The BAM is a statistically sound survey that provides accurate and reliable estimates of improper payments in the UI program; OMB has frequently held BAM out as an example of an effective monitoring program. BAM meets or exceeds the requirements established by OMB in OMB Circular A-123, Appendix C, for measuring and reporting improper payments for IPIA. The Department documents the BAM methodology in its annual IPIA report to OMB, which is published in the Department's annual Agency Financial Report (AFR).

To address the IG finding about the limitation of the BAM survey, the Department is modifying the Overpayment Detection and Recovery Activities report (ETA 227) to obtain a more accurate count of the number of UI claimants in the population who have received high dollar overpayments as defined by OMB. Because requests to modify data collection systems must be submitted for approval to OMB under the Paperwork Reduction Act, these data will not be available until the first quarter of calendar year 2012 at the earliest.

Reducing the UI improper payment rate and improving recovery of overpayments is a top priority for the Department and we are working closely with the Office of Management and Budget and our state partners to identify and implement aggressive strategies to bring the rate down. Our strategies are focused on root causes where there is greatest potential to prevent improper payments.

2. In November 2010, the Department of Labor was unable to submit information necessary to receive a qualified, or "clean," audit.² This initial audit showed the Department could not record in a timely manner the majority of transactions

² FY 2010 Agency Financial Report, November 15, 2010, <http://www.dol.gov/sec/media/reports/annual2010/2010annualreport.pdf>.

related to the Unemployment Trust Fund and could not reconcile the underlying supporting data for certain unemployment Trust Fund balances to the general ledger in a timely manner. While the Department later received an unqualified audit after re-submitting the necessary information, the clean audit still contained four material weaknesses and two significant deficiencies. As it relates to the Unemployment Program, please describe what the Department is doing to address the specific problems identified by KMPG in the FY 2010 Agency Financial Report, and the progress made implementing the related recommendations of the auditor and Inspector General.

In the unqualified opinion received on the resubmitted financial statements, the auditors did not re-evaluate the status of the four material weaknesses. Of the four material weaknesses, three were related to financial reporting. Management did not agree with the fourth material weakness related to department-wide systems access controls.

There were two material weaknesses that included issues related to accounting for the Unemployment Trust Fund (UTF):

1. Lack of Sufficient Controls over Financial Reporting.--The Department has made the following improvements. As noted in the reissued unqualified audit report, as of September 30, 2010, all significant differences and or amounts were properly reconciled and reported in the financial statements.

a. To help eliminate the weakness in interfaces between the general ledger and subsystems, the Department has worked to resolve issues with the interfaces and improved communication and coordination with the U.S. Department of the Treasury's Bureau of Public Debt (BPD). As a result, the Department has improved the timeliness and accuracy for recording UTF data into the New Core Financial Management System (NCFMS).

b. To help eliminate the weakness in accounting resources, the Department has documented the policies and procedures for the UTF accounting cycle. The Department has also included key UTF activities, transactions, and accruals (e.g., repayable advances, accounts receivable, and transfers) in quarterly schedules of accounting cycle activities. Furthermore, the Department has implemented policies and procedures for supervisory reviews to ensure the accuracy of UTF transactions posted to NCFMS and the sufficiency of documentation for the postings using both preventive and detective internal controls.

2. Lack of Sufficient Controls over Budgetary Accounting.--To help eliminate the weakness in the accounting for UTF non-expenditure transfers, the Department has communicated with Federal financial management experts on the appropriate accounting and reporting for the unique transactions of the UTF. The Department has worked with the U.S. Department of the Treasury's Financial Management

Service (FMS) and the Office of Management and Budget (OMB) to document accounting scenarios for UTF activity to ensure compliance with the U.S. Standard General Ledger accounting and OMB reporting requirements (e.g., repayable advances). The specific transactions noted by the auditors were properly classified and reported as of September 30, 2010.

3. In September 2010, the Inspector General reported that \$4 billion in stimulus funds designated for Unemployment Insurance program modernization had not yet been spent, and that \$1.3 billion was “unlikely to be applied for by states.” Please provide an update as to the use of this funding. How much of this money has yet to be spent and applied for?³

Since the Inspector General’s report was issued several states have applied for and received UI modernization funds. As of July 1, \$4,366,743,353 of the \$7 billion set aside for incentive payments has been disbursed to 40 states, leaving \$2,633,256,647 available for distribution. In addition, the Department is working with two other states that anticipate submitting applications for, and being awarded, incentive funds before the September 30, 2011 deadline. Should those two states be awarded their remaining incentive funds – an additional \$50,526,355 – the total disbursed would exceed \$4.4 billion. Any remaining funds that have not been distributed to the states by September 30, 2011 will become available in the Federal Unemployment Account in the Unemployment Trust Fund for advances (loans) to states to pay UI benefits.

Under the terms of the Recovery Act, states may use their UI modernization funds for payment of UI or, if appropriated by the state legislature, for administration of their UI law or public employment offices. As of July 1, \$2,561,383,500 of the \$4,366,743,353 had been expended with \$2,515,423,265 being used to pay UI and \$45,960,235 for permissible administrative expenses. Of the amount provided to states, \$1,805,359,853 remains, and of those funds, \$342,105,102 is reserved for permissible administrative purposes by seven of the states (Arkansas, California, Michigan, New York, North Carolina, Ohio, and Rhode Island).

4. In a letter to Secretary Solis dated April 14, 2011, I raised concerns about a number of program integrity issues within the Unemployment Insurance program, and asked to learn more about the Department’s plan to each of these issues. The letter highlighted the problem of overpayments, and instances where benefits were given to dead people, prisoners, illegal aliens, state employees fired for misconduct, people on disability and people who continued working. The letter also highlighted ways that funds were being inappropriately used, although perhaps not misused technically within the letter of the law – such as \$60,000 in funds being used to buy a painting depicting labor strikes. I look forward to the

³ U.S. Department of Labor Inspector General, “Recovery Act: More Than \$1.3 Billion in Unemployment Insurance Modernization Incentive Payments Are Unlikely to Be Claimed by States,” September 30, 2010, <http://www.oig.dol.gov/public/reports/oa/2010/18-10-012-03-315b.pdf>.

Department's detailed response to this letter by August 1, 2011, as requested in the original letter.

The Department's detailed response was transmitted on August 1, 2011.

5. *The Administration's proposal to curb waste, fraud and abuse in the Unemployment Insurance program ("The Unemployment Compensation Program Integrity Act of 2011") would amend current law to require "tangible evidence" of a work search only be submitted upon the request of the State agency in charge of awarding Unemployment Compensation. Since this provision would effectively lower the bar of evidence that is required of UI applicants, please explain how the Department plans to ensure that work search requirements are upheld and not abused or neglected if this requirement were to become law?*

The requirement that an individual provide "tangible evidence" of a work search is in section 202(a)(3)(E)(ii) of the Federal-State Extended Unemployment Compensation Act of 1970, and applies only to EB and EUC claims. Thus, a change in this provision (that individuals need only keep the evidence and produce it when asked) would not apply to a claim for regular UI. We do not believe that permitting the individual to retain the tangible evidence until it is requested, rather than submitting it with each week's claim, would "lower the bar."

The requirement to provide tangible evidence of a work search was enacted when states took claims in person or via mail with a paper continued claim form. At that time an individual could simply attach the tangible evidence to the form and return it to the state UI agency. Since the mid 1990s, states have been taking claims telephonically via a voice response system (VRS), or over the Internet by filling out the online form. In either case, there is no established mechanism for providing tangible evidence of a work search. Simply mailing the tangible evidence to the state agency does not ensure that it will be matched up with the VRS claim or Internet information. The potential for delay in paying benefits when due while the state attempts to match records is significant.

Moreover, there is no indication that requiring that individuals maintain tangible evidence of a work search would result in an increase in improper payments for EUC and EB claims. This provision is equivalent to the state agency's verification of work search for regular claims.

6. *During the current economic downturn, many states have borrowed funds from the federal government to meet their Unemployment Compensation program obligations. As a result, 32 states currently owe Treasury in excess of \$44 billion. Whether a state trust fund balance is "minimally solvent" is up to each state - there is no federal statutory requirement of an adequately funded UC program. Do you think there should be a federal requirement that state trust funds have a level of reserves deemed adequate? If so, what would the Department*

recommend such a minimum requirement be? What was the reserve balance of each state (and applicable U.S. territories) at the start of calendar year 2007 and 2008? What is the current reserve of each state's (and applicable U.S. territories) trust fund?

With respect to solvency, the Department has supported a 1997 recommendation from the Advisory Council on Unemployment Compensation that states achieve an average high cost multiple (AHCM) of 1.00 to be adequately prepared for a recession. Recently published regulations, as required by section 1202(b)(2)(C) of the Social Security Act, make an AHCM of 1.00 one of the requirements for a state to receive a short-term interest-free advance to pay UI benefits.

Attached is a table displaying the reserve balances of states at the start of calendar years 2007 and 2008, and the balances of states, net of loans, as of July 31, 2011.

| | 12/31/2006 | 12/31/2006 | 12/31/2007 | 12/31/2007 | 7/31/2011 |
|---------------------|-------------------------------|----------------------------------|-------------------------------|-------------------------------------|-------------------------------|
| | Fund Balance (minus loans) | Average High Cost Multiple | Fund Balance (minus loans) | Average High Cost Multiple | Fund Balance (minus loans) |
| Alabama | \$417,411,340 | 0.55 | \$410,639,517 | 0.52 | -\$48,805,007 |
| Alaska | \$284,519,802 | 0.99 | \$331,213,927 | 1.07 | \$234,733,620 |
| Arizona | \$905,039,770 | 1.07 | \$990,481,050 | 1.12 | -\$255,752,692 |
| Arkansas | \$168,706,047 | 0.38 | \$151,132,463 | 0.32 | -\$223,394,670 |
| California | \$2,400,802,072 | 0.27 | \$2,533,133,317 | 0.27 | \$8,474,406,256 |
| Colorado | \$494,600,826 | 0.56 | \$630,396,665 | 0.67 | -\$292,737,849 |
| Connecticut | \$593,732,272 | 0.57 | \$598,111,153 | 0.54 | -\$520,232,851 |
| Delaware | \$192,477,399 | 1.02 | \$174,156,326 | 0.90 | -\$34,233,902 |
| Dist of Columbia | \$376,861,480 | 1.12 | \$400,275,361 | 1.10 | \$321,945,281 |
| Florida | \$2,290,913,150 | 1.12 | \$2,203,888,727 | 1.05 | \$1,585,627,365 |
| Georgia | \$1,272,513,977 | 1.02 | \$1,281,787,070 | 0.98 | -\$470,591,182 |
| Hawaii | \$530,814,668 | 1.90 | \$556,333,926 | 1.88 | -\$8,150,246 |
| Idaho | \$180,067,146 | 0.45 | \$196,048,184 | 0.47 | -\$103,475,502 |
| Illinois | \$1,280,862,814 | 0.26 | \$1,801,982,831 | 0.35 | \$2,206,334,784 |
| Indiana | \$477,322,905 | 0.46 | \$306,787,308 | 0.29 | \$1,908,413,533 |
| Iowa | \$695,731,773 | 0.87 | \$740,177,507 | 0.88 | \$355,431,398 |
| Kansas | \$603,853,027 | 0.97 | \$637,982,983 | 0.97 | -\$13,900,413 |
| Kentucky | \$263,918,644 | 0.26 | \$230,766,405 | 0.21 | -\$816,239,286 |
| Louisiana | \$1,371,467,550 | 0.96 | \$1,444,768,251 | 0.94 | \$856,469,941 |
| Maine | \$463,521,480 | 1.64 | \$479,164,242 | 1.64 | \$260,273,617 |

| | | | | | |
|----------------|-----------------|------|-----------------|------|-----------------|
| Maryland | \$1,018,371,345 | 0.82 | \$1,016,659,433 | 0.79 | \$460,277,372 |
| Massachusetts | \$994,344,531 | 0.41 | \$1,290,297,483 | 0.50 | \$210,190,847 |
| | | | | | - |
| Michigan | \$112,345,823 | 0.03 | -\$103,489,247 | N.A. | \$3,015,153,485 |
| Minnesota | \$396,108,248 | 0.29 | \$545,587,315 | 0.38 | -\$395,723,672 |
| Mississippi | \$732,491,542 | 1.78 | \$727,917,633 | 1.70 | \$359,987,532 |
| Missouri | -\$29,125,630 | N.A. | \$113,246,232 | 0.12 | -\$702,688,317 |
| Montana | \$250,436,508 | 1.41 | \$280,511,903 | 1.45 | \$101,774,555 |
| Nebraska | \$233,698,137 | 1.06 | \$278,865,066 | 1.19 | \$262,775,029 |
| Nevada | \$728,363,997 | 0.99 | \$793,215,432 | 1.02 | -\$717,860,609 |
| New Hampshire | \$265,248,515 | 1.35 | \$240,422,129 | 1.19 | \$67,543,330 |
| | | | | | - |
| New Jersey | \$693,637,682 | 0.23 | \$650,448,688 | 0.21 | \$1,562,401,670 |
| New Mexico | \$578,167,938 | 2.03 | \$575,524,055 | 1.88 | \$168,508,800 |
| | | | | | - |
| New York | \$313,162,079 | 0.07 | \$429,722,589 | 0.09 | \$2,969,748,901 |
| | | | | | - |
| North Carolina | \$186,570,127 | 0.12 | \$394,426,200 | 0.23 | \$2,381,027,438 |
| North Dakota | \$119,470,536 | 0.75 | \$134,441,676 | 0.79 | \$95,128,833 |
| | | | | | - |
| Ohio | \$499,579,845 | 0.14 | \$444,529,523 | 0.12 | \$2,021,860,162 |
| Oklahoma | \$747,654,628 | 1.44 | \$831,387,875 | 1.51 | \$354,850,691 |
| Oregon | \$1,737,202,696 | 1.38 | \$1,933,224,529 | 1.46 | \$931,450,967 |
| | | | | | - |
| Pennsylvania | \$1,383,463,734 | 0.28 | \$1,545,651,574 | 0.30 | \$2,763,192,184 |
| Puerto Rico | \$525,623,317 | 1.02 | \$529,259,719 | 1.00 | \$328,726,404 |
| Rhode Island | \$193,196,145 | 0.47 | \$159,901,128 | 0.38 | -\$234,672,452 |
| South Carolina | \$251,314,916 | 0.34 | \$199,183,309 | 0.26 | -\$748,415,680 |
| South Dakota | \$19,503,961 | 0.28 | \$24,679,928 | 0.33 | \$29,987,129 |
| Tennessee | \$634,284,904 | 0.56 | \$566,160,824 | 0.48 | \$329,171,552 |
| Texas | \$1,432,245,420 | 0.39 | \$1,774,693,730 | 0.45 | \$791,255,216 |
| Utah | \$706,139,789 | 1.35 | \$842,680,347 | 1.47 | \$302,161,644 |
| Vermont | \$195,302,812 | 1.36 | \$177,612,716 | 1.20 | -\$39,058,435 |
| Virgin Islands | \$29,395,757 | 1.14 | \$22,287,451 | 0.80 | -\$23,613,751 |
| Virginia | \$713,061,845 | 0.67 | \$775,202,393 | 0.71 | -\$145,147,295 |
| Washington | \$3,112,285,887 | 1.36 | \$3,794,156,088 | 1.53 | \$2,510,603,586 |
| West Virginia | \$242,450,987 | 0.46 | \$244,785,506 | 0.45 | \$98,253,108 |
| | | | | | - |
| Wisconsin | \$733,017,000 | 0.38 | \$592,228,165 | 0.29 | \$1,306,805,283 |
| Wyoming | \$216,070,430 | 1.14 | \$243,500,141 | 1.15 | \$137,931,613 |



**Testimony Submitted to the U.S. Senate Committee on Finance
Preserving Integrity, Preventing Overpayments and Eliminating Fraud
in the Unemployment Insurance System**

Testimony Submitted by Paul Trause, Washington State Employment Security Commissioner

June 22, 2011

Thank you Chairman Baucus, Ranking Member Hatch and members of the committee for the opportunity to testify today before the Finance Committee on the State of Washington's unemployment insurance system integrity efforts. I am Paul Trause, Commissioner of the Washington Employment Security Department.

As you may have heard over the course of the recession, Washington State has one of the healthiest and most stable unemployment benefits fund in the nation. Employers in our state have been willing to make the investment necessary to keep this fund healthy, in part, because of the high value we place on integrity. To ensure this trust, it is critical we preserve a level playing field for businesses and ensure claimants receive only the benefit to which they are entitled.

The vast majority of benefit overpayments and unpaid taxes are not due to fraud. In my state, 93 percent of our registered employers pay their taxes on time, and less than 5 percent of regular benefits are overpayments. Most of the issues we see are the result of errors and confusion. For example, fraud accounted for less than one half of 1 percent of regular benefit payments in 2010.

Fraud Detection

Let me first discuss fraud detection. In the past few years, our state legislature and Governor have worked to improve our laws and provide us with the framework required to pursue those employers and claimants who seek to defraud the system.

The state legislature has established clearer definitions of fraud – as well as a graduated penalty structure for claimants committing fraud. In addition to having to pay back fraudulently obtained benefits, claimants on the first occurrence of fraud are denied the possibility of receiving benefits for 26 weeks. For the second occurrence of fraud, they serve a 52 week denial period and are charged a 25% penalty of the amount overpaid. For third and subsequent occurrences of fraud, claimants are denied benefits for 104 weeks and must pay a 50% penalty. We believe that this approach serves as an active deterrent.

The Employment Security Department has also worked closely with the Legislature to strengthen laws curbing abuses by businesses seeking to “dump” their state unemployment insurance tax history and escape paying the taxes that they owe. We have also participated actively with the Legislature and multiple state agencies on a multi-year Underground Economy Task Force that targets businesses who gain unfair advantage by not covering their workers with legally required benefits and shirking their tax obligations.

Employers caught trying to manipulate their tax rates must pay the taxes they owe, late payment penalties, and late payment interest. They could also pay up to 10 times the difference between the amount of taxes they should have paid and the amount they did pay. They can then be assigned the delinquent tax rate, and must pay audit costs along with any related collection fees. Recommending schemes that help employers evade their taxes also is against the law. Offenders face a penalty of up to \$5,000 per incident, plus audit costs and collection fees.

The Importance of Technology

We rely heavily on technology to implement our fraud fighting efforts. First, we regularly cross-match unemployment-insurance recipients against databases to identify individuals who either are ineligible, concealing wages or not able to engage in a legitimate job search. The matches we use include :

- National Directory of New Hire
- Department of Labor and Industries (Workers' Compensation)
- Department of Health (obituary)
- Department of Corrections
- Social Security Administration
- Employment Security Benefit Wage
- ESD employee cross match

These matches are responsible for uncovering half of all fraud related claims we uncover. We strongly support expanding the new hire database to include rehires.

Washington has established a unit that “mines” the data available to us to uncover organized fraud. For example, this group will identify instances where the same phone is used to file multiple claims, multiple claimants are claiming from a single address, the same Social Security number is being used in different fraudulent claims, and attempts are being made to obtain information from our system that indicate identify theft or preparation to file a fraudulent claim.

Another example of the importance of technology is our upgraded investigative case management system that allows us to direct investigations through fast path (no investigator necessary) and full path with full investigator involvement. This computer based systems is very efficient, enabling our investigative unit, the Office of Special Investigations (OSI) to complete the greatest number of investigations and reduce the amount of money leaving the trust fund fraudulently.

Although not high-tech, we use toll-free hot lines and our website to solicit tips from the public and other employers. These tips account for 17 percent of our investigations of claimant fraud and about 2.5 percent of our tax audits.

OSI's investigative efforts have been very successful, with \$21.7 million dollars in overpayments detected by OSI in 2010.

Focused Audits of Employers

Audits are the primary tool we use to uncover employer fraud. Again, just as with workers, the vast majority of employers act responsibly. They want to pay what they owe. However, the department has a very active audit program to identify employers who are not paying their share. In 2008 we moved from scheduling audits based largely on random selection to an audit selection process designed to focus on employers who appeared likely to be misclassifying employees or not reporting wages.

The focused audit program stems from a legislative task force created by Governor Christine Gregoire in 2006. The task force was created to address the problem of an underground economy of businesses. These businesses typically are not licensed, do not pay workers compensation, do not contribute to unemployment insurance, and/or fail to pay taxes. This underground economy creates an unlevel playing field; businesses playing by the rules are placed at a competitive disadvantage (particularly in the construction industry). Additionally, consumers are being disadvantaged by substandard work.

This task force generated two continuing initiatives- a Cross-Agency Referral Committee and Cross-Agency Audit Training. Additionally, the task force's efforts helped us to identify five elements which have proven vital to focusing our audit selection:

- Utilize subject matter expertise
- Collect data
- Track audit results based on audit assignment type
- Identify industry specific compliance and reporting issues
- Emphasize and support Underground Economy audits

These elements create the foundation of our Focused Audit Program, and each has significantly contributed to the identification of misclassified workers and discovery of unpaid taxes in Washington State. All are subject to on-going evaluation of their contribution towards steady growth in audit outcomes. As we evaluate the usefulness of the information generated from each of these elements, our program continues to evolve.

As of 2010 the agency has a wide variety of audit types to address particular issues that may arise. We assign audits by computer matching data, unexplained changes in information reported to us, past audit experience, and staff knowledge. We also have forged much closer working relationships with other

state taxing agencies including the Departments of Revenue and Labor and Industries to identify businesses that are completely unregistered. Audit types include:

- Industry: Targeted by NAICS codes
- Blocked Benefit Claims: Generated from unemployment claims
- Random: Randomly selected per USDOL requirements
- Underground Economy: audits requested by tax investigations
- 1099: Generated from IRS leads
- Request: Requested by a District Tax Office
- Labor & Industries: Cross Agency Lead
- Department of Revenue: Cross Agency Lead
- Follow-up: District Tax Office request generated from a previous audit
- Large Payroll Company: Newly created category based on recent USDOL requirement changes
- Out-of-State: Business that use an out-of-state payroll company and therefore categorized as out-of-state but have an in-state location
- State Unemployment Tax Act (SUTA) Dumping: Employers who have a large percentage of the same employees one quarter as a different employer did for a prior quarter

We continue to revisit our audit assignment distribution. Our most recent data indicate that Underground Economy audits lead in discovering misclassified employees as well as additional taxes. We are in the process of formulating and proposing changes based on this information as well as the new U.S. Department of Labor Effective Audit Measure which will be mandatory as of 2014. For the future, we have plans to take all of the data from audit outcomes and other sources and combine it to identify indicators that point to likely audit candidates – not by industry, but by individual business.

As a result of Washington's enhanced audit program:

- We found 102 percent more misclassified workers and 60 percent more unreported taxes in 2010 than in 2009.
- The agency discovered 15,527 misclassified employees; 5,229 of those employees were from underground economy audits.
- In 2010, the Employment Security Department discovered over \$2.9 million in unpaid taxes from audits and investigations; \$1.65 million taxes from underground economy audits.

Deterrence through the Media

Regardless of the source of fraud, we believe that actively publicizing successful fraud prosecutions can work as a deterrent to future fraud. Because of confidentiality restrictions, we are limited in what we can report to the media – but recently, we had great success with a story about a claimant who stated that she was actively looking for work while she was out of state getting married. We couldn't use her

name, but the image of a woman stopping at a movie theater to apply for a job – while on the way to her wedding – captured the imagination of media outlets all over the state, and it generated widespread coverage.

Collecting Overpayments

As in other states, the vast majority of our overpayments to claimants are caused by error, not by fraud. We work aggressively to collect overpayments using existing databases to locate debtors, payment plans to encourage voluntary compliance, and, where that fails, legal tools such as liens and garnishments to compel payments. Washington is investigating entering into the Treasury Offset Program (TOPS) to allow the state access to federal funds to offset outstanding UI debts. We have recently created a small skip-tracing unit that appears to be particularly successful in locating hard-to-find people.

Over the past ten years, we have increased our recoveries by more than 300 percent. Each of our collectors return over \$30 for each dollar we spend. By contrast, the American Collectors Association reports the median recovery is \$1.17 for each dollar spent.

2010 represented a record-breaking year for Washington's collections efforts - \$ 76 million in principal and interest recovered.

Preventing Overpayments

As important as collecting overpayments is, preventing them is more important. We believe there are three keys to preventing overpayments.

The first is improved technology; not just technology to improve our communication with employers, but also the underlying benefit payment systems themselves. Our basic benefit system is more than twenty years old and is mainframe-based. It does not provide the flexibility required to adjust to the demand placed on it by this recession. Our Internet claims system was put in place in 2000 and requires a long list of interface improvements to speed communication with our basic benefit systems and to provide increased edits to ensure information is complete and accessible. If we are given the ability to use recovered overpayments and delinquent contributions to increase integrity, we believe this authority should include the ability to use this money to improve our base technology infrastructure.

The second is education for both employers and claimants so they know what is required of them. We engage in extensive outreach efforts to educate employers - holding more than 70 workshops and forums throughout the state each year. Our statewide accountants and tax-preparer associations have been particularly helpful in our efforts.

We also offer a voluntary audit to review employer records and ensure that they are reporting correctly – without fear of penalty. If the review finds that the employer is not reporting correctly, we will not charge late-payment penalties. However, the employer does still have to pay taxes due and associated interest charges.

Third is the early detection and prevention of issues and speeding people's return to work through aggressive return-to-work assistance. We recognize that we will never have the resources to provide the optimal level of service to each claimant, but we are working to improve the methods we use to review claimants' job searches, assess their skills within the context of the labor market, and help them better target and carry out their job searches. We believe this is crucial to our ability to combat overpayments. In 2009, a peer-reviewed study by our labor market information branch revealed that these efforts returned people to work more quickly and increased earnings. From June 2010 through May of this year, more than 66,000 claimants received a job-search review. We strongly urge continued funding for reemployment activities.

We recognize that the faith of our businesses and worker community in the integrity of our fund is critical to its solvency. We believe the actions we have taken to prosecute and deter fraud and prevent and collect and prevent overpayments are essential.



July 29, 2011

Honorable Max S. Baucus
 Chairman, United States Senate Committee on Finance
 Washington, DC 20510-6200

Dear Senator Baucus:

Thank you for the opportunity to provide responses to your and Sen. Wyden's questions following the Finance Committee meeting on June 22, 2011, at which I was privileged to testify.

Questions from Senator Baucus:

1. Does your state target its re-employment services to job sectors that are growing or in need of workers? If so, how?

Yes, Washington state's employment and training efforts are tailored to meet the local needs of growing job sectors in need of workers. We use labor market information and on-the-ground assessments by local workforce investment boards and businesses to identify in-demand occupations and target those occupations for our state and federal retraining supports. We then actively seek to identify unemployed workers who would most benefit from these programs.

Training efforts targeted to growing job sectors

Linked to Unemployment Benefits

Washington state provides an extension of unemployment insurance weekly benefits and an exemption from the job search requirement for claimants: 1) whose occupation is in decline; and 2) who pursue approved training for an occupation that is in demand within their community. Between 2001 and 2010, an annual average of just under 2,000 people participated in the Training Benefits program, receiving an additional average of 22 weeks of benefits.

Local workforce investment boards established under the Workforce Investment Act are responsible for managing the lists of declining and in-demand occupations with the assistance of the Employment Security Department's labor market information staff.

Through Community and Technical Colleges

A statewide and state-funded worker retraining program operated by the community and technical college system provides financial assistance to unemployed and dislocated workers to pursue approved training programs and receive related support services. Local advisory committees, with a majority of business and labor members, work with the colleges to ensure that training is targeted to occupations that meet employers' needs.

We also rely on Workforce Investment Act and other federal funding sources to provide tuition assistance.

Industry Skills Panels

Washington state has established local and regional industry skill panels. These panels have helped forge closer ties among the business community, education providers, and public and nonprofit entities around the state, bringing them together to pinpoint worker skill gaps and create education and training programs to fill them.

2. Commissioner Trause, will you please discuss your state's emphasis on reemployment initiatives and how they positively impact Americans who are looking for work and the relationship to fraud?

Through the one-stop career development system, referred to as WorkSource, Washington state helps jobseekers achieve successful careers and strives to prevent unemployment-insurance fraud. All claimants are automatically registered with the WorkSource system, through which we provide claimants with the tools and assistance for an effective and appropriate job search. We also identify claimants whose job search activity has not been successful, and work to engage them with available WorkSource services. If claimants do not pursue an appropriate job search, the state takes enforcement action. According to a first-in-the-nation study, unemployment-insurance claimants who use Washington WorkSource employment services are getting back to work faster, thereby earning more money than those who do not. We believe this combination of services and enforcement combine to get claimants back to work and prevent fraud. In 2010, fraud accounted for less than one half of 1 percent of regular benefit payments in the state.

Re-employment Orientations and Workshops for Unemployment-Insurance Claimants

During the initial weeks of a claim, claimants with a job search requirement are invited to participate in re-employment orientation provided through WorkSource, prioritizing claimants who are identified as most likely to exhaust their unemployment benefits. The orientation includes the following topics: employability and skill assessments; job referrals; labor market information; an overview of all employment services available through WorkSource; and referrals for more intensive programs or training opportunities, when appropriate. Claimants are also required to have a one-on-one meeting with a career counselor. For those who are not using WorkSource services, the Employment Security Department continually markets those available services.

Long-term claimants receiving the federally-funded Emergency Unemployment Compensation (EUC) benefits are invited to attend a targeted workshop designed to motivate these claimants and explain available employment services. The session also focuses on overcoming barriers many long-term unemployed claimants face, such as depression, loss of confidence or the need to access other community resources to assist with possible financial needs.

Job Search Review

In accordance with state law enacted in 1998, unemployment-insurance claimants are randomly selected to report to WorkSource for a review of their employer contacts recorded on their job search logs. In addition to the log review, their identification is verified, they are assisted with developing a plan to return to work and may be provided with referrals to job openings. More than 66,000 claimants were called in for a job search review during state fiscal year 2010.

A pilot project in one of Washington's workforce development areas is looking for ways to target job search reviews to those most likely to commit fraud, and pair that review with a greater level of assistance toward obtaining a job. Claimants who are identified as having a high probability for committing fraud are called into WorkSource for a job search review. When those claimants visit WorkSource, staff engage with them in an attempt to motivate the claimants to comply with unemployment-insurance requirements. The names of those identified as not meeting the requirements are forwarded to the Employment Security Department's investigation unit.

Enhanced Reporting and Data Tracking

In 2005, Washington received a U.S. Department of Labor grant to implement a Reemployment Eligibility Assessment (REA) effort to enhance the state's job search review program. Through the REA grant, Washington was able to:

- Enhance reports that track performance activities to specific claimants and staff who served them; and
- Develop a computer application to better track unemployment-insurance claimants and focus on claimants most likely to exhaust their benefits.

The state continues to work to ensure there is a connection between the one-stop data collection system and unemployment-insurance benefit system so that a claimant's failure to participate in a scheduled reemployment service can be addressed promptly. Washington state's IT infrastructure, however, is out-dated and greatly hinders our ability to target claimants for the appropriate level of services.

New One-Stop Service-Delivery Model

Washington state has taken an aggressive approach to re-employment by adopting a new service-delivery model to more actively engage WorkSource customers and provide a consistent level of staff assistance. The new model includes a redesigned front-end process that allows WorkSource to ensure each customer receives the level of service he or she needs. It offers: an assessment of each claimant's education and work history; career planning assistance and referrals, where appropriate, to training for in-demand occupations; and help in "packaging" the claimant for employers and appropriate job referrals.

Questions from Senator Wyden:

1. **Does your state have any problems with TALX or other third-party representatives? If so, how do you address those problems? Does the Administration's proposed Program Integrity Act go far enough to prevent these abuses? Should there be additional measures to prevent these abusive practices that contribute to UI overpayments? For example, should there be (or is there already) any requirement that third-party firms be separately regulated? Should they be required to register with the state, meet acceptable rules of conduct, and impose penalties for those that abuse the system? Should all charges that directly result from late-filed information be charged to the employers, especially given the limited resources of the states to go up against companies like TALX and prove that a given situation rose to the level of a "pattern" of abuse? In cases where an employer or third party representative fails to respond to your office in a timely matter, do you initiate payments to the claimant in the meantime or wait for employer verification?**

Washington state does not oppose allowing states to “charge” the employer for overpaid benefits if the state can show there’s a “pattern” of failing to provide the necessary employer information on time. Our understanding is that the Administration’s proposed Program Integrity Act includes this tool as a way for states to improve integrity efforts. We, however, have not experienced issues with their-party representatives.

Third-Party Representatives

Washington state law provides a tool for dealing specifically with third-party representatives in cases of fraud. An additional fine of \$5,000 per occurrence is charged if the person attempting to evade the appropriate tax rate is not the employer (i.e., third-party representative).

“Conditional” Unemployment Benefits Paid Out when Employers Non-Responsive

If an employer or its representative raises an issue of eligibility after a claimant has already starting receiving benefits, those benefits continue to be paid until the eligibility issue has been resolved. If the claimant is found to be ineligible for those conditional benefits, he or she must pay those back.

Washington state provides written notice to employers when former employees initially apply for unemployment benefits, and asks employers to verify the reason for job separation. Employers have 10 days to respond to that notice. If they do not respond within that time, eligibility determinations are made with available information. Those determinations become final after 30 days.

2. **With all the serious and important focus on recovering overpayments, what more could the federal government and the states be doing to ensure that workers are not innocently swept up in non-fraud or fraud overpayment determinations, and ensure there’s a balanced approach toward program integrity? For example, the vast majority of states require that non-fraud overpayment determinations be waived in appropriate cases? Should all states have similar provisions to help workers who are already financially destitute and have done nothing to contribute to the overpayment?**

Washington state believes that the workforce system could be doing more to ensure a balanced approach to program integrity. First, funding must be available for basic infrastructure and investments in reemployment services so that the national workforce system can better target resources to those who need assistance with finding a job. Funding must also be invested in identifying claimants and employers who are engaged in fraud, particularly those operating in the underground economy. We believe that Washington state has taken a very active approach to both the underground economy and claimant fraud.

Washington state’s Legislature has adopted a rigorous definition of fraud that requires intentionality on the part of the employer or claimant. If the Employment Security Department concludes that fraud has occurred, employers and claimants have ample notice and opportunity to challenge those findings through an independent administrative process before pursuing their case further in the courts. State law also allows the Employment Security Department to waive repayment of an overpayment that was not the result of fraud, misrepresentation, willful nondisclosure or fault attributable to the claimant, and where repayment would be against equity and good conscience.

Claimant Fraud

A finding of unemployment-insurance claimant fraud is serious and results in significant penalties. Washington state has a strict legal definition of fraud based on the following five elements, including a requirement that the act be intentional, all of which must be met:

- The claimant made a representation or statement.
- The representation or statement was material to the claim.
- The representation or statement was false.
- The claimant knew the representation or statement was false or failed to determine whether it was true or false.
- The claimant intended that the Employment Security Department act on the representation or statement.

Claimants have the opportunity to appeal a finding of fraud to an independent agency staffed by administrative law judges who are empowered to rule after hearing evidence from both sides. Claimants are afforded a second level of review by the Commissioner's Review Office, also an independent body of administrative judges. Claimants may then appeal to superior court after exhausting administrative remedies.

Waiving Claimant Overpayments

Washington state requires that claimants repay unemployment benefits to which they were not entitled. However, state law also allows the Employment Security Department to waive repayment in certain cases. Waivers may be considered if an overpayment was not the result of fraud, misrepresentation, willful nondisclosure or fault attributable to the claimant. Claimants are not considered at fault when they have provided the department with all relevant information and could not reasonably have known the payment was improper.

The standard for waiving overpayments was established by Washington State Supreme Court: "if collection would be against equity and good conscience." This ensures that the Employment Security Department considers an individual's circumstances in determining whether repayment meets a basic concept of fairness. This is basically the concept of fairness given an individual's circumstances. In particular, the department is expected to determine whether denying a waiver would deprive the claimant of income needed for basic necessities including food, shelter, medicine and utilities. In addition to income, the department considers a wide variety of other factors including health, education, current employment status, and whether department or employer error contributed to the overpayment.

Washington state law also empowers the Employment Security Department to negotiate terms of repayment agreements to make repayment more affordable for claimants, as well as settlements for partial repayments.

3. **The Obama Administration and the states have taken steps to address employer fraud in the UI program, going after employers who fail to pay their fair share of taxes by not reporting workers on their payroll, by underreporting their payroll, or misclassifying workers as independent contractors. Various government-funded studies have estimated that as many as 15-30% of employers misclassifying workers as independent contractors to avoid paying unemployment taxes, workers' compensation or deny workers their basic rights under employment and labor laws.**

Yet, when it comes to employers who commit UI fraud, the financial and criminal penalties are often very limited, more limited in many cases than the penalties that apply to workers who commit UI fraud. In Utah, workers are subject to a maximum prison term of 15 years when they commit UI fraud, compared to 5 years for employers. In most states, the fines and penalties on employers for committing fraud are far below the proposed 15% penalty imposed on workers by the Administration's Program Integrity Act (they are usually a flat fee, not a percent of the unpaid taxes, ranging from about \$50 to \$2,000 or so).

Why shouldn't the penalties for employers who commit fraud be comparable to the penalties for workers who commit fraud? What more could be done in the Program Integrity Act or other federal or state policies to ensure that employers that intentionally defraud the unemployment system are effectively penalized?

Washington state strongly endorses a balanced approach to fraud which penalizes employers and employees appropriately. The effectiveness of penalties should be judged by whether they deter fraudulent behavior. We believe that our state Legislature has provided a penalty structure which, combined with aggressive enforcement action, provides a strong deterrent to fraud. Claimants who commit unemployment-insurance fraud are charged interest on the benefits owed until the benefits are fully repaid. Repeat offenders may also be disqualified from unemployment benefits for up to two years and fined an amount up to 50 percent of the benefits they owe. In 2007, Washington state laws related to unemployment-insurance claimant fraud were changed. These laws remain in effect today. Since becoming effecting in 2008, 21,500 claimants have been found to have committed fraud. Of that total, 418 or less than 2 percent have been assessed with fraud a second time. Only 2 of the 21,500 claimants who have committed fraud under the current law have been found to have committed fraud a third time. That is one-hundredth of a percent.

These numbers are expected to increase as time goes by, but are accurate as of June 2011. We believe this penalty is adequate since fraud accounted for less than one half of 1 percent of regular benefit payments in the state in 2010, and, more importantly,

Employers who commit unemployment-insurance fraud must pay the taxes they owe, along with late payment penalties and interest. They must also pay audit costs, along with any related collection fees, and may be assigned a higher delinquent tax rate. In 2008, Washington state moved from scheduling audits based largely on random selection to focusing on employers who appeared likely to be misclassifying employees or not reporting wages. As a result of the enhanced audit program, we found 102 percent more misclassified workers and 60 percent more unreported taxes in 2010 than in 2009.

We also believe that a particular penalty, regardless of its severity, is effective only if businesses and claimants believe that there is a substantial risk of detection. We must identify, aggressively pursue and publicize fraudulent behavior to deter fraud successfully.

Employer Fraud

Washington state takes employer unemployment-insurance fraud very seriously. Penalties for intentionally manipulating information to receive a lower state unemployment tax rate include the following:

- Four years of taxation at 2 percentage points above the maximum tax rate;

- Payment of auditing and collection expenses; and
- Fine of \$5,000 per occurrence if the person attempting to evade the appropriate tax rate is not the employer (i.e., third-party representative).

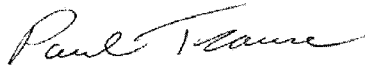
If an employer knowingly misrepresents taxable payroll, the employer is liable for up to 10 times the amount of the difference between what was paid and what was due. The employer must also pay auditing and collection expenses.

Claimant Fraud

Washington state also takes claimant fraud very seriously. In such cases, interest is charged on the benefits owed until the benefits are fully repaid. Repeat offenders may also be disqualified from unemployment benefits for up to two years and fined an amount up to 50 percent of the benefits they owe.

Thank you again for the opportunity to weigh in on these important issues. Please contact me at (360) 902-9304 or by email at paul.trause@esd.wa.gov for any additional information or further questions.

Sincerely,



Paul Trause
Commissioner

cc Senator Orrin G. Hatch

