

**H.R. 1827, THE GOVERNMENT WASTE  
CORRECTIONS ACT OF 1999**

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**HEARING**

BEFORE THE

SUBCOMMITTEE ON GOVERNMENT MANAGEMENT,  
INFORMATION, AND TECHNOLOGY

OF THE

COMMITTEE ON GOVERNMENT REFORM  
HOUSE OF REPRESENTATIVES

ONE HUNDRED SIXTH CONGRESS

FIRST SESSION

ON

**H.R. 1827**

TO IMPROVE THE ECONOMY AND EFFICIENCY OF GOVERNMENT OPER-  
ATIONS BY REQUIRING THE USE OF RECOVERY AUDITS BY FEDERAL  
AGENCIES

—————  
JUNE 29, 1999  
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## **H.R. 1827, THE GOVERNMENT WASTE CORRECTIONS ACT OF 1999**

**TUESDAY, JUNE 29, 1999**

HOUSE OF REPRESENTATIVES,  
SUBCOMMITTEE ON GOVERNMENT MANAGEMENT,  
INFORMATION, AND TECHNOLOGY,  
COMMITTEE ON GOVERNMENT REFORM,  
*Washington, DC.*

The subcommittee met, pursuant to notice, at 2:01 p.m., in room 2247, Rayburn House Office Building, Hon. Stephen Horn (chairman of the subcommittee) presiding.

Present: Representatives Horn, Walden, Ose, Burton, and Turner.

Staff present: J. Russell George, staff director; Randy Kaplan, counsel; Bonnie Heald, communications director; Matthew Ebert, policy advisor; Jane Cobb, professional staff member, Committee on Government Reform; Grant Newman, clerk; Justin Schleuter, Paul Wicker, Lauren Lefton, and John Phillips, interns; Michelle Ash and Faith Weiss, minority counsels; Mark Stephenson, minority professional staff member; and Earley Green, minority staff assistant.

Mr. HORN. The Subcommittee on Government Management, Information, and Technology will come to order.

Fraud, waste, and error in Federal programs and activities are costing taxpayers billions of dollars each year. Earlier this session, the Subcommittee on Government Management, Information, and Technology held its annual series of hearings on the Federal Government's financial management practices. On March 31, 1999, this subcommittee held a hearing examining the Governmentwide Consolidated Financial Statement. The audit of this governmentwide financial statement, performed by the General Accounting Office, illustrated the broad array of financial management problems faced by the Federal Government.

The report confirmed that tens of billions of taxpayer dollars are being lost each year to waste, abuse, and mismanagement in hundreds of programs within the executive branch of the Federal Government. Improper payments made to vendors and others supplying goods and services to Federal departments and agencies is one of the most serious areas of waste and error. According to the General Accounting Office, Federal departments and agencies were unable to determine the full extent of improper payments in major programs, estimated to involve billions of dollars each year.

At the Department of Defense, the General Accounting Office reported that among the most serious financial management weak-

nesses was the Department's inability to determine the full extent of improper payments. The Health Care Financing Administration's Medicare Program was cited by the General Accounting Office as a high-risk area for fraud, waste, and abuse. In 1998, there was an estimated \$12.6 billion in Medicare overpayments.

Today we will examine H.R. 1827, the Government Waste Corrections Act of 1999, introduced by my colleague and the chairman of this full committee, the Committee on Government Reform, Representative Dan Burton of Indiana. This legislation offers a potential solution to address the billions of dollars of erroneous overpayments made each year. This bill would require executive branch departments and agencies to use a process called, "recovery auditing," to review Federal payment transactions to identify and recover erroneous overpayments.

Recovery auditing is a process of reviewing payment transactions to identify and recover incorrect payments. Payments for goods and services can be processed incorrectly for a variety of reasons. Vendors can make pricing errors on their invoices. They may forget to award discounts. Or they can neglect to offer allowances and rebates. Recovery auditors review payment transactions to identify three types of errors.

For decades, private sector companies have successfully used recovery auditing to identify and collect erroneous overpayments. Recovery auditing is currently used to a limited extent in the Federal Government. H.R. 1827 would expand the use of recovery auditing to all executive branch departments and agencies for payment activities of at least \$10 million annually.

Recovery audits could be conducted in house or contracted out to a private recovery audit firm. The bill would require recovery auditors to report on the factors causing overpayments and steps that can be taken to reduce such overpayment. To encourage agencies to participate in recovery auditing, the bill would allow agencies to be reimbursed for costs they incur for their recovery audit efforts. Additional amounts collected could be used by the agency to carry out management improvement programs.

The subcommittee will hear from a variety of public and private sector witnesses who will discuss the provisions of H.R. 1827, including the application of recovery auditing to the Federal Government. I welcome our witnesses. We look forward to their testimony. And I am delighted now to yield for an opening statement to Mr. Turner of Texas, the ranking member on this committee. And we are delighted to have you here, Jim. It is all yours.

[The text of H.R. 1827 and the prepared statement of Hon. Stephen Horn follow:]

106TH CONGRESS  
1ST SESSION

**H. R. 1827**

To improve the economy and efficiency of Government operations by requiring the use of recovery audits by Federal agencies.

IN THE HOUSE OF REPRESENTATIVES

MAY 17, 1999

MR. BURTON of Indiana (for himself, Mr. ARMEY, and Mr. OSE) introduced the following bill; which was referred to the Committee on Government Reform

**A BILL**

To improve the economy and efficiency of Government operations by requiring the use of recovery audits by Federal agencies.

*Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,*

**SECTION 1. SHORT TITLE.**

This Act may be cited as the "Government Waste Corrections Act of 1999".

**SEC. 2. FINDINGS AND PURPOSES.**

(a) **FINDINGS.**—The Congress finds the following:

(1) In private industry, overpayments to providers of goods and services occur for a variety of reasons, including duplicate payments, pricing errors, and missed cash discounts, rebates, or other allowances. The identification and recovery of such overpayments, commonly referred to as "recovery auditing", is an established private sector business practice with demonstrated large financial returns. On average, recovery audits in the private sector identify payment error rates of 0.1 percent of purchases audited and result in the recovery of \$1,000,000 for each \$1,000,000,000 of purchases.

(2) Overpayments are a serious problem for Federal agencies, given the magnitude and complexity of Federal operations and documented and widespread financial management weaknesses. Federal agency overpayments waste tax dollars and detract from the efficiency and effectiveness of Federal operations by diverting resources from their intended uses.

(3) Recovery auditing already has been employed successfully in limited areas of Federal activity. It has great potential for expansion to many other Federal agencies and activities, thereby resulting in the recovery of substantial amounts of overpayments annually. Limited recovery audits conducted to date have identified errors averaging 0.4 percent of Federal payments audited, or \$4,000,000 for every \$1,000,000,000 of payments. If fully implemented within the Federal Government, recovery auditing has the potential to recover billions of dollars in Federal overpayments annually.

(b) **PURPOSES.**—The purposes of this Act are the following:

(1) To require the use of recovery audits by Federal agencies.

(2) To provide incentives and resources to improve Federal management practices with the goal of significantly reducing Federal overpayment rates and other waste and error in Federal programs.

**SEC. 3. ESTABLISHMENT OF RECOVERY AUDITS REQUIREMENT.**

(a) **ESTABLISHMENT OF REQUIREMENT.**—Chapter 35 of title 31, United States Code, is amended by adding at the end the following:

"SUBCHAPTER VI—RECOVERY AUDITS

**"§ 3561. Definitions**

"In this subchapter, the following definitions apply:

"(1) **DIRECTOR.**—The term 'Director' means the Director of the Office of Management and Budget.

“(2) PAYMENT ACTIVITY.—The term ‘payment activity’ means an executive agency activity that entails making payments to—

“(A) vendors or other entities that provide property or services for the direct benefit or use of an executive agency; or

“(B) entities that provide services or make payments on behalf of the Federal Government pursuant to contractual arrangements with an executive agency.

“(3) RECOVERY AUDIT.—The term ‘recovery audit’ means an auditing process to identify overpayments made by executive agencies to vendors and other commercial entities in connection with a payment activity, including overpayments that result from duplicate payments, pricing errors, failure to provide applicable discounts, rebates, or other applicable allowances, or charges or payments that are not authorized by law, regulation, or other applicable requirements.

**“§ 3562. Recovery audit requirement**

“(a) IN GENERAL.—Except as provided in subsection (d), the head of each executive agency—

“(1) shall conduct recovery audits with respect to each payment activity of the executive agency that expends \$10,000,000 or more annually; and

“(2) may conduct recovery audits for any other payment activity of the executive agency.

“(b) PROCEDURES.—In conducting recovery audits under this section, the head of an executive agency—

“(1) shall give priority to the most recent payments;

“(2) shall implement this section in a manner designed to ensure the greatest financial benefit to the Government; and

“(3) may conduct recovery audits directly, by procuring performance of recovery audits by contract (subject to the availability of appropriations), or by any combination thereof.

“(c) RECOVERY AUDIT CONTRACTS.—

“(1) EXECUTIVE AGENCY AUTHORITIES.—With respect to recovery audits procured by an executive agency by contract—

“(A) notwithstanding section 3302(b) of this title, the executive agency head may pay the contractor an amount not to exceed 25 percent of the total amount recovered by the executive agency, through setoff and otherwise, solely on the basis of information obtained as a result of audits performed by the contractor under the contract;

“(B) the executive agency head may authorize the contractor (subject to subparagraph (C)) to notify entities of potential overpayments, to respond to questions concerning potential overpayments, and to take other administrative actions with respect to overpayment claims; and

“(C) subject to section 3711 of this title, the executive agency head shall have final authority to resolve disputes, to compromise or terminate overpayment claims, to collect by setoff, and to initiate litigation or referrals for litigation.

“(2) CONTRACT TERMS AND CONDITIONS.—The head of an executive agency shall include in each contract for procurement of performance of a recovery audit a requirement that the contractor shall—

“(A) provide to the executive agency periodic reports on conditions giving rise to overpayments identified by the contractor and any recommendations on how to mitigate such conditions; and

“(B) notify the executive agency of any overpayments identified by the contractor pertaining to the executive agency or to another executive agency that are beyond the scope of the contract.

“(3) EXECUTIVE AGENCY ACTION FOLLOWING NOTIFICATION.—The head of an executive agency shall take prompt and appropriate action in response to a notification by a contractor under subparagraph (A) or (B) of paragraph (2), including forwarding to other executive agencies any information that applies to them.

“(d) EXEMPTIONS.—The Director may exempt any executive agency payment activity from the requirement of subsection (a)(1) if the Director determines that conducting recovery audits for that payment activity would not be practical or cost-effective.

**“§ 3563. Recovery audit model programs**

“(a) IN GENERAL.—The Director, after consulting with executive agency heads, shall designate not less than five recovery audit model programs. The designated model programs shall—

“(1) reflect a representative range of executive agencies, program activities, and payment practices; and

“(2) continue for a period of at least one year.

“(b) PURPOSE.—The purpose of the model programs designated under this section is to stimulate and enhance recovery audits in the Federal Government by developing best practices and otherwise identifying ways to make recovery audits more effective. In designating the model programs, the Director shall ensure that the designated programs complement, and in no way preempt or delay, other Federal recovery audit activities.

**“§ 3564. Disposition of amounts collected**

“(a) IN GENERAL.—Notwithstanding section 3302(b) of this title, amounts an executive agency collects, by setoff and otherwise, each fiscal year through recovery audits conducted under this subchapter shall be treated in accordance with this section.

“(b) USE FOR RECOVERY AUDIT COSTS.—Not more than one quarter of the amounts collected by an executive agency through recovery audits shall be available to meet obligations to recovery audit contractors and to reimburse applicable appropriations for other recovery audit costs incurred by the executive agency.

“(c) USE FOR MANAGEMENT IMPROVEMENT PROGRAM.—Not more than one half of the amounts collected by an executive agency through recovery audits—

“(1) shall be available to the head of the executive agency to carry out the management improvement program of the agency under section 3565 of this title;

“(2) may be credited for that purpose by the agency head to any agency appropriations and funds that are available for obligation at the time of collection; and

“(3) shall remain available for the same period as the appropriation or fund to which credited.

“(d) USE FOR ORIGINAL PURPOSE.—Not more than one quarter of the amounts collected—

“(1) shall be credited to the appropriation or fund, if any, available for obligation at the time of collection for the same general purposes as the appropriation or fund from which the overpayment was made; and

“(2) shall remain available for the same period and purposes as the appropriation or fund to which credited.

“(e) REMAINDER.—Amounts collected that are not applied in accordance with subsection (b), (c), or (d) shall be deposited in the Treasury as miscellaneous receipts.

“(f) LIMITATION OF AMOUNTS.—In accordance with section 1512(d) of this title, the Director may reserve amounts made available to an executive agency under subsections (b) through (d) to the extent the Director determines that the full amounts otherwise available cannot be used productively for the purposes for which they are made available.

**“§ 3565. Management improvement program**

“(a) IN GENERAL.—

“(1) REQUIREMENT.—The head of each executive agency shall conduct a management improvement program, consistent with rules prescribed by the Director.

“(2) PROGRAM FEATURES.—In conducting the program, the head of the executive agency—

“(A) shall, as the first priority of the program, address problems that contribute directly to agency overpayments; and

“(B) may seek to reduce errors and waste in other executive agency programs and operations by improving the executive agency’s staff capacity, information technology, and financial management.

“(3) INTEGRATION WITH OTHER ACTIVITIES.—The head of an executive agency—

“(A) subject to subparagraph (B), may integrate the program under this section, in whole or in part, with other executive agency management improvement programs and activities; and

“(B) must retain the ability to account specifically for the use of amounts made available under section 3465(b) of this title.

“(b) AWARDS.—

“(1) IN GENERAL.—The head of an executive agency may, under the program under this section and subject to the availability of appropriations, pay cash awards to career employees of the executive agency who have made extraor-



dinary contributions to improving the executive agency's operations in a way that demonstrably and substantially reduces waste and error by the executive agency.

"(2) TERMS AND CONDITIONS.—An award under this subsection shall be subject to the following terms and conditions:

"(A) An award may be granted to an individual employee or to a group of employees, in any amount not exceeding \$150,000 for any individual.

"(B) The award must be based on a written determination by the executive agency head that the awardee (or the group of awardees, collectively) was directly and primarily responsible for actions that result in tangible cost savings to the executive agency of at least double the amount of the award.

"(C) The Director must concur in any award that exceeds \$50,000 to any individual.

"(D) The awards shall be in addition to any pay and allowances to which an employee is otherwise entitled, and shall not affect an employee's eligibility for other bonuses and awards.

"(E) The award shall be subject to such additional terms and conditions as may be prescribed by the Director.

"(3) CAREER EMPLOYEE DEFINED.—In this subsection the term 'career employee' means any employee of an executive agency, other than—

"(A) a noncareer appointee, limited term appointee, or limited emergency appointee (as such terms are defined in section 3132(a) of title 5) in the Senior Executive Service; and

"(B) an employee in a position that has been excepted from the competitive service by reason of its confidential, policy-determining, policy-making, or policy-advocating character.

#### **"§ 3566. Responsibilities of the Office of Management and Budget**

"(a) IN GENERAL.—The Director shall be responsible for coordinating and overseeing the implementation of this subchapter.

"(b) GUIDANCE.—In addition to the Director's specific responsibilities under this subchapter, the Director shall issue rules and provide support to agencies in implementing the subchapter. The Director shall issue initial rules not later than 90 days after the date of enactment of this subchapter.

"(c) REPORTS.—

"(1) IN GENERAL.—Not later than one year after the date of the enactment of this subchapter, and annually for each of the two years thereafter, the Director shall submit a report on implementation of the subchapter to the President, the Committee on Government Reform of the House of Representatives, the Committee on Governmental Affairs of the Senate, and the Committee on Appropriations of the House of Representatives and of the Senate.

"(2) CONTENTS.—Each report shall include—

"(A) a general description and evaluation of the steps taken by executive agencies to conduct recovery audits, including an inventory of the programs and activities of each executive agency that are subject to recovery audits;

"(B) a description of any exemptions from recovery audits made under section 3562(d) of this title;

"(C) a description and evaluation of the recovery audit model programs conducted under section 3563 of this title, that shall include—

"(i) an assessment of the benefits of the programs;

"(ii) an identification of best practices from the programs that could be applied to other recovery audit activities; and

"(iii) an identification of any significant problems or barriers to more effective recovery audits that were experienced in the model programs;

"(D) a description of executive agency management improvement programs under section 3565 of this title, including a description of any awards under section 3565(b) of this title; and

"(E) any recommendations for changes in executive agency practices or law or other improvements that the Director believes would enhance the effectiveness of executive agency recovery auditing.

#### **"§ 3567. General Accounting Office reports**

"Not later than 60 days after issuance of each report under section 3566(c) of this title, the Comptroller General of the United States shall submit a report on the implementation of this subchapter to the Committee on Government Reform of the

House of Representatives, the Committee on Governmental Affairs of the Senate, the Committee on Appropriations of the House of Representatives and of the Senate, and the Director.”.

(b) APPLICATION TO ALL EXECUTIVE AGENCIES.—Section 3501 of title 31, United States Code, is amended by inserting “and subchapter VI of this chapter” after “section 3513”.

(c) DEADLINE FOR INITIATION OF RECOVERY AUDITS.—The head of each executive agency shall begin the first recovery auditing under section 3562 of title 31, United States Code, as amended by this section, by not later than 6 months after the date of the enactment of this Act.

(d) CLERICAL AMENDMENT.—The analysis at the beginning of chapter 35 of title 31, United States Code, is amended by adding at the end the following:

“SUBCHAPTER VI—RECOVERY AUDITS

“3561. Definitions.

“3562. Recovery audit requirement.

“3563. Recovery audit model programs.

“3564. Disposition of amounts collected.

“3565. Management improvement program.

“3566. Responsibilities of the Office of Management and Budget.

“3567. General Accounting Office reports.



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INDEPENDENT

**Hearing on H.R. 1827, the "Government Waste Corrections Act of 1999"**  
**Opening Statement**  
**Rep. Stephen Horn, R-Calif.**  
**Chairman, House Subcommittee on Government Management,**  
**Information, and Technology**  
**June 29, 1999**

A quorum being present, the Subcommittee on Government Management, Information, and Technology will come to order.

Fraud, waste, and error in Federal programs and activities are costing taxpayers billions of dollars each year. Earlier this session, the Subcommittee on Government Management, Information, and Technology held its annual series of hearings on the Federal Government's financial management practices. On March 31, 1999, this subcommittee held a hearing examining the Governmentwide consolidated financial statement. The audit of this governmentwide financial statement, performed by the General Accounting Office, illustrated the broad array of financial management problems faced by the Federal Government. The report confirmed that tens of billions of taxpayer dollars are being lost each year to waste, abuse and mismanagement in hundreds of programs within the Federal Government.

Improper payments made to vendors and others supplying goods and services to Federal departments and agencies is one of the most serious areas of waste and error. According to the General Accounting Office, Federal departments and agencies were unable to determine the full extent of improper payments in major programs estimated to involve billions of dollars each year. At the Department of Defense, the General Accounting Office reported that among the most serious financial management weaknesses was the department's inability to determine the full extent of improper payments. The Health Care Financing Administration's Medicare program was cited by the General Accounting Office as a high-risk area for fraud, waste, and abuse. In 1998 there was an estimated \$12.6 billion dollars in Medicare overpayments.

Today we will examine H.R. 1827, the "Government Waste Corrections Act of 1999," introduced by my colleague and the Chairman of the Committee on Government Reform, Representative Dan Burton. This legislation offers a potential solution to address the billions of dollars of erroneous overpayments made each year. This bill would require Executive Branch departments and agencies to use a process called "recovery auditing" to review Federal payment transactions to identify and recover erroneous overpayments.

Mr. TURNER. Thank you, Mr. Chairman. This hearing, of course, is focused on a piece of legislation that the chairman of this committee, Mr. Burton, introduced last year which seeks to make recovery auditing mandatory for Federal agencies. I appreciate Chairman Horn's interest in this issue and his willingness to focus on it by holding this hearing.

As we know, the Federal Government erroneously pays vendors and contractors billions of dollars each year and, through a series of financial management hearings held by this subcommittee, we have learned, for example, that the Medicare system made approximately \$12 billion in erroneous payments in fiscal year 1998 revealing an error rate of 7 percent. Obviously, these kinds of errors and mistakes do not need to exist in our Federal agencies and I commend Chairman Burton as well as Chairman Horn for focusing on this problem, continuing to search for solutions such as recovery auditing.

Mr. Chairman, thank you again for the opportunity to be a part of this very important hearing.

[The prepared statement of Hon. Jim Turner follows:]

**OPENING STATEMENT OF THE HONORABLE JIM TURNER**  
**GMIT: H.R. 1827**  
**June 29, 1999 (version #3)**

This hearing is focused on H.R. 1827, legislation which was introduced by Chairman Burton this year and seeks to make recovery auditing mandatory for federal agencies. I appreciate Chairman Horn's focus on this issue and am glad to have the opportunity to discuss the use of recovery auditing in the public and private sectors.

The federal government erroneously pays vendors and contractors billions of dollars each year. Through a series of financial management hearings held by this subcommittee, for example, we have learned that the Medicare system made approximately \$12 billion in erroneous payments in fiscal year 1998—revealing an error rate of 7%.

Even more disturbing is the knowledge that defense contractors **voluntarily** returned \$746 million in fiscal 1998, which averages out to about \$2 million per day in overpayments. In the five years between fiscal 1994 and 1998, defense contractors returned about \$4.6 billion. Additionally, the General Accounting Office has discovered that, because there are no requirements which address the notification or return of improperly paid money, many contractors are retaining overpayments until the government issues a demand letter for the recovery of the overpayment. The General Accounting Office recently testified that both the magnitude of overpayments to defense contractors is unknown as is the amount of overpayments being retained by contractors.

Thus it is imperative that the federal government direct its attention toward the improvement of financial management systems and reducing erroneous payments. I would like to commend Chairman Burton for focusing on this important problem and for searching for solutions, such as recovery auditing. I would also like to thank Chairman Horn for providing the opportunity for representatives of the federal government and the private sector to describe recovery auditing and explain its usefulness to the government.

Congress must assure that the executive branch has all the tools it needs to reduce erroneous payments, and the executive branch must use these tools effectively and aggressively. Recovery auditing is the type of tool that should be used where it can render successful results.

This hearing should help answer some specific questions that I have about H.R. 1827, the first of which is how this bill would interact with the current federal debt collection activities and the Federal Acquisition Regulations (FAR). Additionally, I am interested in learning how disputes arising out of recovery auditing will be resolved, and whether the regular federal contracting dispute resolution process would apply. I also question whether the authorization of employee awards, which can be as large as \$150,000 per person, creates appropriate incentives or if these awards give rise to abuse. Finally, I wonder if recovery auditing should be mandated for all agencies when it is unclear whether this process will in fact be useful or appropriate for all agencies. In particular, will recovery auditing work for all agency payments and for all types of payment activities?

With these thoughts in mind, I welcome the witnesses today and look forward to their testimony.

Mr. HORN. I thank the gentleman. And we are waiting for Chairman Burton. He should be here in a minute or so. So we will be in recess for a minute or so. When Mr. Burton arrives, we will have the statement read into the record.

In the meantime, let me note, this is for some of you that have been here before, before this subcommittee or any subcommittee of the Government Reform Committee, we swear in all witnesses. And when we have you at the table, such as panel two where there are four witnesses, when we call on you in that sequence, the document you have given us in writing, we have read. And that automatically goes into the record without any additional motions. And we would like you to summarize those statements so there is more dialog with the committee members on both sides of the aisle to ask questions and get to the core of the matter.

And we are now delighted to introduce the gentleman from Indiana, the chairman of the Committee on Government Reform, for an opening statement.

Mr. BURTON. I want to thank you, Mr. Chairman. And you will see, first of all, I am out of breath because I am out of shape. And, second, I am wearing sunglasses because I forgot to change these. So I don't want you to think I am a movie star or think I am.

Thank you, Chairman Horn, for holding this hearing on H.R. 1827, the Government Waste Corrections Act.

One of my highest priorities as chairman of the Committee on Government Reform is to attack the widespread fraud, waste, and error in Federal programs and activities that cost taxpayers billions of dollars every year. One area where we bleed millions of dollars every day is in overpayments for contractors that often go undetected and almost never get repaid. Many agencies could benefit from the use of recovery auditing. Several of these could see substantial gains.

The Department of Defense, the Environmental Protection Agency, NASA, and the Department of Energy have all been on GAO's high-risk list for almost 10 years for contract management problems. These agencies represent about \$140 billion worth of contracts yearly. DOD alone represents about \$100 billion of this spending. How much of this is wasted in overpayments has not been calculated, but with the problems associated with these contracting operations, I would bet that the figures are pretty high.

Another high-dollar, high-risk area is Medicare. Of about \$200 billion it pays out annually, overpayments in Medicare's fee for service claims last year were estimated at \$12.6 billion. That is \$12.6 billion in just 1 year. Over the past 3 years, this figure is estimated at over \$56 billion. This needless waste of money year after year significantly distorts the true costs of Medicare. Mr. Chairman, if nothing else, recovery auditing should be mandated to recoup Medicare overpayments.

I just hope that when the bill passes and these overpayments start coming back, the checks won't be returned as is the current practice. And I would like to say that, Mr. Chairman, that I read an article that was in the Regulatory News and it indicated that some of these checks are being returned because they don't know what to do with them. And we certainly want to make sure that



that is corrected, because if people are sending overpayments back to the Treasury and to the government——

Mr. HORN. Without objection, that article will be put in the record at this point.

[The information referred to follows:]

Overpayments**HHS IG, HCFA Developing Guidance  
For Providers to Return Overpayments**

**B**ALTIMORE—The Department of Health and Human Services Office of Inspector General and the Health Care Financing Administration are developing guidance for health care providers to return funds they inappropriately receive from Medicare, an IG official said March 24.

"We've been working over the last year with HCFA on trying to get some standardized process for the return of identified overpayments voluntarily identified by providers," Michael L. Shaw, an associate counsel with HHS IG's Office of Counsel, told the American Health Lawyers Association's annual conference on Medicare and Medicaid payment issues.

"Hopefully something soon will come out and that will give providers guidance on what to return and how to return it," Shaw said.

Empathizing with providers who try to return overpayments to their Medicare carrier only to have the check returned, he said, "I know that's a frustrating thing. We constantly hear about it. All I can tell you is we're trying to work on that."

But the government has long failed to make good on promises of issuing such guidance. More than a year ago, former HCFA Director of Program Integrity Linda Ruiz told another health care conference in Washington, D.C., Feb. 19, 1998, that Medicare overpayment guidance could be expected out within the next few months (2 HFRA 118, 2/25/98).

Mr. BURTON. Thank you, Mr. Chairman. And this is even when providers voluntarily return the money, their checks are still returned. Mr. Chairman, I hope your subcommittee will try to get some answers from the representatives from HCFA today on that very problem.

Let me briefly describe what my bill does. The bill requires agencies to conduct recovery auditing to identify and collect overpayments for programs that spend \$10 million or more annually. Up to 25 percent of the money collected back can be used to pay the recovery audit firm, so there is no payment to the contractor unless the overpayments are returned. The bill also allows agencies to put 25 percent of collections back into the programs and activities from which the overpayments originated. Mr. Chairman, this is to provide agencies that need an incentive to commit to this activity.

Requiring agencies to identify and recover overpayments is only one of the bill's key objectives. The other is to remedy the root causes that gave rise to the overpayments in the first place. To this end, the bill also allows for some of the money recovered to be available to the agency to make improvements to their financial and other internal systems in order to prevent overpayments and reduce other problems of waste and error in the future. Recovered moneys not used for these purposes will get returned to the Treasury.

Mr. Chairman, this bill holds great promise. In places where recovery auditing has been tested in government, it has proven effective. For instance, the Army-Air Force exchange program [AAFES] has 16 years of experience with recovery auditing, having begun the practice in 1983. With purchases of approximately \$6.5 billion annually, over \$100 million has been recovered over the past 5 years.

In another example, the Defense Department has been conducting a recovery auditing demonstration program at its supply center in Philadelphia. Looking at purchase transactions from fiscal years 1993 to 1995, over \$27 million in overpayments have been identified. Given the billions of dollars we spend to procure goods and services annually and the magnitude of the overpayment problem in our current programs, this bill has enormous potential to achieve substantial cost savings and benefits for the government and the American taxpayer.

Mr. Chairman, I stand ready to work with you, our Democratic colleagues, and this administration to make whatever improvements that are necessary to get the best bill possible. I want to thank you again for moving forward with the subcommittee consideration of this very important bill. And I apologize, once again, for my tardiness.

[The prepared statement of Hon. Dan Burton follows:]

**Statement of  
The Honorable Dan Burton  
Hearing on H.R. 1827, the Government Waste Corrections Act of 1999  
June 29, 1999**

Thank you, Chairman Horn, for holding this hearing on H.R. 1827, the Government Waste Corrections Act.

One of my highest priorities as Chairman of the Committee on Government Reform is to attack the widespread fraud, waste, and error in federal programs and activities that cost taxpayers billions of dollars every year.

One area where we bleed millions of dollars every day is in overpayments to contractors that often go undetected, and almost never get repaid. Many agencies could benefit from the use of recovery auditing. Several of these could see substantial gains.

The Department of Defense, the Environmental Protection Agency, NASA, and the Department of Energy have all been on GAO's High Risk list for almost 10 years for contract management problems. These agencies represent about \$140 billion worth of contracts yearly. DOD alone represents about \$100 billion of this spending. How much of this is wasted in overpayments has not been calculated, but with the problems associated with these contracting operations, I would bet the figures are high.

Another high-dollar "High Risk" area is Medicare. Of about \$200 billion it pays out annually, overpayments in Medicare's fee-for-service claims last year were estimated at \$12.6 billion dollars.

\$12.6 billion in one year!! Over the past three years, this figure is estimated at over \$56 billion. This needless waste of money year after year significantly distorts the true costs of Medicare. Mr. Chairman, if nothing else, recovery auditing should be mandated to recoup Medicare overpayments. I just hope that when the bill passes and these overpayments start coming back, the checks won't be returned, as is the current practice.

According to an article in BNA's Medicare Report on April 2, 1999, even when providers try to VOLUNTARILY return money they inappropriately received, their checks are returned. Mr. Chairman, I hope your subcommittee will try and get some answers from the representative from HCFA today on this problem.

Let me briefly describe what my bill does:

The bill requires agencies to conduct recovery auditing to identify and collect overpayments for programs that spend \$10 million or more annually.

Up to 25 percent of the money collected back can be used to pay the recovery

audit firm, so there's no payment to the contractor unless overpayments are returned.

The bill also allows agencies to put 25 percent of collections back into the programs and activities from which the overpayments originated. Mr. Chairman, this is to provide agencies the needed incentive to commit to this activity.

Requiring agencies to identify and recover overpayments is only one of the bill's key objectives. The other is to remedy the root causes that gave rise to the overpayments in the first place.

To this end the bill also allows for some of the money recovered to be available to the agency to make improvements to their financial and other internal systems in order to prevent overpayments and reduce other problems of waste and error.

Recovered monies not used for these purposes get returned to the Treasury.

Mr. Chairman, this bill holds great promise. In places where recovery auditing has been tested in government, it has proven effective. The Army Air Force Exchange System (AAFES) has 16 year of experience with recovery auditing, having begun the practice in 1983. AAFES makes purchases of approximately \$6.5 billion annually. Over the last 5 years, over \$100 million has been recovered.

In another example, the Defense Department has been conducting a recovery auditing demonstration program at several of its locations. Roughly \$7 billion in purchase transactions are being reviewed in this audit. This program is nearing completion and has identified over \$27 million in overpayments.

Given the billions of dollars we spend to procure goods and services annually and the magnitude of the overpayment problem in our current programs, this bill has enormous potential to achieve substantial cost benefits for the government and the American taxpayers. It also ensures a long-term investment in the fundamental management reforms so badly needed to achieve lasting improvements in the way the federal government does business.

Mr. Chairman, I stand ready to work with you and this administration to make whatever improvements need to be made to get the best bill possible. Thank you again for moving forward with subcommittee consideration of this important bill.

Mr. HORN. We thank you for putting in this bill. We think it has a lot of merit.

Now if the Comptroller General will stand and raise his right hand?

[Witness sworn.]

Mr. HORN. The clerk will note that the witness affirmed the oath.

And we are delighted to have you with us. It is an honor. And we hope you have enjoyed your first few months on the job, which is one of the most important in the United States. So welcome.

**STATEMENT OF DAVID D. WALKER, COMPTROLLER GENERAL,  
GENERAL ACCOUNTING OFFICE**

Mr. WALKER. Thank you. Chairman Horn, Chairman Burton, Ranking Member Turner, I appreciate the opportunity to discuss H.R. 1827, the Government Waste Corrections Act of 1999 and its relationship to the longstanding issues of government accountability for use of public moneys, overpayments, and the role of recovery auditing in identifying and recovering overpayments.

One of the most important issues facing the government today is the need for greater accountability in managing the finances of our national government. It is a significant problem at many agencies and one that has been the subject of frequent reports by us and others. One key aspect of the problem is the difficulty the government has in assuring proper payment of all of its bills while avoiding overpayments. My testimony today will discuss the dimensions of the overpayment problem, our past work on the DOD recovery auditing demonstration program, and the Government Waste Corrections Act of 1999.

My comments on the bill reflect my belief that there are three principles that should guide any recovery auditing program. First, there should be meaningful incentives for agencies to want to participate in the program and to make it work. Second, there should be adequate safeguards to ensure that the program is implemented in a manner intended by Congress and that it preserves the integrity of the congressional appropriations process. And, third, there should be transparency in the conduct of the program. That is, there should be evaluation reporting on program implementation, to include the amounts recovered under the program and how they are used. In the context of these three principles, I will suggest opportunities to strengthen the bill.

Significant financial systems' weaknesses, problems with fundamental recordkeeping and financial reporting, incomplete documentation, and weak internal controls continue to prevent the government from effectively managing its operations. Significant among these problems is the inability of Federal agencies to determine the full extent of improper payments that occur in major programs estimated to involve billions of dollars annually.

Within the estimated billions of dollars of improper payments, the amount of exact overpayments that are involved is unknown. Given the poor state of the financial accounting record at many agencies, neither the Federal agencies nor we have a very good estimate of the extent of overpayments that occur each year, yet we expect that they are significant. We know, for example, that be-

tween the years 1994 and 1998, contractors returned about \$4.6 billion in overpayments to the Department of Defense alone.

Across government, improper payments, which includes overpayments, occur in a variety of programs and activities, including those related to contract management, Federal financial assistance, and tax refunds. Reported estimates of improper payments total billions of dollars annually. Such payments can result from incomplete or inaccurate data used to make payment decisions, insufficient monitoring or oversight, and other deficiencies in agency information systems and controls.

The risk of improper payments is increased in programs involving one of three criteria: first, complex criteria for computing payments; second, a significant volume of transactions; and, third, an emphasis on expediting payments. The reasons for improper payments range from inadvertent errors to fraud and abuse.

Recovery auditing offers the potential to identify and recover some of these overpayments. Recovery auditing started about 30 years ago and it is used in several industries including the automotive, retail, and food service industries. The DOD, the Army and Air Force Exchange Service, and the Navy exchange service, use recovery auditing. An external audit recovery group may be the only group used by an organization or it may be used in combination with internal resources that examine invoices for overpayments prior to an external group's review.

Recognizing its potential to the government, in fiscal year 1996, the National Defense Authorization Act required the Secretary of Defense to conduct a demonstration project to evaluate the feasibility of using recovery auditing and to identify overpayments made to vendors by DOD. Authority to expand the program was provided in fiscal year 1998 under the National Defense Authorization Act.

The DOD demonstration project began in September 1996 when the Defense supply center in Philadelphia competitively contracted with Profit Recovery Group International [PRGI]. The contract covers purchases made during fiscal years 1993 to 1995 and requires PRGI to identify and document overpayments and to make recommendations to reduce future overpayments. PRGI receives a fee of 20 percent of net collected funds. The focus of the demonstration program is on purchases of subsistence, medical, and clothing items, items that are typically found in retail merchandising establishments.

We have reviewed the demonstration program and concluded that recovery auditing offers the potential to identify overpayments, but implementation problems hindered DOD from fully realizing the benefits of the program. As of June 1999, according to PRGI, it had completed 90 percent of its work and identified \$29.3 million in overpayments made to suppliers on purchases of roughly \$6 billion. However, collections by DOD, as of June 1999, only amounted to approximately \$2.6 million.

DOD has been slow to embrace recovery auditing. For example, in House Report 105-532, which related to a bill providing for fiscal year 1999 DOD authorizations, DOD was directed to expand the use of recovery auditing. We found, however, that DOD had not done so. While DOD issued an August 1998 memorandum encouraging the use of recovery auditing and some activities within DOD

have expressed interest in this concept, no contracts had been awarded at the time we completed our work in March 1999. We subsequently ascertained, however, that in June 1999, earlier this month, one of the recipients of the 1998 memorandum, the U.S. Transportation Command, had entered into such a contract and that it should be awarded in the near future.

The Government Waste Corrections Act of 1999 would require the use of recovery auditing by Federal agencies and provide incentives to improve Federal management practices with the goal of reducing overpayments. We believe the bill is a positive step in the government's effort to reduce overpayments and to obtain timely identification and recovery of overpayments when they occur. The act addresses recommendations we made in our recent report on DOD's demonstration program. This includes giving the head of the executive agency the option to perform recovery auditing with internal staff, by contract, or through a combination of internal staff and contract resources.

We believe it is very important that heads of agencies perform a sound evaluation of the applicability of recovery auditing to their operations and the related cost and benefits of undertaking internal recovery auditing before asking an external audit group to do such auditing. Simply stated, we believe that it is important to pick the low-hanging fruit before turning to contingency fee arrangements on the outside. Where recovery auditing can be cost-effectively used across government and whether that is the case remains somewhat of an open question that needs to be carefully thought through.

We also support the bill's requirement that recovery auditing contractors provide periodic reports with recommendations on how to mitigate overpayment problems and that, as part of the agency's management improvement program, the agency is to give first priority to addressing problems that contribute to overpayments.

Finally, the bill allows applicable appropriations to be reimbursed for costs incurred by government activities in supporting recovery audit efforts and to provide other incentives to support the use of recovery auditing. These features should eliminate some of the implementation problems we saw in the demonstration program at DOD.

While we are positive toward the concept of recovery auditing and its potential for application to the Federal Government, the government's experience with recovery auditing has been limited. Thus, we think it is a good idea to further mandate additional model programs in Federal agencies to determine the applicability of recovery auditing and to develop best practices for their use governmentwide. In conducting the mandated model programs—at least five are currently provided for in the bill—there should be sufficient diversity in where recovery auditing is modeled to adequately test the concept among the different types of payment activities. Beyond the mandate of the model programs, we believe that the use of recovery auditing should be, at least for the time being, available but not mandated for other Federal agencies.

The committee may also want to reexamine the bill's provisions relating to the use of recoveries made under the program. While financial incentives are critical to the program's success, incentives



that are too great are unnecessary and may undermine the program by creating inappropriate disincentives to making accurate and timely payments in the first instance. The committee may want to provide for a more substantial portion of the recoveries to be returned to the Treasury, therefore creating a win-win situation whereby the agency benefits and the taxpayers benefit as a result of this effort, more than just the recoveries.

We will be happy to discuss further technical comments with the committee staff.

In summary, Mr. Chairman, Federal agency managers have a fiduciary responsibility relating to and are accountable for the proper use of Federal funds. Our work has shown that in certain cases, these responsibilities are not being exercised adequately and the result is billions of dollars a year in improper payments, a substantial portion of which represent overpayments that may never be recovered.

Federal agencies need to achieve more effective control over their payment processes. The causes of the payment problems are varied and many are longstanding. The solutions can be found in the effective use of technology, the establishment of sound internal control and payment processes, and the wise use of human capital.

If Federal agencies do not effectively tackle these challenges, they will continue to risk erroneously paying contractors billions of dollars and perpetuating other financial management problems. Effectively addressing these challenges, however, will require investment and sustained commitment by top-level management. Recovery auditing, which has a longstanding track record in the private sector, offers a low-risk opportunity to identify and recover some of these overpayments.

We strongly support the provisions of H.R. 1827 providing for model recovery auditing programs. In this way, the government can assess the applicability of recovery auditing to different types of payments and develop the best practices for its use on a wider scale. In our view, with the use of model programs plus strong monetary incentives, it would be unnecessary to mandate recovery auditing across the government. There may also be opportunities to employ novel servicing arrangements, such as creating a center of excellence in a Federal agency to provide leadership to other agencies in implementing recovery auditing.

The keys to the successful execution of governmentwide recovery auditing programs are: one, meaningful incentives for agencies to want to participate in the program and to make it work; two, adequate safeguards to ensure that achieving congressional intent is attained and that the proper use of appropriations is maintained; and, three, assuring transparency in the conduct of the program.

Mr. Chairman, this concludes my statement. I would be happy to answer any questions that you or Chairman Burton may have at the present time.

[The prepared statement of Mr. Walker follows:]

**GAO**

**Testimony**

Before the Subcommittee on Government Management,  
Information and Technology, Committee on Government  
Reform, House of Representatives

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For Release on Delivery  
2 p.m.,  
Tuesday,  
June 29, 1999

**RECOVERY AUDITING**

**Reducing Overpayments,  
Achieving Accountability,  
and the Government Waste  
Corrections Act of 1999**

Statement of David M. Walker, Comptroller General  
of the United States



Mr. Chairman and Members of the Subcommittee:

I appreciate the opportunity to discuss H.R. 1827, the Government Waste Corrections Act of 1999, and its relationship to the long-standing issues of government accountability for use of public monies and overpayments and the role of recovery auditing in identifying and recovering overpayments. To put these issues in perspective, in fiscal year 1998, federal executive departments and agencies contracted for about \$173 billion in goods and services. The Department of Defense (DOD) spent about \$115 billion, or about two-thirds of this amount. In addition to direct contracting, federal agencies indirectly pay out many more billions of dollars annually for health care, education, and agricultural programs.

One of the most important issues facing the government today is the need for greater accountability in managing the finances of our national government. It is a significant problem at many agencies, and one that has been the subject of frequent reports by us and others. One key aspect of the problem is the difficulty the government has in assuring proper payment of all its bills while avoiding overpayments.

My testimony, today, will discuss the dimensions of the overpayment problem, our past work on the DOD recovery auditing demonstration program, and the Government Waste Corrections Act of 1999. My comments on the bill reflect my belief that there are three principles that should guide a recovery auditing program. First, there should be meaningful incentives for agencies to want to participate in the program and make it work. Second, there should be adequate safeguards to ensure that the program is implemented in a manner intended by Congress and that preserves the integrity of the congressional appropriations process. Third, there should be transparency in the conduct of the program—that is, there should be evaluation and reporting of program implementation, in

this case, to include how the recovered amounts are used. In the context of these three principles, I will suggest opportunities to strengthen H.R. 1827.

#### RESULTS IN BRIEF

Significant financial system weaknesses, problems with fundamental recordkeeping and financial reporting, incomplete documentation, and weak internal controls continue to prevent the government from effectively managing many of its operations. Significant among these problems is the inability of federal agencies to determine the full extent of improper payments that occur in major programs and that are estimated to involve billions of dollars annually. Within the billions of dollars of improper payments is an unknown amount of overpayments.

While neither the federal agencies nor we have a good estimate of the extent of overpayments that occur each year, given the poor state of the financial and accounting records, we expect that they are significant. We know, for example, that between fiscal year 1994 and 1998, contractors returned about \$4.6 billion in overpayments to DOD.

At the direction of Congress, DOD is conducting a recovery auditing demonstration program to identify overpayments for subsistence, medical, and clothing items purchased in fiscal years 1993 through 1995. We evaluated the demonstration program and concluded that the concept of recovery auditing offers the potential to identify overpayments. However, we found that implementation problems have limited the program's success. As of June 1999, the recovery auditing contractor had identified about \$29 million in overpayments made to suppliers on purchase volumes of roughly \$6 billion. Collections by DOD amount to \$2.6 million. While authorized to do so, DOD has been slow to expand the use of recovery auditing beyond the initial demonstration program.

Although contractors are sometimes overpaid, under current law, they are not required to inform the government of the overpayment or to return the money prior to the government issuing a formal demand letter<sup>1</sup> requesting repayment. In effect, the overpayment provides an interest free loan to the contractor. Contractors should be required to notify the government of overpayments when they become aware of them and to return the money promptly upon becoming aware of the overpayments. If they do not return the money promptly, there should be some economic consequence.

Given the large volume and complexity of federal payments, federal agencies need to concentrate on paying bills properly in the first place. However, recognizing that some overpayments are inevitable, they also need to adopt best practices to quickly identify and recover them. The Government Waste Corrections Act of 1999 offers an opportunity to use recovery auditing to identify overpayments and the factors contributing to overpayments. We support the objectives of this important legislation. Some commercial companies have used recovery auditing for many years as one mechanism to identify and recover overpayments. The extent to which recovery auditing is applicable to the full range of federal agency overpayments, however, remains an open question since its use in the federal government has been limited. Thus, we strongly support provisions of the bill that provide for model programs. In this way, the government can assess the applicability of recovery auditing to different types of payments and develop best practices for its use on a wider scale. In our view, with this use of model programs, plus strong monetary incentives, it would be unnecessary to mandate recovery auditing across the government.

The Committee may also want to reexamine the provisions in the bill relating to reallocation or use of overpayment recoveries. While financial incentives are critical to the program's success, incentives that are too large are unnecessary

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<sup>1</sup> A demand letter is a formal notification to the contractor that it owes the government money.

and may undermine the program by creating inappropriate incentives to making accurate and timely payments in the first place. The Committee may want to provide for a substantial portion of the recoveries to be returned to the Department of Treasury.

#### POOR FINANCIAL CONTROLS ARE A GOVERNMENTWIDE PROBLEM

Across the government, improper payments, including overpayments, occur in a variety of programs and activities, including those related to contract management, federal financial assistance, and tax refunds. Reported estimates of improper payments total billions of dollars annually. Such payments can result from incomplete or inaccurate data that are used to make payment decisions, insufficient monitoring and oversight, or other deficiencies in agency information systems and internal controls. The risk of improper payments is increased in programs involving (1) complex criteria for computing payments, (2) a significant volume of transactions, or (3) an emphasis on expediting payments. The reasons for improper payments range from inadvertent errors to fraud and abuse.

The full extent of improper payments, however, is unknown because many agencies have not estimated the magnitude of improper payments in their programs, nor have they considered this issue in their annual performance plans. The use of appropriate performance measures relating to improper payments can provide a management focus on reducing related losses. For example, the Department of Health and Human Services has reported a national estimate of improper payments in its Medicare fee-for-service benefits since fiscal year 1996. For fiscal year 1998, the Department reported estimated improper payments of \$12.6 billion, or more than 7 percent, of Medicare fee-for-service benefits—down from about \$20 billion, or 11 percent, reported for fiscal year 1997 and \$23.2 billion, or 14 percent, for fiscal year 1996. An analysis of improper Medicare payments helped to implement several initiatives intended to reduce improper

payments. These initiatives significantly reduced the incidence of improper Medicare payments.

#### DOD IS A CASE FOR RECOVERY AUDITING

Because it spends more contracting for goods and services than all other agencies combined, it is particularly important that DOD have sound controls to ensure that contract payments are proper, accurate, and timely. In recent years, our reports have identified hundreds of millions of dollars in improper DOD payments, interest expense on late payments, and other financial management problems. For example, in March 1994, we reported that during a 6-month period in fiscal year 1993, the Defense Finance and Accounting Service (DFAS) in Columbus, Ohio--a principal DOD contract paying activity--processed \$751 million in payments returned by defense contractors.<sup>2</sup> Our examination of about one-half of these checks disclosed that about 78 percent represented overpayments by the government. We also found that while some contractors returned overpayments, others did not. In one case, an overpayment of \$7.5 million was outstanding for 8 years. We estimated that the government lost interest on the overpayment amounting to nearly \$5 million.

DOD continues to make substantial erroneous payments to its contractors. For example, in the 5 years between fiscal year 1994 and 1998, defense contractors returned about \$4.6 billion to DFAS Columbus—in fiscal year 1998, they returned \$746 million. However, some contractors were still retaining overpayments. For example, 4 of the 13 contractors we visited during a recent review were retaining overpayments totaling about \$1.1 million. At each location, contractor personnel told us that they had a practice of retaining overpayments until the government issued a demand letter requesting the overpayments be returned. Under current law, there is no requirement for contractors who have been overpaid to notify the

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<sup>2</sup> DOD Procurement: Millions in Overpayments Returned by DOD Contractors (GAO/NSIAD-94-106, Mar. 14, 1994).

government of overpayments or to return overpayments prior to the government issuing a demand letter for a refund. The magnitude of overpayments defense contractors are retaining is not known.

#### DOD Is Taking Actions To Address Payment Problems

DOD is taking steps to address its payment problems. Its initiatives include testing and adopting some best practices. In the long term, it is developing procurement and payment systems that will be linked by sharing common data. This linkage is expected to allow one-time entry of contract data critical to making correct payments. In the meantime, DOD is enhancing its current technologies to further automate the payment process, testing streamlined payment practices, and making efforts to reduce the number of contract fund citations. But, as we state in our recent high-risk report,<sup>3</sup> it is likely to be many years before DOD gets its payment problems under control.

#### Additional Steps Could Be Taken

Recognizing DOD's actions and the fact that DOD continues to overpay its contractors, one question is: are there additional steps that might be taken to improve the process for both identifying and collecting overpayments? The answer is yes.

First, we believe defense contractors, and for that matter, all contractors should be required to promptly notify the government of overpayments when they become aware of them. If they do not return the money promptly, there should be some economic consequence. This seems simple enough, but currently a

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<sup>3</sup> Major Management Challenges and Program Risks, Department of Defense (GAO/OCG-99-4, Jan. 1999).



contractor is not required to tell the government that it has been overpaid, nor is it required to return an overpayment until the government becomes aware of the overpayment and issues a demand letter for repayment. Many contractors do promptly return overpayments; however, some do not. While we know the amount of overpayments that contractors have returned to the government, we do not know how much they are still keeping. Thus, as pointed out earlier, the true magnitude of the overpayment problem is not known. In this regard, we will shortly begin a review to assess the extent to which defense contractors are retaining and not promptly returning overpayments to the government.

Second, we believe that all federal agencies should take advantage of best practices that commercial companies use to identify and recover overpayments. One such practice is the use of recovery auditing procedures. Clearly, the government's focus should be on paying its bills properly in the first place. However, for both private industry and government agencies, some payments are processed incorrectly for a variety of reasons. For instance, vendors make pricing errors on their invoices, forget to include discounts that have been publicized to the general public, neglect to offer allowances and rebates, or miscalculate freight charges. Government payment activities may also neglect to take discounts to which they are entitled. These mistakes, when not caught, result in overpayments. Identifying and recovering these types of overpayments is referred to as recovery auditing.

#### RECOVERY AUDITING OFFERS POTENTIAL TO IDENTIFY AND RECOVER OVERPAYMENTS

Recovery auditing started about 30 years ago, and it is used in several industries, including the automobile, retail store, and food service industries. Within DOD, the Army and Air Force Exchange Service and the Navy Exchange Service use recovery auditing. An external audit recovery group may be the only

group used by an organization or it may be used in combination with an internal group that examines invoices for overpayments prior to an external group's review.

Recognizing its potential value to the government, the Fiscal Year 1996 National Defense Authorization Act required the Secretary of Defense to conduct a demonstration program to evaluate the feasibility of using recovery auditing to identify overpayments made to vendors by DOD. Authority to expand the program was provided in the Fiscal Year 1998 National Defense Authorization Act.

The DOD demonstration program began in September 1996, when the Defense Supply Center, Philadelphia (DSCP), competitively contracted with Profit Recovery Group International (PRGI). The contract covers purchases made during fiscal years 1993-95 and requires PRGI to identify and document overpayments and to make recommendations to reduce future overpayments. PRGI receives a fee of 20 percent of net collected funds. The focus of the demonstration program is in purchases of subsistence, medical and clothing items, items that are typically found in retail merchandising.

We reviewed the program and concluded that recovery auditing offers potential to identify overpayments, but implementation problems hindered DOD from fully realizing the benefits of the program.<sup>4</sup> As of August 1998, PRGI had identified \$19.1 million in overpayments. However, recoveries of overpayments amounted to only \$1.9 million, in large part, because vendors took issue with some of the overpayments. This caused the recovery process to virtually stop for 8 months while the DSCP reviewed the merits of the vendors' issues. DSCP concluded

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<sup>4</sup> Contract Management: Recovery Auditing Offers Potential to Identify Overpayments (GAO/NSIAD-99-12, Dec. 3, 1998).

that the claims of overpayment were valid. However, according to the contracting officer, his letter of final decision regarding vendors' indebtedness has not been issued. PRGI continues to identify overpayments. As of June 1999, according to PRGI, it had completed 90 percent of its work and identified \$29.3 million in overpayments made to suppliers on purchases of roughly \$6 billion. Collections by DOD as of June 1999 amounted to \$2.6 million. According to PRGI, its overpayment identification rate under the demonstration program is 0.48 percent of purchases reviewed, which is consistent with its experience with new private sector clients before corrective measures are implemented. PRGI told us that, as corrective measures are implemented, the overpayment rate typically drops to about 0.1 percent of purchases reviewed.

PRGI has also made recommendations to DFAS and DSCP to reduce future overpayments, but, at the time of our review, DOD had not implemented them. These recommendations ranged from reprogramming payment systems to providing contracting personnel additional training to help them determine price reasonableness.

#### DOD Is Slow To Use Recovery Auditing Techniques

DOD has been slow to embrace recovery auditing. For example, in House Report 105-532, which related to a bill providing for fiscal year 1999 DOD authorizations, DOD was directed to use recovery auditing by selecting at least two commercial functions within its working capital fund and issuing a competitive request for proposal by December 31, 1998. We found, however, that DOD had not done either.<sup>5</sup> While DOD issued an August 1998 memorandum encouraging the use of recovery auditing, and some activities have expressed an interest, no contracts had been awarded at the time we completed our work in March 1999. In June 1999, we checked with the recipients of the August 1998 memorandum

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<sup>5</sup> Contract Management: DOD Is Examining Opportunities to Further Use Recovery Auditing (GAO/NSIAD-99-78, Mar. 17, 1999).

and, with the exception of the U.S. Transportation Command, which had just entered into a contract for recovery auditing services, no other contracts had been awarded. The Defense Commissary Agency said it has completed a statement of work, and plans to have a contract by July 30, 1999. The Defense Logistics Agency told us it issued a solicitation on May 28, 1999, to expand the use of recovery auditing from the demonstration program in place at DSCP to its other four supply centers. The Defense Logistics Agency said it plans to have a contract by August 31, 1999. Each of the services and the Defense Information Services Agency also expressed an interest in recovery auditing, and they are evaluating whether to use it.

#### Issues Related To Using Recovery Auditing

While we believe that recovery auditing could be beneficial to DOD and other federal agencies, there are some important implementation issues that need to be considered as federal agencies evaluate using recovery auditing to identify and recover overpayments. First, it is not clear how agencies should organize to perform recovery auditing. Should it be contracted out? Should it be performed with in-house personnel? Should some combination of the two be used? We believe that agencies need to carefully consider the extent to which recovery auditing is applicable to their operations and, if applicable, if it would be cost-effective to undertake moderate internal recovery auditing efforts to "pick the low hanging fruit" before turning audit recovery efforts over to an external group.

Second, it is important that there be (1) periodic reporting by those performing recovery auditing on the factors causing overpayments and on recommendations to reduce overpayments and (2) a process to evaluate these recommendations and implement those that make sense. One of the criticisms we made of the demonstration program was that DOD did not implement the contractor's recommendations to reduce overpayments.

Finally, it is important to recognize that the DOD demonstration program has been focusing primarily on identifying overpayments related to subsistence, medical, and clothing purchases. While representing an audit base of about \$7.2 billion, it is only a small part of the dollars spent on contracts by DOD each year. Most DOD expenditures are for purchases of major weapon systems. The applicability of recovery auditing to these types of contract payments is, at this time, unclear.

#### THE GOVERNMENT WASTE CORRECTIONS ACT OF 1999

The Government Waste Corrections Act of 1999 (H.R. 1827) would require the use of recovery auditing by federal agencies and provide incentives to improve federal management practices with the goal of reducing overpayments.

We believe the act is a positive step in the government's effort to reduce overpayments and to obtain timely identification and recovery of overpayments. The act addresses recommendations we made in our recent report on DOD's demonstration program. One recommendation was to give the head of an executive agency the option to perform recovery auditing with internal staff, by contract or through a combination of both internal staff and contract.

We are also pleased to see that the bill requires a contractor to provide periodic reports with recommendations on how to mitigate overpayment problems and that as a part of the agency's management improvement program, the agency is to give first priority to addressing problems that contribute to overpayments.

Finally, the proposed act allows applicable appropriations to be reimbursed for costs incurred by government activities in supporting recovery audit efforts and provides other incentives to support the use of recovery auditing. These features should help eliminate some of the implementation problems we saw in the demonstration program.

Suggestions to Improve the Bill

While we are positive toward the concept of recovery auditing and its potential for application in the federal government, the government's experience with the use of recovery auditing has been limited. Thus, we think it is a good idea to mandate further model programs in civilian and defense agencies to determine the applicability of recovery auditing and to develop best practices for their use governmentwide. In conducting the mandated model programs—at least five are currently provided for in the bill—there should be sufficient diversity in where recovery auditing is modeled to adequately test the concept among the different types of payment activities. Beyond the mandated model programs, we believe that the use of recovery auditing should, at least for the time being, be available, but not mandated, for other federal agencies. Currently, the bill provides for mandatory use of recovery auditing by federal agencies, in addition to the model programs.

The Committee may also want to reexamine the provisions in the bill relating to reallocation or use of overpayment recoveries. While financial incentives are critical to the program's success, incentives that are too great are unnecessary and may undermine the program by creating inappropriate incentives to making accurate and timely payments in the first place. The Committee may want to provide for a substantial portion of the recoveries to be returned to the Treasury. We will be happy to discuss further technical comments with the Committee staff.

CONCLUSIONS

In closing, Mr. Chairman, federal agency managers have a fiduciary responsibility relating to, and are accountable for, the proper use of federal funds. Our work has shown that, in certain cases, these responsibilities are not being exercised adequately and the result is billions of dollars a year in improper

payments, a portion of which represent overpayments that may never be recovered. Federal agencies need to achieve more effective control over their payment processes. The causes of the payment problems are varied and many are long-standing. The solutions can be found in the effective use of technology, the establishment of sound internal control and payment processes, and the wise use of human capital. If federal agencies do not effectively tackle these challenges, they will continue to risk erroneously paying contractors and perpetuating other financial management problems. Effectively addressing them, however, will require investment and sustained commitment by top-level management.

Recovery auditing, which has a long-standing track record in the private sector, offers a low-risk opportunity to identifying and recovering overpayments. We strongly support provisions of H.R. 1827 that provide for model recovery auditing programs. In this way, the government can assess the applicability of recovery auditing to different types of payments and develop best practices for its use on a wider scale. In our view, with the use of model programs, plus strong monetary incentives, it would be unnecessary to mandate recovery auditing across the government. There may also be opportunities to employ novel servicing arrangements, such as creating a "center of excellence" in a federal agency to provide leadership to other agencies in implementing recovery auditing.

The keys to the successful execution of government wide recovery auditing programs are (1) meaningful incentives for agencies to want to participate in the program and make it work, (2) adequate safeguards to ensure achieving congressional intent and the proper use of appropriations, and (3) transparency in the conduct of the program.

Mr. Chairman, this concludes my statement. For the record, major contributors to this testimony were David E. Cooper, Daniel J. Hauser, and Charles W.

Thompson. I will be glad to answer any questions you or the other Members of the Subcommittee may have at this time.

(707433 )



Mr. HORN. Well, I thank the gentleman for that very thoughtful statement and now yield for questioning to the chairman of the full committee, Mr. Burton of Indiana.

Mr. BURTON. The first thing that comes to my mind, which I alluded to in my statement, is that you said that—and I think about the DOD—that there was \$29 million, in overpayments and only \$2.6 million of that has been recovered? Is that correct?

Mr. WALKER. That is correct, sir.

Mr. BURTON. Well, why is that?

Mr. WALKER. There are a number of reasons, Mr. Chairman. I would be happy to provide more for the record, but first the contractor identifies the alleged overpayment and then there has to be actions taken on behalf of DOD in order to actually recover those moneys.

Mr. BURTON. What kinds of actions?

Mr. WALKER. Well—

Mr. BURTON. They have to send a bill out or a letter out saying there was an overpayment made and we want you to respond?

Mr. WALKER. Well, they would have to have some type of correspondence interaction. But, they typically would want to satisfy themselves that they agree that, in fact, there is an overpayment. I would be more than happy, Mr. Chairman, for the record, to provide some specific details if you would like.

[The information referred to follows:]

Responses to Questions From  
The CG's June 29, 1999 Testimony on  
"Government Waste Corrections Act of 1999"

**Question 1**

Provide the response for the record concerning DOD's recovery of only \$2.6 million of Only \$2.6 million of the identified \$29 million in overpayments (see pages 23 and 24 of the transcript)

**Answer**

The Defense Supply Center Philadelphia (DSCP) has recovered only \$2.6 million of the identified \$29 million in overpayments for two reasons. First, because vendors disagreed that overpayments were made, the process of recovering contractor-identified overpayments was halted for 8 months while DSCP reviewed vendor complaints. In April 1998, DSCP concluded that the vendor's concerns were not valid and decided to resume the debt collection process. The second reason only \$2.6 million has been recovered is the DSCP corporate decision to avoid potential litigation and/or the likelihood that indebted vendors will overwhelm the Armed Services Board of Contract Appeals with appeals. Rather than issue letters of final decision regarding vendor indebtedness, DSCP is trying to negotiate a settlement with each indebted vendor.

Mr. BURTON. Well, you know, for instance, with the Department of Defense, if a contractor wants to do business with the Department of Defense in the future on future contracts, if he has been overpaid to the tune of \$29 million, it would appear to me that he would check that out pretty quickly and make restitution. Otherwise, he might not be able to be a primary bidder on a contract in the future. I don't know why in the world it should take a long period of time once you find out there are \$29 million in overpayments to get it back and \$2.6 million is not even a tenth of that. It just doesn't make any sense.

Mr. WALKER. Mr. Chairman, clearly it should have been handled more expeditiously than it has. The only thing that we note in my full statement that I would like to add now is that—it is interesting—there are actually some provisions in the law right now I think that also need to be looked at, beyond what we are addressing here.

For example, right now the government can be required to pay interest if it does not make its payments on a timely basis. However, if contractors knowingly received overpayments, they are not required to pay any interest on those overpayments, even if they knowingly hold onto those payments for an extended period of time—potentially years—waiting for the Department of Defense to ask them.

Mr. BURTON. Well, that might be something we could even incorporate into this bill. If there is an overpayment made with the knowledge of the contractor and the contractor doesn't return that in a timely fashion, he pays an interest penalty. That is something I think our staff ought to write down and look at to the feasibility of putting in this bill.

The other thing I wanted to ask you about is you said that you want to have these audits done internally rather than externally. Why? It seems to me that if it had been handled—if the auditing process had been handled properly in the first place within the agency, the overpayment would have been caught initially. And if the overpayment wasn't caught, what is the incentive for the interior auditor to correct the mistake that was made?

Mr. WALKER. Mr. Chairman, actually I believe what is important is that efforts be taken to try to capture the low-hanging fruit.

Mr. BURTON. Well—

Mr. WALKER. Either through internal resources or external contractors. Either one or a combination thereof, before entering into contingent fee arrangements. My point is if we don't do that, then we can end up paying fairly significant contingent fees to recover overpayments that could more cost-effectively be obtained even potentially through contractor resources, but not under a contingent fee arrangement.

Mr. BURTON. Well, that might drag out for a long period of time. I mean, the overpayments have been known for a long time. The agencies involved have not been collecting those overpayments. The reauditing after the payments have been made hasn't been done very effectively. And the incentive for an outside auditing firm to do it will stimulate them to get the job done. And I am not sure that stimulation would be there on the inside of the agency.

Mr. WALKER. I think it is facts and circumstances. Let me give you an example—

Mr. BURTON. And, besides, wouldn't you have to have more funds expended in that agency to be able to provide for this reauditing?

Mr. WALKER. Not necessarily. I think there could be an impact on the appropriations process that would have to be examined. Let me give you one example, Mr. Chairman. HCFA had about \$24 billion in overpayments. They have gotten it down to about \$12 billion. Still too high. No question about it.

One of the things that we have been encouraging HCFA to do for some time, and they have adopted our recommendation, is to make use of commercially available software to help identify some of these overpayments. Such software is used widely in the private sector. That is something that HCFA has done, which is one of the reasons they found a lot of these recoveries. In that case, the government gets 100 cents on the dollar for all of the savings.

Mr. BURTON. Well, hasn't GAO reported regarding this reduction you are talking about that this decrease was attributable to better documentation provided to the auditors, rather than to a substantive reduction in improper payments?

Mr. WALKER. Much of it has been attributable to documentation, that is true. There has been some reduction in improper payments. But a lot of it was the documentation issue.

Mr. BURTON. Yes. Does this mean that the earlier figures were not accurate? I mean the higher figures there? You know, you said it was reduced from—

Mr. WALKER. I would say that we had better clarity as to the nature of what that number was. It wasn't exactly what was thought initially.

Mr. BURTON. But they may have been inaccurate.

Mr. WALKER. That is true. They could have been, Mr. Chairman.

Mr. BURTON. Have there been specific actions taken by HCFA over the last years or so that can be attributed to the decline in the overpayment estimates?

Mr. WALKER. They are taking actions now. For example, they have adopted our recommendation to use commercially available software in order to try to identify possible improper payments. It was a while in coming, but they have done it now.

Mr. BURTON. What is HCFA doing right now, specifically, to try to recover these overpayments?

Mr. WALKER. Well, they are taking a number of steps with both internal and external resources, including their normal contractual relationships to try to identify double payments; to try to identify payments for services that were not rendered; to try to identify payments where there may have been some upcoding with regard to the nature of the services that were rendered. Mr. Chairman, it is my understanding they are actually going to appear here after me and they would probably be in a better position to tell you exactly what they are doing.

Mr. BURTON. Well, I don't want to belabor my questioning because I know the chairman has questions, but I still can't see where these overpayments being handled within an agency with a reaudit would be that beneficial. I mean, if the problem hasn't been corrected by now, it seems like to me an exterior auditing firm with

an incentive to really get at it would be more accurate and more effective. Then, of course, the problem, once it is identified, is getting the money in. And I still can't understand why, with \$29 million-plus in overpayments to DOD, only \$2.6 million has been recovered and that is something else we need to look into.

Mr. Chairman, I thank you very much for yielding to me.

Mr. HORN. Well, you are certainly welcome to continue your line of questioning. Because you and I have it here, we can take all afternoon. [Laughter.]

Mr. BURTON. Well—

Mr. HORN. Go ahead.

Mr. BURTON. OK, sure. I mean, if you don't mind. You say that between fiscal years 1994 and 1998, contractors returned about \$4.6 billion in overpayments to DOD. Were these overpayments voluntarily identified and returned by the vendors?

Mr. WALKER. It is my understanding that most of them were identified by the contractors.

Mr. BURTON. Was DOD even aware of the overpayments, in many cases?

Mr. WALKER. Not all of them, no. Their financial records—

Mr. BURTON. Well, that brings up this question again about interior auditing. I mean, if you have got auditors—don't they have auditors at DOD?

Mr. WALKER. They do, Mr. Burton.

Mr. BURTON. And payments are made and \$4.6 billion is returned in overpayments and much of that was returned without the knowledge of the people in DOD that they were overpayments? And you want to have these reaudits done internally?

Mr. WALKER. Not necessarily by the same people, Mr. Chairman. Let me clarify. We don't oppose the use of external contractors. Let me make it clear. We are not saying that at all. We are saying that an agency may decide on day one that it wants to use external contractors as a means to deal with this issue. We don't have a problem with that.

Mr. Burton, my only point is that one should consider, based upon individual facts and circumstances, if agencies haven't done anything to try to get the low-hanging fruit, whether you should go to a contingent fee arrangement on day one or whether you ought to try to consider another fee arrangement with external contractors and then go to contingent fees. It is just facts and circumstances.

Mr. BURTON. It seems to me that right now the auditing departments of all these agencies ought to be going through the billing records on a regular basis and finding out if overpayments were made. That is their job. And if they are not doing it now, I can't for the life of me figure out why they would do it if we hired some more people and put them in there.

Mr. WALKER. As you know, Mr. Chairman, we are, on record, for several years, as saying that many aspects of DOD's financial management system are a high-risk to the government. They don't have adequate internal controls. They don't have adequate accountability mechanisms. And we are trying to shine the light on that to try to get them to improve it.

Mr. BURTON. Well, in the short run, an exterior audit firm might light a fire under them. Congress can always restructure the auditing process. But, as far as I am concerned, there needs to be a strong incentive for there to be corrections in the auditing process. And that incentive, I think, is not going to come from an interior restructuring.

Mr. HORN. Would the gentleman yield on this topic?

Mr. BURTON. Be happy to yield.

Mr. HORN. A few years ago, I held a hearing entitled, "The Defense Department: What did you do with the \$25 billion we can't find?" And what it seemed to get down to was what we are noting in some of our questions here. The Defense Finance and Accounting Service in Columbus, OH. Did the General Accounting Office go out and look at that operation or did they leave it to Defense? Do you know, offhand whether they took a careful look at it?

Mr. WALKER. Yes, we have been out there. The primary responsibility is with the IG but we do work at DFAS in various locations.

Mr. HORN. Well, we let 2 years go by to see if they could clean it up. And then, presumably, they have got it down to \$10 billion we can't find. So \$15 billion was accounted for.

Now how come we got to the \$25 billion? It seemed to be the following: No. 1, they were having GS-1s—and I hadn't heard of those since the first world war. I wasn't around then, but I read it. And apparently GS-1s were staffing some of that. And contractors were getting checks from the government out of that center and they would phone up and say, I don't have a contract with the government. And the Defense group there would say, "oh, yes, you do. Our records show you do."

One guy, I am told—and I don't think it is just apocryphal—put the check in interest earning. And he knew they would get around to it some day. And they did. And he paid them back the amount of overpayment, but he kept the interest. And apparently he was pretty well paid by that little thing.

So one of the problems is the man power at what level of brains and knowledge. And, No. 2, the type of training that goes on in a center like that. It seems to me you have got to build in the blocks before those checks go out. And that is where an internal auditor ought to be working and picking randomly some of these checks to see if the paper matches.

Well, what the problem was on the \$25 billion is they had ordered \$25 billion. The acquisition documents never quite related to the inventory documents. So you would find it if you could. And I just wondered the degree to which GAO is looking at some of it or are you taking the Inspector General's word for it?

Mr. WALKER. No, we are.

Mr. HORN. Because we have great faith in the Inspector General over there.

Mr. WALKER. Several things, Mr. Chairman. Three things are really key in this area. First, people; second, process; third, technology. On the people front, you have mentioned two of the key ingredients. You have got to have people with the right kind of skills doing this work. They may or may not exist within the current organization. You may have to go out to the outside. And you need

training for the people that are doing this work, if they are internal.

Second, concerning the process, among other things, you need internal controls. You need solid internal controls.

Third, concerning technology, we have to automate much of this and we have to integrate systems. There are so many different systems at DOD.

But, you know, those are three key elements. And, in many cases, you are going to have to turn to contractors because you don't have the resources internally in order to get it done.

Mr. HORN. OK. Go ahead. I yield back.

Mr. BURTON. Yes. My very able staff assistant just mentioned that, I guess in the correspondence we have had on this issue, the various agencies including DOD say that the reauditing is not a core function of the Department. And, with the lack of adequately trained personnel, it seems that the prudent thing would be to use exterior auditors until you were able to bring your staff up to snuff.

Now when these overpayments voluntarily came back to the DOD, was that money credited back to the government or did it go back to the programs? Where did it go?

Mr. WALKER. I am not sure, Mr. Chairman. I can try to provide some more information for the record.

Mr. HORN. Without objection, the answer of GAO will be put in the record at this point.

[The information referred to follows:]

Responses to Questions From  
The CG's June 29, 1999 Testimony on  
"Government Waste Corrections Act of 1999"

Question 2

Now when these overpayments that voluntarily came back to DOD, was that money credited back to the government or did it go back to the programs?

Answer

Generally, 31 U.S.C. 3302(b) requires that money received for the government from any source be deposited into the Treasury. However, there are exceptions. An agency may retain moneys it receives if it has statutory authority to do so, and receipts that qualify as "repayments" to an appropriation also may be retained. "Repayments" may be either reimbursements or refunds, the latter being amounts collected from outside sources for payments made in error, overpayments, or adjustments for previous amounts disbursed. We were told that in this case the money was sent to the Treasury.



Mr. WALKER. Thank you.

Mr. BURTON. OK. And my understanding is that in the case of Medicare overpayments voluntarily returned to HCFA, checks were returned because there was no systematic way to deal with this money coming back to the government. You know, that just boggles my mind. Somebody sends a check back to HCFA saying, "Hey, listen, this is an overpayment that we didn't deserve," and they sent it back him, saying, "We are sorry. You are going to have to just keep the money because we don't know what to do with it." That boggles my mind—how can that happen?

Mr. WALKER. It is mind-boggling, Mr. Chairman. You are right there. It does happen.

Mr. BURTON. I mean, people want to do the right thing and send money back to the government for an overpayment and you say, gosh, you are just going to have to keep it because we don't know what to do with it?

Mr. WALKER. Well, it is mind-boggling that it would happen. But, there are many circumstances I mentioned earlier where, actually, people know it is an overpayment. They don't send it back because, under current law, they take the position that they don't have to until they are notified. And, in fact, there is no economic incentive for them to send it back.

Mr. BURTON. Yes, I understand. But I don't want to change the subject.

Mr. WALKER. Sure.

Mr. BURTON. We are talking about payments that are voluntarily sent back and it boggles the mind to send a check back to somebody just because you don't know how to enter it. And you are worried about reauditing? I mean, if they don't know how to—I mean, I took bookkeeping in college, you know. And it is not that hard to put it in the bank and mark it down, you know? I don't understand that.

Mr. WALKER. The people that actually process the payments that are supposed to put those in the bank aren't the ones that would be doing the auditing. But I hear you, Mr. Chairman.

Mr. BURTON. I understand that the places in government now using recovery auditing are not funded on annual appropriations but are set up on revolving funds or no-year accounts. In other words, they are attuned to a monetary bottom line like businesses in the private sector. In order to create this kind of incentive for regularly appropriated agencies, my bill would allow 25 percent of the moneys or up to 25 percent of the moneys to go back to the program that it originated from. Do you see any problem with that kind of an incentive?

Mr. WALKER. Mr. Chairman, we think it is essential that you have an incentive for the agencies to want to play and to participate in this program. And, in fact, what we had suggested was something along the lines of 50 percent of the money being able to go back to the agency and 50 percent going for the taxpayer. So I think it is crucial that you have an incentive for the agencies.

Mr. BURTON. OK. Finally, you said that if we required the use of model programs and provide the right incentives, it would not be necessarily to mandate the use of recovery auditing across the

government. I think you have elaborated on that, but is there anything further you would like to add to that?

Mr. WALKER. I think it is critical that we have some additional model programs that look at different aspects of where recovery auditing might be applied. And, at least five of those should be required. I think, beyond that, if you provide the kind of incentives that we are talking about, that should go a long way to encouraging people to do this. And if they don't, you can always go to a mandate system.

Mr. BURTON. OK. Let me ask just one more question.

Mr. WALKER. Sure.

Mr. BURTON. To put a recovery auditing system in these agencies where it does not now exist would take time, right?

Mr. WALKER. That is correct.

Mr. BURTON. Do you have any idea what kind of time?

Mr. WALKER. Well, it depends on the program, Mr. Chairman.

Mr. BURTON. Well, it would take some time. The outside recovery auditing companies are ready to go right now. They have got the auditors there. They have done it. They have got the experience. Why should we wait when we know that these overpayments are made? We know that the waste is there. We know that they should be recovered. Why should we wait for a model program when it is going to take time to put it in place when we already have an outside entity that can do it?

Mr. WALKER. I guess my only point, Mr. Chairman, would be if you take a number like \$10 million—which is what the bill currently proposes—if you look at the number of Federal entities and agencies that would be affected by that, it would be a significant number. The types of purchases they end up making are fundamentally different and I think that there would be a lot of time and energy spent on the contracting aspect of it. So it is really just a cost-benefit question, frankly, from a different perspective, Mr. Chairman.

Mr. BURTON. What if the threshold were raised to \$50 million or \$100 million or \$500 million?

Mr. WALKER. Obviously, we would have to take a look at how that would affect the number of entities that would potentially be impacted by it.

Mr. BURTON. OK. OK. Thank you, Mr. Chairman.

Mr. HORN. Thank you. Some of this has been covered, but let me just ask it for the record's sake. According to your testimony, the General Accounting Office supports the provisions of the bill with Mr. Burton providing for model programs for recovery auditing. What are the Federal programs you suggest using for these model programs? Which ones would you say we ought to apply that to?

Mr. WALKER. Well, we don't speak to specific programs. I would be happy to provide something for the record if you would like. I do think that what we need to do is we need to analyze what are the different types of purchasing activities that the Federal Government engages in. Also, we ought to make sure that we have at least one program for each major type of purchasing activity.

One area that is more problematic, but I think we ought to explore is how recovery auditing can be applied. But, there are some unique issues that need to be explored in the health area. Contrac-

tors give a lot of money in overpayments, but there are also some peculiarities in dealing in the health area, because many of these overpayments have to do with medical decisions, medical necessity, and the nature of the services that are being provided. I think that might be an example where you might need to take a look at it because there are specific things that have to be looked at that would be different than, for example, how it has been applied at DOD where they are purchasing, clothing and supplies. Recovery auditing has been used for decades in the private sector for those types of activities.

I might add, recovery auditing has been used in health care as well in certain circumstances in the private sector.

Mr. HORN. Well, would GAO say, let us start on the ones with the largest amount of money that are overpayments and deal with that?

Mr. WALKER. There is clearly a logic to that, Mr. Chairman.

Mr. HORN. OK. Now you mentioned the purchasing models. Give me an idea. What are the purchasing models that you are thinking of?

Mr. WALKER. When you are contracting for things that are readily commercially available on the outside. Obviously, in this instance, there is clearly an application. When you are contracting for major weapons systems or other things that are customized, obviously, there is potential application there too, but one would have to approach it a different way.

When you are dealing in the health care area, there is potential application, but there are a number of special considerations, given the nature of how overpayments might occur. Obviously, if it is a double payment or if it is for service that wasn't rendered, that is easier than if a judgment call has to be made as to whether the service that was provided was appropriate under the circumstances, based upon the nature of the illness?

So those would be three examples, Mr. Chairman.

Mr. HORN. OK. Another question for the record. The Government Waste Corrections Act of 1999 currently provides that of the amounts collected through recovery auditing, up to 50 percent can be applied for management improvement programs. Up to 25 percent can be applied for the payment of the contractor and to reimburse the fund from which overpayments were made. You testified that you would reexamine the allocation of overpayment recoveries and provide for a substantial portion to be returned to the Department of the Treasury. Why do you suggest these changes and how would you restructure the allocations?

Mr. WALKER. Our view is that if you say that 50 percent of the recoveries would go to the agency either to pay for the contractor and/or to reinvest in their systems and programs to prevent this from happening in the future or to minimize it, that that should be enough of an incentive and should provide enough funding for the agencies to engage in this activity, especially if it is on a contingent basis where they only have to pay if the amounts are actually recovered.

Mr. HORN. Well, if that is at the 50 percent mark, does that mean we simply apply that money to better cost recovery? Or do we let the agency do anything with it?

Mr. WALKER. No. I think you want to target it, as has been contemplated in this bill, to the types of initiatives that are designed to improve the systems, the controls, and the recovery mechanisms that the bill is intended to address.

Mr. HORN. OK. In other words, this would relate to getting new human resources in auditing.

Mr. WALKER. Either systems or human capital or enhanced processes.

Mr. HORN. Right. Or investment in computing.

Mr. WALKER. Correct. Technology, for example. I agree, Mr. Chairman.

Mr. HORN. OK.

Mr. WALKER. One of the three: People, process, technology focused in this area.

Mr. HORN. Do you feel the current ratios may create inappropriate incentives, which is from the bill?

Mr. WALKER. We think there clearly ought to be something directly in this for taxpayers. The taxpayers ought to get part of this recovery. And we are a little concerned, Mr. Chairman, that the agencies not be in a circumstance where they get 100 cents directly or indirectly of every dollar that is recovered because that might create a perverse incentive for them to overpay in the first instance.

Mr. HORN. Right.

Mr. WALKER. We don't want to do that.

Mr. HORN. OK. Does the gentleman from Indiana have any other—

Mr. BURTON. Mr. Chairman, unfortunately I have to depart for another meeting. But I want to thank Mr. Walker for his candor and you for holding this hearing. And I hope we can work out any differences we might have so we can get this bill moving as rapidly as possible. I think we have got a little difference on the exterior rather than interior auditing, but maybe we can work that out and get a bill that we can all live with and save the taxpayers a lot of money.

Mr. WALKER. Thank you, Mr. Burton.

Mr. BURTON. Thank you. Thank you, Mr. Chairman.

Mr. HORN. Thank you. And thank you, Mr. Comptroller General. We will now go to panel two.

Mr. WALKER. Thank you, Mr. Chairman.

Mr. HORN. Thanks for coming.

Panel two has the Honorable Deidre Lee, Acting Deputy Director for Management, Office of Management and Budget; Mr. George H. Allen, Deputy Commander, Defense Supply Center of Philadelphia; Mr. Gerald R. Peterson, Chief, Accounts Payable Division, Army-Air Force Exchange Service; and Ms. Michelle Snyder, Director, Financial Management Office, Chief Financial Officer of the Health Care Financing Administration.

If you would stand and raise your right hands. And are there any assistants in back of you that might be talking? If they are, get them to stand, too. I only like these baptisms once. All right. Fine. We have one. Anybody else? Two. So we have got six witnesses to be sworn. Do you affirm—there are a few back there somewhere? OK. So we have got seven, then. Is that it? All right.

[Witnesses sworn.]

Mr. HORN. OK. It seems the lips were moving. Yes, it is eight. It was eight. OK.

So that is taken care of and we now start with Ms. Lee. And we are glad to see you here. And, as you know, your statement is in the record. We would like you to summarize it and then we will have more time for questions.

**STATEMENTS OF DEIDRE LEE, ACTING DEPUTY DIRECTOR FOR MANAGEMENT, OFFICE OF MANAGEMENT AND BUDGET; GEORGE H. ALLEN, DEPUTY COMMANDER, DEFENSE SUPPLY CENTER OF PHILADELPHIA; GERALD R. PETERSON, CHIEF, ACCOUNTS PAYABLE DIVISION, ARMY-AIR FORCE EXCHANGE SERVICE; AND MICHELLE SNYDER, DIRECTOR, FINANCIAL MANAGEMENT OFFICE, CHIEF FINANCIAL OFFICER OF THE HEALTH CARE FINANCING ADMINISTRATION**

Ms. LEE. Thank you very much. Good afternoon, Chairman Horn, Mr. Ose. I am here today to discuss the administration's view on H.R. 1827, the Government Waste Corrections Act of 1999. This bill would mandate that agencies use the technique of recovery auditing to identify and collect overpayment to vendors and contractors.

At the outset, let me clearly state that we share the committee's desire to eliminate overpayments. Our goal is to make all payments correctly and on time. When we pay correctly the first time and on time, we prevent errors and eliminate the need and expense of correction and collection. Making the right payment at the right time is the most cost-effective approach for reducing erroneous payments whether the payment is made to a contractor, a food stamp recipient, or a Medicare provider.

In conjunction with the Congress, the administration has made progress in improving overall financial management, yet there is more to be done. We will continue to make improving financial management systems and modernizing payments a high priority. This priority is reflected in this year's financial management status report and 5-year plan, which will be transmitted to the Congress soon.

Progress has been made and significant initiatives are underway. For example, use of technology. Agencies are updating their financial systems, including electronic payment systems. These systems automate document matching, reduce errors associated with paper payment systems, and provide automated checks and edits to prevent the occurrence of duplicate payments, pricing errors, and missed cash discounts, rebates, or other allowances.

We are also simplifying small transactions paying processes. The 80-20 rule applies here; 80 percent of the transactions equate to 20 percent of the dollars. Use of purchase cards also simplifies the buying process. And, as you know, Chairman Horn, that is near and dear to my heart as we talk about acquisition reform.

By using purchase cards, we streamline the payment process and save the cost, both in terms of dollars and labor resources, for most small purchases, or the 80 percent. We are also revising circular 8125. You had hearings on this just a few weeks ago. We are focus-

ing on ways to facilitate electronic payments and improve implementation of the Debt Collection Act.

Specifically, in recovery auditing, we are working with the DOD to evaluate the results of their demonstration project in recovery auditing. In recognition of recovery auditing as a tool for other agencies, GSA established a multiple award schedule to provide Federal agencies with easy access to private sector experts in recovery auditing who can tailor techniques to meet specific agency requirements.

We are working with the users of this schedule to gain additional insight into the uses and benefits of recovery audits. As you can see, we are focusing on paying correctly. H.R. 1827 includes some promising provisions: Paying for audit recovery services out of proceeds; gainsharing for our financial management improvement; identifying management improvement opportunities; and rewarding employee performance.

We also have some issues with H.R. 1827, which I would like to highlight today. Specifically, thresholds: Requiring recovery audits for payment activities that expend \$10 million or more annually. Using the industry recovery standard of \$1 million recovered for every \$1 billion audited, a threshold of \$10 million would result in gross collections of \$10,000. While this is not insignificant, based upon work that is already done to certify accurate payments, as well as the cost of setting up the program, requiring or mandating recovery audits may not be cost effective at this threshold.

Payment activity. This term may be read to include benefit and entitlement payments. Most major benefit and entitlement programs have statutory provisions for identifying and recovering overpayments. HCFA will address this today in their testimony. We need to clarify the proposed applicability and retain appropriate tailoring of recovery audits to specific programs.

And, last, but not least, congressional appropriations. I think it was discussed at length with Mr. Walker, but this bill allows agencies to return up to 25 percent of collections to programs. We need to ensure that this return process is consistent with congressional intent and the appropriations process. And, also, be sure we emphasize the correct incentives for reaction to recovery audits.

Mr. Chairman and members of the subcommittee, the administration is committed to good financial management and making the right payment on time. We will continue our efforts, working with the CFOs, to identify and address ways to improve accountability, specifically, payment accuracy, including exploring the use of recovery audits. We welcome the opportunity to work with you in exploring the most effective means of using recovery audits. And I will be pleased to answer any questions you may have.

[The prepared statement of Ms. Lee follows:]



EXECUTIVE OFFICE OF THE PRESIDENT  
OFFICE OF MANAGEMENT AND BUDGET  
WASHINGTON, D.C. 20503

**STATEMENT OF DEIDRE A. LEE  
ACTING DEPUTY DIRECTOR FOR MANAGEMENT  
OFFICE OF MANAGEMENT AND BUDGET  
BEFORE THE  
COMMITTEE ON GOVERNMENT REFORM AND OVERSIGHT  
SUBCOMMITTEE ON GOVERNMENT MANAGEMENT, INFORMATION  
AND TECHNOLOGY**

June 29, 1999

Chairman Horn, Congressman Turner, and Members of the Subcommittee, I am pleased to be here today to discuss the Administration's views on H.R. 1827, "The Government Waste Corrections Act of 1999." This bill would require that agencies use the technique of recovery auditing to identify and collect overpayment to vendors and contractors.

At the outset, let me state that we strongly share the Committee's desire to eliminate our overpayments to the providers of goods and services purchased for the Federal Government. Overpayments detract from agencies' ability to carry out their missions by diverting resources from their intended uses.

Our goal is to make all payments correctly and on time. When we pay correctly and on time, we prevent errors and eliminate the need and expense of collection. Making the right payment at the right time is the most cost-effective approach for reducing erroneous payments -- whether the payment is made to a contractor, a food stamp recipient, or a Medicare provider.

The Administration will continue to make improving financial management systems and modernizing payments a high priority. This priority is reflected in this year's "Financial Management Status Report and Five-Year Plan" which will be transmitted to Congress soon.

Ongoing Activities

Significant initiatives are underway to ensure that we pay correctly and on time.

Agencies are installing modern electronic payment systems. These systems automate document matching, reduce the errors associated with paper payment systems and free up valuable staff time for other workload priorities. Modern payment systems provide automated checks and edits to prevent the occurrence of duplicate payments, pricing errors, and missed cash discounts, rebates or other allowances.

Federal agencies are increasing their purchase card use for Government purchases below \$2,500. In 1999, government purchases through the use of the purchase card have reached 60 percent and are expected to increase to over 80 percent of all purchases below \$2,500 in 2000. This means that we are effectively streamlining our payment process for most small purchases.

OMB in close consultation with Treasury and the major payment agencies is revising the OMB Prompt Payment Circular (A-125) to facilitate electronic payments and to implement the requirements of the Debt Collection Improvement Act such as the requirement that agencies collect the Tax Identification Number (TIN) which is useful for matching vendors against our delinquent debtor files.

Specific action we have underway in audit recovery include the following:

(1) The National Defense Authorization Act of 1998 required the Secretary of Defense to conduct a demonstration program to evaluate the use of recovery auditing. Based on the pilot study, about four tenths of one percent of the payments sampled were incorrect. According to industry experts, the private sector runs an error rate of about one tenth of one percent. So far of



the over \$25 million identified \$2.6 million has been collected excluding the cost of the contractor's fees. OMB will monitor this pilot in order to better gauge the cost-effectiveness of recovery auditing.

(2) Several of the major payment agencies are ready to acquire recovery auditing services. In March of 1998, the General Services Administration (GSA) established a multiple award schedule to provide Federal agencies with easy access to private sector experts in recovery auditing who can tailor techniques to meet specific agency requirements. These contracts are priced on a contingency basis – that is, firms are only paid when money is recovered. The commission is 20 percent (as opposed to the 25 percent cap proposed in H.R. 1827). Contracts are in place at the U.S. Transportation Command and the Department of Veterans Affairs.

As you can see, significant efforts are underway to ensure that we make the right payment on time.

#### Specific Issues with H.R. 1827

H.R. 1827 includes some promising provisions on paying for audit recovery services out of proceeds, gainsharing for financing management improvement, and rewarding employee performance. While we support the aims of these provisions, these concepts need additional refinement.

We also have several issues regarding H.R. 1827 that we would like to highlight today, specifically:

- The bill requires that agencies conduct recovery audits for payment activities that expend \$10 million or more annually. Considering that the private sector recovery standard is \$1 million for every \$1 billion audited, a threshold of \$10 million would result in gross collections of \$10,000 dollars. Because of the work that is already done to certify accurate payments as

well as the additional cost of setting up the program and the cost of the audit, recovery audits may not be cost-effective at a low threshold.

- The term "payment activity" in H.R. 1827 may be read to include benefit and entitlement payments. Most major benefit and entitlement programs already have statutory provisions for identifying and recovering overpayments which may be inconsistent with the requirements of H.R. 1827. For example, the Medicare program currently contracts with entities to identify and collect overpayments made from the Medicare Trust Fund. These overpayments are returned to the Trust Fund to ensure that Medicare can continue to pay for services provided to beneficiaries. Our contractors are already paid to perform this function, and thus should not receive an additional payment for doing this work.
- The bill would allow agencies to return up to 25 percent of collections to programs and activities from which the overpayment arose. These provisions could be used to bypass the normal Congressional appropriations process.

Conclusion

Mr. Chairman and Members of the Subcommittee, as I hope you can see, the Administration is committed to making the right payment on time. We will continue our efforts to be diligent in authorizing payments correctly up front, improving our financial management, and exploring the use of recovery audits.

We will continue to review the bill and welcome the opportunity to work with you in further exploring the most effective means of using recovery audits. This concludes my prepared remarks. I would be pleased to answer any question you or any Member of the Subcommittee might have.

Mr. HORN. Thank you. We will have the questions deferred until after the four witnesses have testified.

Mr. George H. Allen is the Deputy Commander, Defense Supply Center of Philadelphia. Welcome.

Mr. ALLEN. Good afternoon, Mr. Chairman, distinguished members.

I will just summarize my remarks. On behalf of the Department of Defense, I want to thank you for the opportunity to appear here before the subcommittee to describe our experience with recovery auditing. The 1996 Defense Authorization Act directed the Defense Personnel Support Center, which has since been renamed the Defense Supply Center of Philadelphia or later referred to as DSCP, to be the test site for demonstration of private-sector recovery auditing.

In September 1996, DSCP competitively contracted with Profit Recovery Group International [PRGI] as I will refer to them. Although the pilot program is not complete, I can say with certainty, the commercial recovery auditing has proven to be a cost-effective practice for our center.

Let me describe briefly how we demonstrated this commercial practice. As law directed, we required PRGI to audit available accounting and procurement records from fiscal years 1993 through 1995. The audit base was \$7.2 billion in payments to vendors over that 3 year period. Thus far, PRGI has identified potential overpayments of about \$27.3 million. The overpayment arose from a variety of reasons, including duplicate payments, interest paid in error, discounts offered but not taken, overcharges, and breaches of the price warranty provisions in our contracts.

Of the amount identified, we have collected \$2.6 million, leaving a potential uncollected balance of \$24.7 million. We have moved forward to issue claims to collect about \$10.4 million in those overpayments and another \$2 million in dispersing errors. We have not yet approved \$12.3 million of potential overpayments.

In addition to the numerical data just reviewed, I believe the demonstration project has benefited our operation in three other ways. First, recovery auditing has allowed us to continuously encourage vendors to comply with contract terms and conditions. The additional scrutiny of recovery auditing has provided and will continue to provide more assurance that overpayments will be identified and collected promptly.

Second, the auditing process has uncovered systemic problems, including the need to fine tune our automated payments systems to assure that we comply with all statutory requirements.

And, third, dispersing errors uncovered by the auditing program have highlighted the need for closer oversight of the payment function itself and should result in the reduction of these types of errors in the future.

Mr. Chairman, I would like to now briefly discuss our expansion plans with NDLA. The 1998 Defense Authorization Act directed the recovery auditing be expanded to all Defense Working Capital Fund activities. However, under this legislation, the program will be self-funding. That is, the audit contractor's fee will be paid from the amounts recovered. As with the original demonstration program, fees may not exceed 25 percent of the total recovered. DSCP

is serving as the lead center for expansion to other DLA agency activities. A competitive solicitation has been issued and we anticipate an award by the end of next month.

In closing, Mr. Chairman, let me say the recovery audit programs have been successful at DSCP and they have become an integral part of our business practices in Philadelphia. And I am prepared to answer any questions at the appropriate time.

[The prepared statement of Mr. Allen follows:]

**STATEMENT OF  
MR. GEORGE H. ALLEN  
DEPUTY COMMANDER, DEFENSE SUPPLY CENTER PHILADELPHIA  
BEFORE THE  
SUBCOMMITTEE ON GOVERNMENT MANAGEMENT, INFORMATION,  
AND TECHNOLOGY  
HOUSE COMMITTEE ON GOVERNMENT REFORM AND OVERSIGHT  
JUNE 29, 1999**

Good afternoon Mr. Chairman and distinguished members. I am George Allen, Deputy Commander of the Defense Supply Center Philadelphia. I appreciate the opportunity to appear before this subcommittee to discuss the Defense Logistics Agency's participation in a demonstration program using private sector recovery audit services. Let me begin with some brief background on the Defense Supply Center Philadelphia.

### **BACKGROUND**

The Defense Supply Center Philadelphia is one of the Defense Logistics Agency's five supply management centers. Our mission is to ensure the combat readiness and sustainment of America's Fighting Forces by providing world class logistical support in peace and war. We also support other federal agencies and some foreign governments. We are the providers of food, clothing & textiles, medicines & medical supplies. Our mission extends to peacetime military operations that include ensuring capability to support other non-war activities such as disaster relief and humanitarian aid. We have 33 branch offices throughout the United States, Europe and the Pacific. We buy and sell over \$3.2 billion in product annually.

### **SUBCOMMITTEE TOPIC**

The 1996 Defense Authorization Act required the Secretary of Defense to conduct a demonstration program to evaluate the feasibility of using private contractors to identify overpayments made to vendors by the Department of Defense (DoD). The process of identifying and recovering overpayments is referred to as recovery auditing. The Act directed the demonstration program be conducted for the Defense Logistics Agency (DLA) and include the Defense Personnel Support Center, which has since been renamed the Defense Supply Center Philadelphia (DSCP). The Act further provided that the audit focus on records related to fiscal years 1993, 1994, and 1995, and that the contractor be required to use data processing techniques generally used in audits of similar private-sector records. It authorized that the contractor could be paid up to 25% of amounts recovered on the basis of information obtained by the audit. The Act further made \$5,000,000 available under the program. Payment records for all three of DSCP's major

commodity groups (Clothing, Medical, and Subsistence) were audited. The universe of potential overpayments was approximately \$7.2 billion for the three-year period.

In September 1996, DSCP competitively contracted with Profit Recovery Group International, hereafter referred to as PRGI. For its performance under the contract, PRGI is paid a fee of 20% of net amounts recovered as a result of information it provided through the audit. PRGI performs most of the audit work at its on-site location at the Defense Finance and Accounting Service (DFAS) in Columbus Ohio. Some additional data processing is performed at PRGI's headquarters in Atlanta.

As part of the effort, the contracting officer at DSCP appointed a technical representative at DFAS in Columbus to review disbursing-type errors identified by PRGI. Disbursing errors include among other things, duplicate payments, unauthorized charges, payment for material not received, interest paid in error, discounts offered but not taken, and any systemic errors of our automated disbursing systems.

The audit work began in June 1997. At that point, the records being audited were up to 4 years old. As with their private sector audits, one of PRGI's first actions was to request that vendors submit statements of their accounts with DSCP. In many instances, the statements showed aged credit balances that vendors were holding from previous transactions. Thus far, we have identified and collected more than \$2 million of overpayments from that action alone.

Through 1998, PRGI continued its audit work, including a review of DSCP contractual terms and conditions. One clause in some of our contracts during that time required suppliers to warrant their prices and payment discount terms to be as good or better than what they offered their most favored customer. PRGI discovered that many vendors may have failed to comply with this contract clause. When we first asserted this apparent indebtedness, many suppliers, and one of their major trade groups, protested. After what we believe was a reasonable period of attempting to resolve these disagreements, DSCP concluded that an overall framework for a settlement with this industry segment could not be achieved. At that point, DSCP moved to formally assert its right to recover these overpayments. To date, we have issued claims amounting to approximately \$10.4 million for most favored customer payment discount terms not offered to us. We have settled

payment discount claims with several contractors and are in the process of resolving the others. However, about \$5.5 million in claims of straight overcharging were placed in abeyance and are being reviewed based on additional information that PRGI has obtained.

#### **ASSESSMENT TO DATE**

Mr. Chairman, since the start of this demonstration program PRGI has identified potential overpayments of about \$27.3 million. Of that, about \$2.6 million has been collected, leaving a potential uncollected balance of \$24.7 million. As I stated earlier, cash discount claims of about \$10.4 million have been approved by the contracting officer and are currently being settled. About \$2 million in disbursing errors have also been approved and are in the process of being collected by DFAS. Potential claims of about \$5.5 million in overcharging are being reviewed by PRGI. Another \$6.8 million in potential overpayments resulting from a variety of reasons, are under review by either the contracting officer or his technical representative and have not yet been approved for collection.

In addition to the numerical data that I just reviewed, this demonstration project has benefited our operation in three ways:

First, recovery auditing has allowed us to continuously encourage vendors to comply with their contract terms and conditions. The additional scrutiny of recovery auditing has provided more assurance that overpayments will be identified and collected promptly.

Second, the auditing process has uncovered several systemic problems, including the need to fine-tune the automated payment systems to assure compliance with all statutory requirements.

Third, disbursing errors uncovered by the auditing program have highlighted the need for closer oversight of the payment function and should result in a reduction of these types of errors in the future.



**FUTURE ACTIONS**

Mr. Chairman, I would now like to discuss our future actions within DLA.

DSCP will serve as the lead supply center within DLA to expand this program to other activities of our Agency. A competitive solicitation to acquire recovery auditing services has been issued with an award anticipated by the end of July. The resulting contracts will require the use of commercial data processing and financial management techniques that are generally used in similar audits of private sector records. In conducting the audits, contractors will be required to compare government contracts, purchase agreements and related documents against invoices submitted by vendors. The purposes of the comparison are to identify and/or describe the following:

- contract compliance regarding costs, price, discounts, billing, etc.
- any overpayments identified
- accounts receivable transaction input for amounts overpaid (accounts reconciliation)
- generation of statement letters relating to vendors' accounts with the DLA.
- summary reports of transactions reviewed and overpayments identified by category
- analyses of overpayments to identify systemic problems or patterns of errors

The annual audit base under this expansion is approximately \$9.6 billion, divided as follows:

- Defense Supply Center Philadelphia (includes the Defense Industrial Supply Center) <sup>1</sup>	\$4.0 billion
- Defense Supply Center Columbus	\$1.8 billion
- Defense Supply Center Richmond	\$0.8 billion
- Defense Energy Support Center	\$3.0 billion

The program is self-funding; that is, the audit contractors' fees will be paid from amounts recovered.

<sup>1</sup> The Defense Industrial Supply Center (DISC) will be disestablished on July 2, 1999, at which time the Defense Supply Center Philadelphia will assume its mission.

**CONCLUSION**

In closing, Mr. Chairman, let me say that this recovery audit program has been successful at DSCP and has become an integral part of our business practices in Philadelphia. I am prepared to answer any questions you may have.

**Defense Supply Center Philadelphia**

700 ROBBINS AVENUE  
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**George H. Allen**  
Deputy Commander

Mr. George H. Allen is the Deputy Commander for the Defense Supply Center Philadelphia. DSCP annually buys over \$4.45 billion worth of food, clothing and textiles, medicines, medical supplies and general and industrial items for America's warfighters and other non-Defense customers worldwide.

Before coming to DSCP, Mr. Allen was the Deputy Commander at the Defense Industrial Supply Center, also located in Philadelphia. Other positions held while at DISC included: Director of Planning and Management Systems, Comptroller and the Director of Planning and Resource Management. While at DISC he also completed a six month tour of duty with DLA Headquarters.

His other federal experience includes: 10 years of service with the General Services Administration in Washington, DC., and the Philadelphia region. He began his career with GSA as a management intern, reaching the position of Regional Budget Officer before joining the DISC team in 1982.

Mr. Allen is a veteran of the U.S. Army with tours in New York and Germany. He is a graduate of Penn State University with a master's in public administration and a bachelor's in political science. He is also an alumnus of the Federal Executive Institute.

In 1984, he was awarded the DLA Meritorious Civilian Service Award and in 1987 was the first DISC employee to receive the DLA Exceptional Civilian Service Award. In 1992, he was named the Federal Women's Program Manager of the Year for making DISC a "family-friendly" place to work. In 1998, he was named as a "Distinguished Member of the Regiment" by the Quarter Master General, U.S. Army. In January 1999, he was inducted in DISC's Hall of Fame.

Active in the Delaware Valley community, he has coached numerous youth baseball, softball and basketball teams. Mr. Allen has also served in a number of positions at the Bensalem United Methodist Church.

Mr. Allen was promoted to the Senior Executive Service in 1993. He and his wife, Robin, are the parents of four children ranging in ages from seven to eighteen.

(Current as of July 1999)

Mr. HORN. Thank you very much, Mr. Allen.

Our next presenter is Gerald R. Peterson, Chief, Accounts Payable Division of the Army and Air Force Exchange Service. Mr. Peterson.

Mr. PETERSON. Mr. Chairman and honorable members of the subcommittee, on behalf of the Army and Air Force Exchange Service [AAFES], thank you for the opportunity to appear before your committee to relate our experience with recovery audits.

Although AAFES has over 25 businesses, our principal business is retail sales. We follow commercial retail best practices to the extent possible. Employing professional audit recovery firms is a best practice we adopted many years ago.

AAFES signed its first contract with a commercial audit recovery firm in 1983. We currently have audit recovery contracts with two firms, a primary and a secondary. Firm A has the primary contract at a rate of 21.75 percent. It recovered \$24.4 million last year. Firm B has the secondary contract with a rate of 35 percent. It recover \$1.1 million last year. In September 1994, AAFES instituted its first in-house recovery effort to detect duplicate payments. The in-house group now recovers missed discounts and outstanding credits on supplier statements in addition to duplicate payments.

We have learned that a successful audit program involves the following. First, partner with both suppliers and audit recovery firms. The relationship with a recovery firm is a partnership in which each provides a benefit to the other. Similarly, suppliers must be viewed with respect to maintain a long-term relationship built upon trust.

Second, develop an in-house recovery program to augment the commercial recovery. During the last 5 years, AAFES' in-house team recovered \$33.3 million at a total cost of approximately \$465,000.

Third, compress the audit cycle. Suppliers know most retailers employ audit recovery firms and getting claims after the fact is a part of doing business. To avoid straining a supplier relationship, it is important to find payment errors in a timely manner. No supplier appreciates having to go back into records that are 4 or 5 years old.

And, fourth, learn from the recovery firm. Review what the commercial recovery firm is finding and determine if it is the result of a systemic flaw in the accounts payable process. It is much cheaper to fix the source of the program or to recover the funds through an in-house group than to pay a commercial firm.

AAFES has greatly benefited from audit recovery services during the last 16 years. And many government agencies could benefit from their services as well. As presently written, however, there are several aspects of H.R. 1827 which will have a negative impact on AAFES.

The first one is the recovery audit requirements. This section states, "The executive agency head may pay the contractor an amount not to exceed 25 percent of the total amount recovered by the executive agency." Twenty-five percent may be acceptable for primary audits, but the fee paid for secondary audits will exceed this amount. If the bill isn't amended to provide higher fees for secondary audits, AAFES will have to cancel its contract with Firm

B and lose the \$700,000 in net earnings that contributed to our bottom last year. So, ideally, AAFES would like to be exempted from this provision.

The second area is disposition of amounts collected. This section states how funds recovered may be used. If amounts recovered aren't applied in accordance with this section, the funds revert to the Treasury. Non-appropriated funds, instrumentalities, NAFEs, should be totally excluded from this section as we generate our own operating funds. The bill should be amended to allow recovered funds to remain within the NAFE, in accordance with its operating rules.

And, third, responsibilities of the Office of Management and Budget. This section sets forth the reporting requirements from the individual agencies. NAFEs should be totally excluded from this reporting requirement, especially entities such as ours. We work continually with our commercial recovery firms to maximize the recovery potential.

For the reasons just mentioned, AAFES requests favorable consideration for the requested changes to the bill.

Mr. Chairman, the Army and Air Force Exchange Service appreciates the opportunity to testify before this subcommittee. The use of audit recovery firms has been a success story for us. The millions of dollars recouped through audit recovery efforts have helped improve the quality of life of our stakeholders; the soldiers and airmen serving around the world. We support your initiative to bring best practices to government agencies. At the appropriate time, I will be happy to answer any questions you might have.

[The prepared statement of Mr. Peterson follows:]

RECORD VERSION

STATEMENT BY

GERALD R. PETERSON

CHIEF, ACCOUNTS PAYABLE DIVISION  
ARMY AND AIR FORCE EXCHANGE SERVICE

BEFORE THE

SUBCOMMITTEE ON GOVERNMENT,  
MANAGEMENT, INFORMATION, AND TECHNOLOGY

OF THE

COMMITTEE ON GOVERNMENT REFORM

HOUSE OF REPRESENTATIVES

FIRST SESSION, 106<sup>TH</sup> CONGRESS

ON THE GOVERNMENT WASTE CORRECTIONS ACT

(H.R. 1827)

29 JUNE 1999

NOT FOR PUBLICATION  
UNTIL RELEASED BY  
THE GOVERNMENT  
REFORM COMMITTEE

**Biography of Gerald R. Peterson**

**Gerald Ray Peterson began his Army and Air Force Exchange Service (AAFES) career in June 1969, as a Retail College Trainee. He worked in the retail career field from 1969 through February 1979, at Richards-Gebaur Air Force Base in Kansas City, MO; McConnell Air Force Base in Wichita, KS; Fort Jackson, SC; and, Fort Leavenworth, KS. In February, 1979, Mr. Peterson became a Field Financial Specialist in the Comptroller career area for the Ohio Valley Exchange Region in Charleston, Indiana of AAFES. Mr. Peterson assumed the responsibilities of an area Accounting Operations Specialist in Colorado Springs, CO, from January 1981 until April, 1983. Mr. Peterson was transferred to the AAFES Headquarters in Dallas, TX in 1983 where he worked in the Fiscal Policies, Procedures, and System Development Division for 10 years, eventually becoming the Chief of the Division. In January 1994, Mr. Peterson was selected head to the General Accounting Division. Mr. Peterson also lead the Payroll Division before assuming his current position of Chief, Accounts Payable Division in August 1997.**

**Mr. Peterson has a B.S. in Economics (with minor in Mathematics) from South Dakota State University. He is married with two children.**

Mr. Chairman, and Honorable members of the Subcommittee, on behalf of the Army and Air Force Exchange Service (AAFES), thank you for the opportunity to relate our sixteen year experience with recovery auditing. Although AAFES has over 25 businesses, our principal business is retail sales through shopping centers, convenience stores, troop stores, Military Clothing Sales Stores, and Class Six stores. Accordingly, AAFES approaches many issues from the perspective of a large commercial retailer. We follow commercial retail "best practices" to the maximum extent possible. Employing professional audit recovery firms is a best practice we adopted sixteen years ago.

#### History Of Audit Recovery Within AAFES

AAFES signed its first contract with a commercial audit recovery firm in 1983. While we had computers back then, much of the work of detecting duplicate payments, lost discounts, missed rebates and other errors was through manual effort on the part of the recovery firm. The fee paid under that first contract was approximately 35-40%. AAFES used a number of firms before signing with its current contractor in 1991. The initial fee of 30% included furnished office space at AAFES. The contract service, when re-solicited in 1996, was again awarded to contractor 'A' at a lower fee of 21.75 %, including office space. The fee percentage continues to decrease due to both industry competition and computer advances within AAFES. With Electronic Data Interchange (EDI) invoicing and AAFES' new imaging systems, recovery firms can examine more information faster than ever before. Last year, contractor 'A' recovered \$24.4 million for AAFES. The attached chart breaks down recovery performance for the last five (5) years, by type of payment error.

In September 1994, AAFES instituted its first in-house recovery effort assigning a staff of two to detect duplicate payments. The in-house recovery unit began monitoring payments for missed discounts using programs written by internal auditors. The staff was expanded in 1997 and now includes a third associate who



reviews supplier statements for outstanding credits. Last year, the in-house team recovered \$7.8 million.

In February 1998, AAFES added contractor 'B' to perform a secondary commercial recovery audit. Having two recovery firms is quite common in the retail industry. The secondary firm serves as a check and balance on the primary recovery firm and also provides an incentive for the primary firm to excel. The fee paid to the secondary recovery firm is a higher percentage than that paid the primary contractor, because of the difficulty involved. Despite a lengthy initial learning curve contractor 'B' recovered \$1.1 million last year. We expect the figure to rise as the new recovery firm learns more about AAFES.

#### Keys To Success

We have learned that a successful audit recovery program includes the following:

- **Partner with both suppliers and audit recovery firm(s).** The relationship with a recovery firm is a partnership in which each provides a benefit for the other. Many view the percentage paid to recovery firms as wasted money—this is only true if payment errors aren't made in the first place. Similarly, suppliers must be viewed with respect to maintain a long-term relationship built upon trust. Although there are exceptions, most suppliers treat their customers the same way—they don't knowingly overcharge a customer. Commercial recovery firms interact with their client's suppliers as aggressively as the client wishes. In the commercial retail environment, there are large companies that are very demanding and aggressive in supplier relations, while smaller retailers are generally more accommodating and willing to negotiate differences. AAFES has historically been between the two extremes. As a large retailer, with more clout than we sometimes realize, we endeavor to approach recovery disputes with fairness.

- **Develop an in-house recovery program.** In addition to the commercial recovery audit contractors, the development of an in-house recovery team is

complementary and cost effective. Most large retailers have a small in-house staff that identifies errors and recoups duplicate payments and/or missed discounts. Over the last five years, the AAFES team has recovered \$33.8 million. Finding these errors in-house increased earnings by \$8.8 million, the amount we would have paid in fees. These earnings provided an additional \$5.9 million for MWR dividends to support the quality of life of our stakeholders, the men and women in the Army and the Air Force. Personnel costs associated with in-house recovery approximated \$465,000, for the five year period. However, an in-house team can't take the place of a commercial recovery firm. Specialized techniques and systems development is costly for an individual company. AAFES contracts with the same audit recovery firm as Wal-Mart, K-Mart, Sears, Walgreen, and many other retailers. Although contractor 'A' can't share proprietary information, it does have information on deal packages and rebates not available to a single in-house recovery unit. It's important to look at more than the fee when choosing an audit recovery firm—it's equally important to look at the size of audit recovery company's client base within an industry and ask for recommendations from other clients.

- Compress the audit cycle. Suppliers know that most commercial businesses employ audit recovery firms and that after-the-fact claims are part of doing business. However, it's important to process and find payment errors in a timely manner or strain supplier relations. Before AAFES contracted with contractor 'B' in February 1998, four year old records were being audited. We learned that no supplier can afford to go back four or five years. To maintain effective supplier partnerships, audit completion is required no more than 30 months after the payment date.

- Centralize operations where possible. AAFES has the information systems capability to store procurement, receiving, and payment records centrally. This makes the audit recovery process more manageable and less costly.

- Optimize the use of technology. The EDI (Electronic Data Interchange) processes invoices and payment with little or no human intervention. Digital invoice

data is transmitted to audit recovery firms for detail analysis. In the last two years, contractor 'A' has recovered \$11.7 million in 'Overcharges' a category that previously yielded very little due to the expense involved in collection and analysis. In 1996, AAFES installed an imaging and workflow system which eliminated a heavily manual "internal paper mill" and streamlined the payment process. Far more functional than originally conceived, the system received nationwide recognition when it was nominated by William Gates, Chairman of Microsoft, for the Smithsonian Computerworld Award in 1998. In April 1999, the application received the 'Windows World Award' for workflow applications over Intel and Deloitte & Touche. AAFES is working with contractor 'A' on CD-ROM imaging of paper invoices. NOTE: Large retailers receive virtually 100% of invoices via EDI requiring electronic transmission as a contractual requirement of doing business. As AAFES receives 58% of total invoices via EDI, transferring images to CD-ROM is the only way to identify and recover unit cost discrepancies on 42% of the bills received. Federal procurement guidelines relating to small and minority businesses and our quasi-governmental status preclude AAFES from mandating EDI. Unless or until all suppliers have EDI capability, the accounts payable function will be less efficient than that of other large retailers and the audit recovery fees will be higher.

- Learn from audit recovery firms. Quarterly status reports are provided by the audit recovery contractors. These reports show the types of claims processed and the suppliers charged. Through an analysis of these reports, in-house recovery teams can learn new methods and techniques which when implemented, yield cost savings and, in turn, challenge audit recovery firms to look for other ways to recoup funds.

Mr. Chairman, the Army and Air Force Exchange Service appreciates the opportunity to testify before this sub-committee. The use of audit recovery firms has been a success story for us. The millions of dollars recouped through audit recovery efforts have helped improve the quality of life of our stakeholders, soldiers and airmen serving around the world.

**We support your initiative to bring “best practices” to government agencies. I shall be happy to answer any questions you may have.**

**RECOVERIES BY MAJOR CATEGORY**  
(S in Millions)

Primary—Contractor A

<u>Category</u>	<u>JUN 1999</u>	<u>JUN 1998</u>	<u>JUN 1997</u>	<u>JUN 1996</u>	<u>JUN 1995</u>	<u>JUN 1994</u>
ALLOWANCES	\$ 9.4	\$ 6.8	\$ 6.0	\$ 10.4	\$ 5.1	\$ 5.4
DUPLICATES	2.2	1.1	0.4	0.8	1.4	2.1
STATEMENT/CM	3.1	2.1	1.7	1.6	1.3	1.2
CO-OP	1.8					1.1
OVERCHARGES	5.9	5.2	0.7	0.4	0.4	0.5
DISCOUNTS	1.3	0.8	0.7	3.1	1.7	0.4
ANTICIPATION			0.1	0.2	0.5	0.4
FREIGHT	0.7	2.3	0.9	1.7	1.3	0.3
PRICE PROTECTION						0.2
OTHER					0.2	0.1
TOTAL	24.4	18.3	10.5	18.2	11.9	11.7

AAFES—In-House

<u>Category</u>	<u>JUN 1999</u>	<u>JUN 1998</u>	<u>JUN 1997</u>	<u>JUN 1996</u>	<u>JUN 1995</u>	<u>JUN 1994</u>
DUPLICATES	1.3	3.4	6.1	2.7	10.8	
DISCOUNTS	1.2	1.4	0.7			
STATEMENT/CM	5.3	0.9				
TOTAL	7.8	5.7	6.8	2.7	10.8	

Secondary—Contractor B

<u>Category</u>	<u>JUN 1999</u>	<u>JUN 1998</u>	<u>JUN 1997</u>	<u>JUN 1996</u>	<u>JUN 1995</u>	<u>JUN 1994</u>
ALLOWANCES	0.1					
DUPLICATES	0.5					
DISCOUNTS	0.4					
OTHER	0.1					
TOTAL	1.1					
GRAND TOTAL	\$ 33.3	\$ 24.0	\$ 17.3	\$ 20.9	\$ 22.7	\$ 11.7

Mr. HORN. Thank you very much.

The next presenter has one of the toughest jobs in the U.S. Government, and that is Ms. Snyder, being the Chief Financial Officer for the Health Care Financing Administration. Welcome.

Ms. SNYDER. Thank you, Mr. Horn. I have been CFO now for 4 months and I am beginning to appreciate just how difficult this job is.

Chairman Horn and distinguished subcommittee members, thank you for inviting us to testify about the Government Waste Corrections Act and our extensive efforts to prevent and recoup improper payment. As you know, we reduced Medicare's payment error rate from 14 percent to 7 percent in just 2 years. We are working diligently to build on this success and we are very grateful for this subcommittee's support in these efforts.

We have had good success with the kind of recovery audit efforts described in the proposed legislation. And we believe that they may well have value for other government agencies as well.

We, of course, have pursued a different kind of strategy in addition to recovery audit efforts. And that is to prevent improper payments from occurring in the first place. We are making solid progress on that front, in large part due to increased efforts by providers to document and file claims correctly. We also use nearly 100,000 computerized edits that detect and automatically deny payment for improper claims as well as manual medical record reviews and cost report audits. We are making solid progress in identifying and collecting overpayments as well.

As you know, the HHS Inspector General audits have found that most Medicare claims are correct on their face. Finding most of our remaining payment errors requires going beyond what is on the claim to look at documentation and medical necessity. These activities are now primarily performed by our claims processing contractors. We recently held an open competition to establish a pool of new program safeguard contractors to augment these efforts. And the President is proposing legislation to further increase competition for Medicare work among qualified entities.

However, the act's authorization to compensate recovery auditors on a contingency basis may have only limited value for Medicare. We recoup most overpayments by making deductions from future payments to providers who have been overpaid. And paying on a contingency basis for error identification could be perceived as a bounty system by health care providers. The vast majority of Medicare providers, we have found, make only honest errors and their good will and cooperation are key to much of our success in preventing improper payment in the first place.

Furthermore, a financial incentive to identify errors could well lead to inappropriate denials and thus create errors instead. Our obligation is to pay correctly. And we do not want to deny proper payment any more than we want to make improper payment. Inappropriate denials resulting from contingency payment also could backfire on the bottom line due to increased costs for appeals filed by beneficiaries and providers denied proper payment. So while we would be willing to consider use of the contingency fee option, we would need to take extreme caution in ensuring that any use of it would, indeed, be constructive.

We also generally endorse the idea of increasing funding for program management improvement activities that could reduce overpayment. We have greatly benefited from the stable source of program for program integrity activities provided to us under the Health Insurance Portability and Accountability Act, which totaled \$560 million in fiscal year 1999 and \$630 million in fiscal year 2000. However, we generally believe that recouped overpayments should be returned to the trust fund or general revenue fund as is now the case.

I would also just like to take a few seconds to address the remarks made by Mr. Burton earlier. I have not seen the article to which he refers about the returned checks, but I would like to assure this subcommittee that we have instructed our fiscal intermediaries and carriers to cash checks that are returned and to properly credit them to the Medicare account.

We have had some experiences in the past where people returning checks wanted us to say that, in cashing the check, that satisfied their full liability, which we have not, of course, been willing to do. And our instruction has been we will cash the check and make it clear that this does not necessarily release them of their liability until further investigation might be completed. But we would be very happy to work with Mr. Burton's staff to make sure that we are responsive, indeed, to the article that he mentioned.

We also look forward to continuing to work with the subcommittee on efforts to improve Medicare program integrity. I thank you for holding the hearing. And would be happy to answer any questions you might have.

[The prepared statement of Ms. Snyder follows:]

**TESTIMONY of  
MICHELLE SNYDER, CHIEF FINANCIAL OFFICER  
HEALTH CARE FINANCING ADMINISTRATION  
on the  
"GOVERNMENT WASTE CORRECTIONS ACT"  
before the  
HOUSE GOVERNMENT REFORM  
MANAGEMENT, INFORMATION, & TECHNOLOGY SUBCOMMITTEE**

Chairman Horn, Congressman Turner, distinguished Subcommittee members, thank you for inviting us to testify about the Government Waste Corrections Act and our extensive efforts to prevent and recoup improper payments. As you know, we reduced Medicare's payment error rate from 14 percent to 7 percent in just two years, and we continue to work diligently to build upon this success. We are very grateful for this Subcommittee's support in these efforts.

We have had good success with efforts similar to the recovery audits described in the proposed legislation. Of course, we prefer to prevent improper payments from occurring in the first place. We are making solid progress on that front, in large part due to increased efforts by providers to document and file claims correctly. We also use nearly 100,000 computerized "edits" that detect and automatically deny payment for improper claims, as well as manual medical record reviews and cost report audits. Our success with such efforts strongly suggests that they may have value for other government agencies.

We are making solid progress in identifying and collecting overpayments as well. As you know, the HHS Inspector General's CFO audits have found that the vast majority of Medicare claims paid by our contractors are correct on their surface. Finding most payment errors requires going beyond what's on the claim to look at the documentation behind the claim and its medical necessity. These activities are now primarily performed by our claims processing contractors. We recently held an open competition to establish a pool of new Program Safeguard Contractors to augment these efforts, and the President is proposing legislation to further increase competition among Medicare contractors.

The Act's authorization to compensate recovery auditors on a contingency basis may have



appropriate uses in some circumstances, as the Department of Defense experience may suggest. It may have value for Medicare in the limited situations where we are unable to collect from providers. However, most overpayments are now recouped by making deductions from future payments to providers who have been overpaid.

We also do not believe contingency payment is necessary, or necessarily prudent, for identification of Medicare payment errors. As mentioned above, we have made solid progress identifying payment errors under existing contractor arrangements. More importantly, paying on a contingency basis for error identification could be perceived pejoratively as a "bounty system" by health care providers. Providers have raised such concern about even the very modest reward available to beneficiaries who uncover fraud under the Health Insurance Portability and Accountability Act. The vast majority of Medicare providers make only honest errors, and their good will and cooperation are key to much of our success in preventing improper payments in the first place.

Furthermore, a financial incentive to identify errors could well lead to inappropriate denials and thus create errors, instead. Our obligation is to pay correctly, and we do not want to deny proper payment any more than we want to make improper payment. Inappropriate denials resulting from contingency contracts also could backfire on the bottom line due to increased costs for appeals filed by beneficiaries and providers denied proper payment.

We also believe that all recouped overpayments made from the Medicare Trust Funds should be returned to the Trust Funds or general revenue funds, as is the case now. This will ensure that Medicare can continue to pay for necessary health care for our beneficiaries, and is consistent with the fraud and abuse control program created under the Health Insurance Portability and Accountability Act.

**Background**

Since the Clinton Administration took office, the Department of Health and Human Services has

taken numerous steps to stop fraud, waste, and abuse. Achieving this goal is one of our top priorities at HCFA. With help from Congress, providers, beneficiaries, and our many other partners, we have achieved record success in assuring proper payments and recouping improper payments.

Obviously, the most cost effective way to collect overpayments is to not make them in the first place. We have had great success by cooperating with providers to help them document and file claims properly to prevent improper payments. Documentation errors had been the single largest factor in our error rate, but have declined by almost 80 percent from fiscal 1996 to fiscal 1998. They now account for only about 17 percent of improper payments.

That is why our Comprehensive Plan for Program Integrity features increased efforts to educate providers about how to properly document and file claims. Most providers who make billing errors have no intent to do anything wrong, but simply make honest mistakes, and we want to ensure that providers understand our coding and documentation rules. We are therefore taking nationwide a highly successful provider education pilot project conducted last year in 13 States. It includes:

- ▶ seminars on how to document and file claims that we have broadcast via satellite to thousands of providers and their billing agents;
- ▶ special training to help medical residents set up their practices to bill Medicare correctly;
- ▶ a special duplicate claims reduction program; and
- ▶ training modules on the Internet at [www.medicaretraining.com](http://www.medicaretraining.com) that any individual with Medicare billing responsibilities can use.

We also are meeting with physicians around the country to explore ways we might be able to make it easier to understand and comply with Medicare rules and regulations. In all these activities, it is essential that we maintain a constructive partnership with providers.

Our Comprehensive Plan also features efforts to increase and improve ongoing activities that parallel the "recovery audits" described in the Act. For example, we are tightening the performance standards and evaluation for contractor medical review efforts, in which physicians

review medical records to ensure that claims are correct. We also are engaging independent contractors to evaluate key medical review processes. Some of these medical reviews are conducted on a random, post-payment basis, and others are focused on providers with aberrant billing patterns.

Other ongoing activities we use to identify overpayments include:

- ▶ auditing of cost reports, which are filed by institutional providers;
- ▶ statistical analysis to identify aberrant billing patterns; and
- ▶ coordination with other insurers to recover any payments Medicare has made that should have been covered by other insurers.

Specialized contractors will assist us with the tasks of statistical analysis and coordination with other insurers. The President also has proposed legislation to require private insurers to share information with us, so that we can more easily identify cases where another insurer owes Medicare.

Ongoing activities to collect overpayments include:

- ▶ issuing demand letters notifying providers of our intent to recoup improper payments;
- ▶ deduction of overpayment amounts from future payments, which is the primary means of recoupment; and
- ▶ referral to the Treasury Department's Debt Collection Center when administrative remedies are exhausted.

We also pursue legal remedies, including civil and criminal prosecutions, to recover funds that providers have obtained through fraudulent acts. The Federal Government won or negotiated more than \$480 million in judgments, settlements, and fines in 1998.

**Conclusion**

We support any legislation that will give government agencies tools to help collect overpayments. However, given the extremely high priority this Administration and our Agency place on fighting fraud, waste, and abuse, it is unlikely that paying for recovery audits as

envisioned in H.R. 1827 would significantly increase our success. We are concerned that contingency fees could have a negative impact on the constructive partnership with providers that is critical to preventing improper payments in the first place.

I thank you again for holding this hearing, and I am happy to answer any questions you might have.

# # #

Mr. HORN. We thank you.

And I am now going to yield to the time for questioning to Mr. Ose, the gentleman from California.

Mr. OSE. Thank you, Mr. Chairman. I am going to work as procedurally as I can here. Ms. Lee, on your statement here the 5-year plan will be transmitted to Congress soon?

Ms. LEE. Yes, sir. It is in final sign-off.

Mr. OSE. When can we expect it? I mean, is soon next week, next month, what is it?

Ms. LEE. I was hoping next week, but let us say when you get back from recess.

Mr. OSE. August? Or Fourth of July?

Ms. LEE. In July.

Mr. OSE. OK. Now, secondarily, you talked about, under the National Defense Authorization Act. In a pilot study four-tenths of 1 percent of the payments sampled were incorrect. The pilot study must have used a sample. Again, Ms. Lee, there must have been a sample size or something that you looked at. It is on page 2 of your testimony at the bottom. I am wondering about the sample size.

Ms. LEE. Can I get that for you, for the record?

Mr. OSE. Certainly. That would be fine.

Mr. HORN. Without objection, the response of the Deputy Director for Management will be put in the record at this point.

[The information referred to follows:]

I have confirmed with the Department of Defense and the contractor that the pilot covered \$7.2 billion in payments from 1993, 1994 and 1995 made by the Defense Supply Center in Philadelphia.

Mr. OSE. Thank you, Mr. Chairman. And then on page 3, I am a little bit confused about something. On page 2, when we talk about the sample or my question about the sample sizes there is a statement about four-tenths of 1 percent of the payments sampled were incorrect, which is remarkable. And then when the discussion gets to the issue of the threshold, the \$10 million threshold, there is a comment about the threshold of \$10 million would result in a gross collection of \$10,000 under this bill if a overpayment was found. That is one-tenth of 1 percent, if I understand.

Ms. LEE. That is the industry standard, as we understand it.

Mr. OSE. In private industry.

Ms. LEE. In private industry.

Mr. OSE. OK. That is not bad either.

And then, finally, in the last page of your testimony, when you talked about the provisions in the middle of your—right above conclusion—“The bill would allow agencies to return up to 25 percent of collections to programs and activities from which the overpayment arose. These provisions could be used to bypass the normal Congressional Appropriations process.” I am not quite sure I understood your explanation.

Ms. LEE. We would propose that we structure the bill to make sure that when we returned those moneys to a program, it was, in fact, Congress' intent to spend the funds. For example, sometimes we recover after a period of time and if the program has been eliminated or is completed or finished, we want to make sure the

moneys go back where you originally intended the moneys to be spent.

Mr. OSE. The flaw being that if a program is terminated, there is no point in returning the money back to it.

Ms. LEE. To that program, right.

Mr. OSE. If the program is continuing, you would not have an objection to returning the money to that program.

Ms. LEE. Correct.

Mr. OSE. OK. Thank you.

I have got more questions.

Mr. HORN. Yes. Go ahead.

Mr. OSE. OK. Let us see. Mr. Allen, on page 3 of your testimony, the fourth paragraph, you talked about DSCP's recoveries to date being \$2 million. That is for audit work begun in June 1997. And what I am curious about is I don't see much point in spending \$5 million if you only recover \$2 million. My question would be the cost of recovering the \$2 million is roughly—

Mr. ALLEN. By the contract we have with PRGI, we pay them I believe it is 20 percent of whatever we collect.

Mr. OSE. OK.

Mr. ALLEN. We have up to \$5 million under that initial legislative proposal to pay them, at a rate of 20 percent of whatever we collect.

Mr. OSE. So, potentially, in anticipation of finding \$25 million in overpayment, you are authorized to spend up to \$5 million?

Mr. ALLEN. That is correct.

Mr. OSE. These aren't my words, as a bounty?

Mr. ALLEN. That is correct.

Mr. OSE. OK. Thank you.

Mr. ALLEN. The subsequent legislation authorizes us to pay from the proceeds, that is, from the amounts collected.

Mr. OSE. At the outset, there was an appropriation to pay the reward?

Mr. ALLEN. That is correct.

Mr. OSE. OK.

Now, Mr. Peterson, I got the first two points on AAFES's request for exemption. Those being the threshold on the secondary audits and the reversion to Treasury of the recovered funds. But you lost me on the third one. You had three points there that you were seeking an exemption under this legislation for.

Mr. PETERSON. Yes. Since our program has been undergoing for 16 years, we feel that we have already demonstrated that we are following industry best practices in that we are working continually with our recovery firms to bring best practices to bear. And so for that reason, we don't feel that we should be reporting back to the OMB.

Mr. OSE. Is it your rationale that as this is essentially self-funded—

Mr. PETERSON. Yes.

Mr. OSE [continuing]. That these funds should stay in AAFES's jurisdiction?

Mr. PETERSON. That is correct. We are a non-appropriated fund instrumentality. We generate our own revenues through our sales.

Mr. OSE. All right. On the methodology that you used for contractor A in your example and contractor B, I would presume—and maybe that is not safe to presume and you can correct me if it is appropriate, certainly—the methodologies at the outset that contractor A used generated  $X$  amount of recoveries. And the secondary audit firm, contractor B, used a slightly different methodology, I presume, that generated around, your example, \$1.1 million.

Mr. PETERSON. Yes. We have only had the secondary audit for a little over 1 year.

Mr. OSE. Well, my question really is when you have contractor B who uses a slightly different methodology than contractor A, over time do those two methodologies get merged so that we are continually improving the larger portion, if you will, of the audit work? That being, we merge methodology A and B in the subsequent or successive contract?

Mr. PETERSON. Sir, the two firms don't really get together as far as how they perform their audits. And I don't know that they use different techniques. I believe that the secondary firm probably is quite familiar with the primary and looks for areas where the primary has thought it wasn't beneficial to look. The secondary has a higher recovery rate, you know, 35 percent versus 21 percent, so they can afford to perhaps delve into some areas that may not have been efficient or economical for the primary to do.

Mr. OSE. My point is, as Congress looks out into the future and considers these challenges, not in this round of audit awards, if you will, but maybe the next round, is there any rationale for us thinking that, on an RFP or RFQ or whatever it is we use to enter into these contracts, that we would merge the methodologies?

Mr. PETERSON. Well, I don't know that those are different methodologies, Congressman.

Mr. OSE. OK. You think the added result might be attributable to the 13.25 percent extra in the bounty, if you will?

Mr. PETERSON. It is that and then just looking for areas—they may approach something—use a little different computer program than the first one used that might detect something that the first one missed.

Mr. OSE. All right. Finally—let me make sure that is finally—on page 5, I think you touched on something that is very important to business people and that is the reach-back, if you will, 4 or 5 years. I can't imagine somebody coming into my affairs and asking me to substantiate something that happened in 1994. I see that the audit competition and target would be 30 months. Is there any possibility of even compressing that further?

Mr. PETERSON. Not within our industry. We approach things from the viewpoint of a commercial retailer, rather than that of a government agency because that is our primary business is retailing.

Mr. OSE. Right.

Mr. PETERSON. And many of the items that our audit recovery tracks are year-to-date purchases and so to compress an internal review cycle, a primary and a secondary, into much less than 30 months would really be pressing the audit companies.

Mr. OSE. Is the 30 months an industry standard? Or is that just what you have come to as fitting the—

Mr. PETERSON. That is what we have come to.

Mr. OSE. OK.

Mr. PETERSON. That is our goal.

Mr. OSE. Do we support—or to what degree are we providing resources to outside firms to do these audits? In other words, we have got a certain clerical staff. Are we, in effect, providing support staff for audit firms? Or is this a totally arms-length, third-party transaction where they come into AAFES. We are not providing or AAFES isn't providing or some of these other agencies isn't providing committed staff to support the audit done by a third party?

Mr. PETERSON. OK. We provide no people. We do provide space in our facility for them and we provide access to our computerized records.

Mr. OSE. All right. Finally—Mr. Chairman, you are being very patient with me and I appreciate that.

Mr. HORN. We have all afternoon, my friend.

Mr. OSE. Oh, lordy, lordy. [Laughter.]

I appreciate HCFA being—

Mr. HORN. No, no. Forget the bells. [Laughter.]

That is to keep us alert. [Laughter.]

Mr. OSE. I appreciate the opportunity to visit with Ms. Snyder. The reason I do is that Medicare remains one of the largest programs we have and 14 percent, 7 percent, 5 percent of Medicare's number is a huge number. Which begs the question—and you are going to have to take me through it—you have got the payment error rate down in 2 years from 14 to 7 percent. The other testimony we have heard indicates somewhat less than that in a payment error rate. Is it possible to get to the payment error rate that these other agencies are experiencing by their samples? And what is the relationship between getting to it and the cost we are likely to incur?

Ms. SNYDER. When we first started out trying to drive down the payment error rate, it was based off of a statistically valid sample and an extrapolation, if you will, of the error rate and the dollar amount established by the IG. And we have continued to use that methodology to try to measure what the error rate is for Medicare payments. And I would also like to point out that that is a measure of error. It is not a measure of fraud or abuse.

Mr. OSE. I understand. I understand.

Ms. SNYDER. It is just a measure of our total due to error.

Mr. OSE. Believe me, I know. I have had lots of constituents come in and talk to me about this.

Ms. SNYDER. OK. What we have found is we do believe that we can drive the error rate lower, since we have had such good success in the last 2 years. A large part of the dollars that we use for that came out of the MIP program, the Medicare Integrity Program, which was authorized under HIPPA. So we fully expect to spend those dollars on continuing to drive down the error rate. And that dollar amount does increase from year to year. We were at \$560 million this year and it eventually increases to \$720 million.

I am cautiously optimistic that we can drive the error rate much lower than 7 percent. I think the fact that in 2 years we have seen good results from our corrective action plans and corrective activi-



ties that we have undertaken will help us reduce that even lower. And our goal is to get to 5 percent.

We do recognize that in a program this large, there will always be some error. We don't know yet where that bottom line is or what that bottom line percentage is. Right now, as I said, we are pushing to get to 5 percent and then to evaluate where we can go from there. Again, I would like to point out that it is sort of like the old—if you will allow me—the diet analogy. That first 10 pounds is easy to lose. It is that last 5 that is the killer. And we are starting to move into that last 5 pound range.

So I do believe we can drive it lower. I believe that the funds that are available to us through the MIP program will help with that. The return on investment for all of our program integrity activities is 15 to 1, so we still have a good return on investment. So I am cautiously optimistic.

Mr. OSE. So the 7 percent, again, is the rate at which we are able to identify the errors. And then, in terms of recovery, you are suggesting a 15 to 1 pay-back in terms of the cost that HCFA incurs in doing the identification. But how much or what is the—I don't even know what the—

Ms. SNYDER. The recovery.

Mr. OSE. Yes. The recovery rate. Thank you.

Ms. SNYDER. It would be the recovery. Right. OK.

Mr. OSE. It's my bill and I don't even know the darned phrase.

[Laughter.]

Ms. SNYDER. We believe that we are going to recover the bulk of those overpayments. And, in fact, again, if you will remember, this is an extrapolated sample, if we look at our yearly activity and we look at our accounts receivable and look behind that, which may be a better place to look in terms of recoveries, what we find is that we capture back approximately \$12 billion to \$13 billion annually through offsetting collections and other receipts. And, of course, many of those dollars never show up. And I can submit the exact dollars to you for the record.

Mr. OSE. I think that would be helpful, Mr. Chairman.

Mr. HORN. Without objection, it will be put in the record at this point.

[The information referred to follows:]

The dollar amounts are: 1) new receivables for FY 1998 total \$15.4 billion; collections on receivables total \$12.6 billion; and, 3) the amount which is offset is \$7.7 billion.

Mr. OSE. My final inquiry is, Ms. Lee, Mr. Allen, and Mr. Peterson, if I understand correctly, you have third parties coming in and doing the audits in your agencies. And they are doing it for a fee that is negotiated and, if the pattern as identified by Mr. Peterson is correct, basically all we are providing is a desk and a phone and they bring their own personnel in and do the analysis. Is that correct?

Mr. ALLEN. That might be more true in AAFES, who has 16 years of experience in doing that. In case of us, within DOD, there is a little bit more effort than that, for a wide variety of reasons. Again, we are in a pilot program in DOD. We have not compressed our audit cycle. We are dealing with auditing contracts that are,

in some cases, 4 years old. We have to go find that documentation. There is some effort associated with that.

We have the Defense Finance Accounting Service in Columbus, OH, who makes the payments for us. They have records. They have to provide those records and they have to go through some effort to make the records available to the auditing firm for the audit. So I would say, initially, there is probably a lot more work, effort, in starting up an internal government effort to make records available to an outside auditing firm, but over time, one of the systemic things we would learn is we would be able to figure out how to get that effort down to next to nothing. And we might, then, in 16 years or in some period of time be somewhere close to where AAFES is.

Mr. OSE. Let me introduce you to Mr. Peterson. He has got a model, I think, we ought to make—

Mr. ALLEN. Well, absolutely. We benchmarked with AAFES when we started out the program and you are absolutely right. And we are doing the same thing with some other agencies today.

Mr. OSE. Ms. Lee, is that consistent with your experience?

Ms. LEE. We at OMB don't employ the auditors, but it certainly sounds very logical. And, of course, the specific contract terms and conditions are things that you would want the auditors to have access to to make sure that they have the right baseline.

Mr. OSE. It is timely, Mr. Chairman, that we have these discussions since we are struggling with our appropriations and, granted, we are going to deal with it, but I daresay that if you were able to take Mr. Peterson's model, for instance, and apply it to Ms. Snyder's organization and reduce not only the identification rate, but increase the recovery rate to reflect AAFES's, we would have substantially greater resources to commit to serving the people of this country and that is the underlying purpose of this bill.

While I very much appreciate the gaps that we have not addressed, in terms of recovery and, if you will, the entitlement nature of some of your organizations, you know, we are going to try and fix this, subject to your testimony, and we are going to go forward. And I appreciate the opportunity to visit with you today. So, thank you. Thank you, Mr. Chairman.

Mr. HORN. The gentleman is absolutely correct on the impact that it would make in a program such as Medicare. The gentleman from Oregon, Mr. Walden.

Mr. WALDEN. Thank you, Mr. Chairman. I had a question for Ms. Snyder, I guess. Reading through your testimony, on page 3 you talked about how most providers who make billing errors have no intent to do anything wrong, simply make honest mistakes, which I would tend to agree with.

I guess what troubles me, having served 5 years on a community hospital board, I have seen the letters come out from the Department of Justice that allege just the opposite. And I believe it is the Fraudulent Claims Act that is invoked by the Justice Department on behalf of your agency, chasing claims that go back 8 or 9 years in some cases. Are you still using those tactics?

Ms. SNYDER. What we have tried to do, also, as part of our program integrity strategic plan, is to work to have more of a partnership with our providers, because we recognize some of the same

concerns that you just raised. And we think that is partly why we have been so successful in pushing down the error rate. But through provider education, making sure that people understand the right way to bill, what the requirements are, what the right codes are, that, indeed, they are paid correctly, then, from the beginning. We still use the False Claims Act when it is appropriate. But I believe that it is more of a partnership effort, these days, to try to make sure we are paying claims correctly.

Mr. WALDEN. So I guess I—

Mr. HORN. If you could move the microphone a little closer to you, Ms. Snyder.

Mr. WALDEN. So I guess I would say, Ms. Snyder, is, again, I have met with a lot of people and I represent a district with lots of small rural hospitals and all and reading those letters are extraordinarily intimidating. They say you either admit that you—on what is I think you have correctly recognized here probably a simple honest mistake, but they are being told either admit to false claims and fraud or we are going to come do major damage to your bottom line, taking a \$2,000 error in billing and turn it into a \$100,000 issue. And I thought it was overkill and I thought if I ever got in a position where I could say that, I would. Well, here I am. [Laughter.]

And I guess—

Ms. SNYDER. And I certainly appreciate your guidance, sir.

Mr. WALDEN. I also wanted to be in a position to say, in reverse, however—I am a bit off-topic here, but I think, because we are going to be putting pressure on you to go do this and, yet, there is this balance. And I always wondered how often does Medicare make payment errors on the other way? And, you know, what if the Fraudulent Claims False Claims Act was used in reverse? What is good for the goose ought to be good for the gander. And I am glad to see that you are kind of taking this a different direction.

Not to say there isn't fraud out there. I realize there is.

Ms. SNYDER. I would just like to mention that the Department of Justice just recently issued new guidelines to try to take care of that overkill problem that you reference.

Mr. WALDEN. Good.

Mr. HORN. Can you get us those regulations?

Ms. SNYDER. Certainly.

Mr. HORN. We will save a part at this point in the record, without objection, so they are spread out in this document.

[The information referred to follows:]

A copy of the Department of Justice's guidelines is provided here as an attachment to the transcript.



## U.S. Department of Justice

Executive Office for United States Attorneys

Office of the Director


Room 2244A, Main Justice Building  
550 Pennsylvania Avenue, N.W.  
Washington, D.C. 20530

(202) 514-2121

DEC - 8 1998

MEMORANDUM - Sent via Broadcast Fax

TO: ALL UNITED STATES ATTORNEYS  
ALL FIRST ASSISTANT UNITED STATES ATTORNEYS  
ALL CIVIL CHIEFS  
ALL CIVIL HEALTH CARE FRAUD COORDINATORS  
ALL AFFIRMATIVE CIVIL ENFORCEMENT COORDINATORS

  
FROM: Donna A. Bucella  
Director

SUBJECT: Compliance with Guidance on the Use of the  
False Claims Act in Civil Health Care Matters

ACTION REQUIRED: Distribute the Attached Memorandum to all  
Assistant United States Attorneys Handling  
Civil Health Care Matters

CONTACT PERSON: Robert Liles  
Health Care Fraud Coordinator  
Legal Programs  
Phone: (202) 616-6444  
E-mail: aex12.pc.rliles

On June 3, 1998, the Deputy Attorney General issued a Guidance Memorandum to all Department attorneys handling civil health care matters regarding use of the False Claims Act in civil health care matters. The Guidance Memorandum emphasizes the importance of pursuing civil False Claims Act cases against health care providers in a fair and even-handed manner, and implements new procedures with respect to the development and implementation of national initiatives. Additional instruction, stressing the need for compliance with the Guidance Memorandum was issued by the Deputy Attorney General on December 4, 1998. A

copy of that memorandum is attached.

Please ensure that all Assistant United States Attorneys handling civil health care matters receive a copy of the attached memorandum. Should you have any questions regarding the guidance issued on use of the False Claims Act in civil health care matters, please contact Robert Liles at the number above.

Attachment



U.S. Department of Justice


Office of the Deputy Attorney General

The Deputy Attorney General

Washington, D.C. 20530

December 4, 1998

MEMORANDUM FOR: All United States Attorneys  
 All First Assistant United States Attorneys  
 All Civil Health Care Fraud Coordinators in  
 the Offices of United States Attorneys  
 All Trial Attorneys in the Civil Division,  
 Commercial Litigation Section

FROM:  Eric H. Holder, Jr.

SUBJECT: Compliance with Guidance on the Use of the  
 False Claims Act in Civil Health Care Matters

The False Claims Act (FCA) is the Department's most important civil enforcement tool for addressing fraud and abuse against federal health benefits programs. While the broad reach and substantial penalties of the Act make it a powerful anti-fraud tool, all DOJ attorneys must ensure that we use such tools in a fair and even-handed manner. To this end, I issued a Guidance Memorandum on the Use of the Civil False Claims Act in Health Care Matters (June 3, 1998) for use in all pending and future health care fraud cases. The Guidance Memorandum, inter alia, emphasizes the need to develop an adequate factual and legal predicate as to each element under the FCA before contacting a provider about potential FCA liability; establishes new procedures for the development and implementation of national initiatives; and establishes that, as a general matter, contact letters shall be used in national initiatives when contacting providers about their potential liability under the False Claims Act.

It is imperative that all Departmental attorneys comply with the June 3, 1998, Guidance Memorandum. In addition, to facilitate supervisory review, Departmental attorneys are encouraged to document their compliance with the Guidance. Supervisors should consider the use of narrative summaries or other appropriate entries in case files that reflect consideration of the Guidance's principles. Finally, Departmental attorneys should reach out to local, state or national health care provider organizations and others to explain the Guidance Memorandum.


I appreciate your careful attention to these issues. If you have any questions, please contact the EOUSA Health Care Fraud Coordinator, Robert Liles, at (202) 616-5136.



Office of the Deputy Attorney General  
Washington, D.C. 20530

June 1, 1999

MEMORANDUM FOR: All United States Attorneys  
All First Assistant United States Attorneys  
All Civil Health Care Fraud Coordinators in  
the Offices of United States Attorneys  
All Trial Attorneys in the Civil Division,  
Commercial Litigation Section

FROM:  Eric H. Holder, Jr.  
Deputy Attorney General

SUBJECT: Guidance on the Use of the False Claims Act  
in Civil Health Care Matters

One of the Department's most important tools in protecting the integrity of Medicare and other taxpayer-funded health care programs is the civil False Claims Act. While the broad reach and substantial damages and civil penalties under the Act make it one of the Department's most powerful tools, Departmental attorneys are obligated to use their authority under the Act in a fair and responsible manner. This is particularly important in the context of national initiatives, which can have a broad impact on health care providers across the country.

This guidance is being issued to emphasize the importance of pursuing civil False Claims Act cases against health care providers in a fair and even-handed manner, and to implement new procedures with respect to the development and implementation of national initiatives.

1. National Initiatives.

Generally, national initiatives deal with a common wrongful action accomplished in a like manner by multiple, similarly situated health care providers. National initiatives must be handled in a manner (i) that promotes consistent adherence to the Department's policies on enforcement of the False Claims Act, as well as a consistent approach to overarching legal and factual issues, (ii) while avoiding any rigid approach that fails to recognize the particular facts and circumstances of an individual case.

Memorandum from the Deputy Attorney General  
 Subject: Guidance on the Use of the False Claims Act in Civil  
 Health Care Fraud Matters

To achieve these objectives, the Department has instituted the following procedures:

(A) Legal and Factual Predicates.

Before alleging violations of the False Claims Act, whether in connection with a national initiative or otherwise, Department attorneys must evaluate whether the provider: (i) submitted false claims to the government, and (ii) submitted false claims (or any false statements made to get the false claims paid) with "knowledge" of their falsity, as defined in the Act. These are separate inquiries. Department attorneys shall not allege a violation of the False Claims Act unless both of these inquiries lead to the conclusion that there is a sufficient legal and factual predicate for proceeding. The following issues, among other issues, shall be considered in these determinations:

(i) Do False Claims Exist?

a. Examine Relevant Statutory and Regulatory Provisions and Interpretive Guidance. Department attorneys shall examine relevant statutory and regulatory provisions, as well as any applicable guidance from the program agency or its agents, to determine whether the claims are false. In certain circumstances, such as when a rule is technical or complex, Department attorneys should communicate with knowledgeable personnel within the program agency (e.g., the Health Care Financing Administration, TRICARE, or Office of Personnel Management) concerning the meaning of the provision.

b. Verify the Data and Other Evidence. Department attorneys shall take appropriate steps to verify the accuracy of data upon which they are relying, either independently, or with the assistance of the fiscal intermediaries and carriers, the Department of Health and Human Services - Office of Inspector General, the Federal Bureau of Investigation, or another investigative agency.

c. Conduct the Necessary Investigative Steps. Department attorneys should conduct such investigative steps as are necessary under the circumstances, including where appropriate, the subpoenaing of documents and the interviewing of witnesses.



Memorandum from the Deputy Attorney General  
 Subject: Guidance on the Use of the False Claims Act in Civil  
 Health Care Fraud Matters

(ii) Did the Provider Knowingly Submit the False Claims?

In the event the claims are false, Department attorneys must also evaluate whether the health care provider "knowingly" submitted the false claims or "knowingly" made false statements to get the false claims paid. As set forth above, and before making this determination, Department attorneys should conduct such investigative steps as necessary under the circumstances, including where appropriate the subpoenaing of documents and the interviewing of witnesses. Under the False Claims Act, false claims and false statements are submitted "knowingly" if the provider had actual knowledge of their falsity, or acted with deliberate ignorance or reckless disregard as to their truth or falsity. While relevant factors will vary from case to case and the list below is not intended to be exhaustive, factors that must be considered are:

- a. Notice to the Provider. Was the provider on actual or constructive notice, as appropriate, of the rule or policy upon which a potential case would be based?
- b. The Clarity of the Rule or Policy. Under the circumstances, is it reasonable to conclude that the provider understood the rule or policy?
- c. The Pervasiveness and Magnitude of the False Claims. Is the pervasiveness or magnitude of the false claims sufficient to support an inference that they resulted from deliberate ignorance or intentional or reckless conduct rather than mere mistakes?
- d. Compliance Plans and Other Steps to Comply with Billing Rules. Does the health care provider have a compliance plan in place? Is the provider adhering to the compliance plan? What relationship exists between the compliance plan and the conduct at issue? What other steps, if any, has the provider taken to comply with billing rules in general, or the billing rule at issue in particular?

Memorandum from the Deputy Attorney General  
 Subject: Guidance on the Use of the False Claims Act in Civil  
 Health Care Fraud Matters

e. Past Remedial Efforts. Has the provider previously on its own identified the wrongful conduct currently under examination and taken steps to remedy the problem? Did the provider report the wrongful conduct to a government agency?

f. Guidance by the Program Agency or its Agents. Did the provider directly contact either the program agency (e.g., the Health Care Financing Administration) or its agents regarding the billing rule at issue? If so, was the provider forthcoming and accurate and did the provider disclose all material facts regarding the billing issue for which the provider sought guidance? Did the program agency or its agents, with disclosure of all relevant, material facts, provide clear guidance? Did the provider reasonably rely on such guidance in submitting the false claims?

g. Have There Been Prior Audits or other Notice to the Provider of the Same or Similar Billing Practices?

h. Any Other Information That Bears on the Provider's State of Mind in Submitting the False Claims.

(B) Oversight by National Initiative Working Groups.

For all current and future national initiatives, the Attorney General's Advisory Committee (AGAC) and the Civil Division shall establish a working group to coordinate the development and implementation of each initiative.

Working groups will be comprised of Assistant United States Attorneys and Civil Division attorneys with particular expertise in health care fraud. In accordance with the health care guidelines promulgated in January 1997, in appropriate instances each working group may also need to coordinate and plan the initiative with the Department's Criminal Division.

Each working group will (i) examine the initiative to ensure that a factual and legal predicate is present for the initiative prior to its implementation, (ii) prepare initiative-specific guidance and sample documents (such as legal analyses, summaries of audit data, contact letters, tolling agreements, compliance and settlement agreement language) for use in the initiative, and (iii) prepare a general investigative plan, setting forth

Memorandum from the Deputy Attorney General  
 Subject: Guidance on the Use of the False Claims Act in Civil  
 Health Care Fraud Matters

suggested investigative steps that each office should undertake prior to proceeding. Working groups shall be responsible for coordination with law enforcement agencies, the Health Care Financing Administration, and other appropriate entities.

While the working groups shall be responsible for coordinating the overall development and implementation of national initiatives, each matter against a specific provider must be evaluated on a case-by-case basis.

(C) Use of Contact Letters in National Initiatives.

As outlined above, Department attorneys participating in national initiatives shall, in general, make initial contacts with health care providers, to resolve a case, through the use of "contact" letters. The purpose of a contact letter is to notify a provider of their potential exposure under the False Claims Act and to offer the provider an opportunity to discuss the matter before a specific demand for payment is made. In limited circumstances, where the specific facts of a situation warrant a different approach, Department attorneys may make an initial contact through other legitimate means.

The use of contact letters to make initial contact with health care providers is in furtherance of Executive Order 12988, which obligates Department attorneys to make a reasonable effort to notify the opposing party about the nature of the allegations, and attempt to resolve the dispute without litigation if at all possible. The type of contact employed will depend on the nature of the allegations and the stage of the investigation. Regardless of the form of initial contact, Department attorneys must ensure that health care providers are afforded: (i) an adequate opportunity to discuss the matter before a demand for settlement is made, and (ii) an adequate time to respond. In addition, Department attorneys shall grant all reasonable requests for extensions of time to the extent that they do not jeopardize the government's claims. The use of statutory tolling agreements are strongly encouraged to allow providers time to respond without jeopardizing the government's claims.

2. Alternative Remedies.

After reviewing the legal and factual circumstances of a particular matter, Department attorneys shall consider other available remedies -- including administrative remedies such as recoupment of overpayments, program exclusions, and civil monetary penalties -- to determine what remedy, or combination of

Memorandum from the Deputy Attorney General  
Subject: Guidance on the Use of the False Claims Act in Civil  
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remedies, would be the most suitable under the circumstances. Should the recoupment of an overpayment be the most appropriate remedy, Department attorneys shall consider referring the matter to the appropriate carrier/fiscal intermediary for appropriate action.

3. Ability to Pay Issues.

Attorneys shall consider any financial constraints identified by a provider in determining a fair, reasonable and feasible settlement between the parties. Hospitals and other health care providers citing an inability to pay a specific settlement amount should be asked to present documentation in support of their stated financial condition.

4. Rural and Community Health Care Provider Concerns --  
Impact on Availability of Medical Services.

When dealing with rural and community hospitals and other health care providers, Department attorneys shall consider the impact an action may have on the community being served. In determining an appropriate resolution, or deciding whether to bring an action, care must be taken to consider the community's interest in access to adequate health care along with any other relevant concerns.

5. Hospitals and Other Health Care Providers Not Represented by Counsel.

Department attorneys shall pay special attention to contacts with hospitals and other providers that choose (due to financial constraints or otherwise) to resolve claims without legal representation. Department attorneys faced with this circumstance must carefully assess every action taken to avoid even an appearance of coercion or overreaching because of the absence of opposing counsel.

6. Minimizing Burdens Imposed on Providers During Investigations.

Department attorneys also should be mindful of the ways in which our investigations and audits can disrupt and burden the day-to-day operations of providers in both a financial and practical sense. In developing and implementing an investigative plan, we should do what we can do to minimize these adverse effects, while still meeting our obligation to diligently

Memorandum from the Deputy Attorney General  
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investigate allegations of potential fraud. For example, while recognizing that certain circumstances might warrant different approaches, Department attorneys should consider a provider's request to accept the results of an audit of a sample of claims in lieu of a complete audit.

7. Provider Assistance with the Investigation.

In determining an appropriate settlement amount, Department attorneys should consider the extent to which a health care provider has cooperated with the audit or investigation of the relevant matter.

8. Individualized Review.

The proper determination as to the use and application of the False Claims Act or other appropriate remedy requires an individualized review of each case, ensuring that each of the above factors are given full consideration.

9. Review of Guidance.

In order to assure the fair and appropriate application of the False Claims Act, this guidance will be subject to review in six months.

10. Additional Information.

Questions regarding use of the False Claims Act should be referred to the Health Care Fraud Coordinator in your district, or to Robert Liles, Health Care Fraud Coordinator for the Executive Office for United States Attorneys (tel. no. 202-616-5136), or Shelley R. Slade, Health Care Fraud Coordinator for the Civil Division (tel. no. 202-307-0264).

Ms. SNYDER. Yes, sir.

Mr. HORN. Thank you very much.

Mr. WALDEN. I think that would be helpful because I know there was a lot of pressure brought in both directions.

Ms. Snyder, in a letter back in December, I guess, of last year to Senator Kennedy, the administrator of HCFA stated that HCFA was unable to consider using private recovery specialists because we don't have the statutory authority to pay contractors a contingency fee basis. H.R. 1827 would provide that statutory authority. Is that something you would welcome?

Ms. SNYDER. Actually, one of the things that we are looking at is whether or not we would actually need a different kind of authority or a new authority. We believe that the authority that we have under the Medicare Integrity Program allows us to look at a variety of fee arrangements, if you will, including incentive payments or incentive fees with contractors. Our concern with that is that we would have a performance measure with the contractor that accounts not only for the identification of overpayments, but the fact that those overpayments are sustained through the appeals process and are, indeed, overpayments when we get to the end of the process.

So we have been looking at our current authorities. There may be a slightly different interpretation since we responded to that letter. We don't believe that we need additional authority for recovery auditing.

Mr. WALDEN. You don't. OK. All right. Thank you, Mr. Chairman.

Mr. HORN. Well, that is a very important point, the contractor relationship within Medicare. How much control actually under the law do you have with the contractors on, say, a program such as this? On both error recovery and what not? Can you really get them to do it or are they just there and defy you?

Ms. SNYDER. No, sir. I think that, again, this is another relationship that has been over a very long period of time. We have been in business for 30 years with our fiscal intermediaries and carriers. We do give them direct instruction about activities to undertake. They have been involved in overpayment identification recovery audits. They do that work for us now. It is part of our contract agreement and budget agreements with them. They are paid to do that.

We are, however, very interested—and I know that we have spoken about this before, about contracting reform and our ability to encourage competition among entities that might also be able to do Medicare work in addition to the insurance companies.

Mr. HORN. How often does the Health Care Financing Administration take a look at contractors? And is there a fixed point in time for each contractor or how do you handle that?

Ms. SNYDER. There is a requirement that we do yearly contractor performance evaluations. HCFA has not been as diligent about that in terms of our contractor oversight, as we should be. Part of our performance evaluation expectations are around overpayment collections, financial controls, and those kinds of evaluation activities. We renew those contracts yearly and we do look at their performance.

Mr. HORN. Anything anybody in the panel would like to state and comment on, based on any dialog that has gone on up here? Often we hear people halfway home say, gee, I wish I had said something about that. That isn't the way I look at it. So anything to add to this dialog, Mr. Peterson, based on the exchanges you have heard between Members and witnesses?

Mr. PETERSON. Well, I would just second the gentleman from GAO's comments about picking the low-hanging fruit. That is essentially what our internal staff does. And you notice that we recovered \$33.8 million at a cost of less than \$500,000 in personnel costs. So that is a very cost-effective way of recouping duplicate payments and missed discounts and so forth and displays that you can do it in-house instead of paying a contractor to do it. But that does not take the place of a commercial audit recovery firm because they possess the expertise that we don't have and audit recovery is not one of our core businesses. That is not what we are in business to do.

We try to pay accurately the first time, but we do make mistakes. People make mistakes. But we try to catch them internally, if we can. Then, if we can't, what we miss, we pay the audit recovery firms to find and that is money that we wouldn't have if we didn't employ them.

Mr. HORN. Is that done by an audit firm that is internally involved on a random sample basis? Or is that a total universe examined?

Mr. PETERSON. That is the total universe. They examine all of our records.

Mr. HORN. What have you done as a result of their findings and recommendations that has lowered the amount of errors that have been had within the agency? Is it just a matter of training and getting more auditors on your own payroll? Or what?

Mr. PETERSON. Well, it is partly that. And it is learning to develop programs internally to find duplicate payments. We have found out that there are commercial auditors running computer programs looking for these. Two of our internal auditors wrote programs for us that we can learn ourselves, that our small internal staff runs on an ad hoc basis every month to look for these errors. We have found that they were finding a lot of credits on vendor statements. So we have added people to our internal staff to do that. And that has been very cost-effective.

So we are constantly learning from them. We meet quarterly to see what they have found, who they are finding it from, what firms. We go back and look at it and find out why the errors occurred and try to correct them. We are not as good as what we would like to be, but we certainly make every conscious effort to improve.

Mr. HORN. Well, I thank you for that remark. Mr. Allen.

Mr. ALLEN. We want to be like AAFES. [Laughter.]

Mr. HORN. It depends on which AAFES you are talking about, I think.

Ms. Lee, any comments on this?

Ms. LEE. Chairman Horn, one of the beauties of having this opportunity at OMB is to see the broad management issues. It struck me, in preparing for this hearing, that I saw in several cases where

there were discussions of the contractors not, for whatever reason, feeling an affirmative requirement to notify the government if they had been or suspected they had been overpaid. And so I have made an action item to talk to the CFO's. I have pulled out the payment clauses myself and was reading them and saying, you know, perhaps this is something we ought to explore. So I have got a self-action item from this hearing.

Mr. HORN. Good. Well, when you have a self-action item, I am sure it is completed. So thank you. Ms. Lee, on this point, you will recall our Debt Collection Improvement Act of 1996 that we tucked into the Omnibus Appropriations Bill of that year. There was a provision in there called gainsharing that would allow agencies to retain a portion of delinquent debts collected and this provision was designed to be an incentive for agencies to collect delinquent debt, both in terms of human resources and in terms of up-to-date computing capability.

As far as I know, no Federal department or agency is presently using the gainsharing program for debt collection. Do you know why this is?

Ms. LEE. Chairman Horn, my understanding is we at OMB have some more work to do regarding budget authority and how that gainsharing activity plays. And we look forward to working with the Congressional Budget Office to sort through those issues.

Mr. HORN. When are we going to sort it out?

Ms. LEE. Soon.

Mr. HORN. How soon? Next month?

Ms. LEE. Could I try after recess, again?

Mr. HORN. Next week? Well, after the July recess, I am all with you.

Ms. LEE. I will do that.

Mr. HORN. OK. And because there is an analogy here. And when you return that money, to what degree will it be used? Or will OMB be sitting on it to try and say the deficit is less than it is? I don't know what pot you put that in. Does it just sit in the agency accounts and they can't touch it?

Ms. LEE. I owe you an answer.

Mr. HORN. Pardon?

Ms. LEE. I owe you an answer.

Mr. HORN. OK. Without objection, Ms. Lee's answer will be in after the end of the July recess.

[The information referred to follows:]



**BEA SCORING OBSTACLE TO IMPLEMENTING GAINSHARING**

The Administration has been supportive of gainsharing for improved performance in debt collection. In 1997, OMB issued a government wide data request for agencies interested in gainsharing as authorized by the Debt Collection Improvement Act (DCIA). OMB worked closely with the Department of Treasury to provide appropriations language in the President's Budget for gainsharing in the budgets for FY 1998 and for FY 1999. In the President's Budget for 1998, \$384,000 was proposed. In the following year, the Administration proposed an appropriation of \$3 million to be used for debt collection improvement, to be derived from increased agency collections of delinquent debt, as authorized by the Debt Collection Improvement Act of 1996 which the Administration fully supported.

These proposals did not receive serious consideration in Congress due, at least in part, to congressional scorekeeping under the BEA. CBO says that it scored all of the effects of gainsharing when the DCIA was enacted. CBO contends, therefore, that the Administration's proposed appropriations of discretionary budget authority and outlays for debt collection improvement would not generate any collections that have not already been scored by them. OMB did not score the outyear effects of the DCIA and would treat the estimated additional receipts generated by the appropriations for debt collection improvement as offsets to the discretionary spending. Furthermore, the proposed appropriation language was written so that the debt collection agencies could not spend the additional appropriations unless they generated additional collections first. OMB and CBO technical staff have discussed our differences, and there appears to be no way to resolve them administratively.

Mr. HORN. Very good.

Now, Mr. Peterson, according to your statement, over the last 5 years, the Army-Air Force Exchange Service recovered about \$130 million through recovery auditing and I congratulate you on that. What was the total amount that was audited? Was it all of the \$130 or did you just miss some or how did it work?

Mr. PETERSON. Well, the total amount audited would have been, sir, approximately \$5.5 or \$6 billion times 5, over the 5 years.

Mr. HORN. Did you pick any goal when you started the internal function, down the line? Did you say, gee, if we get 10 percent out of this we will be lucky and paying the bills and so forth? Or how did you go about it in terms of a strategic plan that related to how you target the—one, reduce the errors; two, get the recovery.

Mr. PETERSON. For the commercial audit recovery, sir, or the internal?

Mr. HORN. Well, I would like to hear about both. I am trying to get experiences in the record here.

Mr. PETERSON. Well, I wasn't there in 1983 when we started, but, I guess, at that point, we knew that private industry was using commercial recovery firms and that we knew that we must have some erroneous payments, overpayments. And so we started our first contract back then. I don't know that we really had a specific goal as far as what we were going to recoup. The percentage in that first contract was very high. It was 35 to 40 percent and, as we have gone forward, the percentages have gone down with each contract that we have administered. And that is due both to the competition within the recovery business and also the ease with which they can audit records. But I can't give you an answer, sir.

Mr. HORN. Well, in other words, you used the private sector as the model in your business, which is sort of like the private sector.

Mr. PETERSON. Yes. Yes, we have applied private business practices whenever we can.

Mr. HORN. Did you get a higher level of return than business? How close was it to—

Mr. PETERSON. No, we recover probably 95 to 98 percent of the claims that are validated. Now perhaps 80 percent of our claims that are issued are validated. So out of 100 percent, 80 percent are valid. And, of that, we probably collect 95 to 98 percent.

Mr. HORN. So your cost-benefit ratio is very high, then, on recovery.

Mr. PETERSON. Oh, yes.

Mr. HORN. Well, that is very helpful and I would ask both Mr. Peterson and Mr. Allen, of the amounts identified through recovery audits, how much was disputed?

Mr. PETERSON. Well, 20 percent of ours was disputed and 20 percent is what our contracting officer agrees with, when a supplier comes back and says, well, this is the deal.

Mr. HORN. And is that, essentially, how vendor disputes are resolved? By the actual contract officer involved?

Mr. PETERSON. Yes, it is our internal procurement or purchasing person who listens to the response and that person decides whether or not the claim is valid or not. And if it is valid, then we deduct from the next payments. So we get a very high percentage of the

money. If the contracting officer feels that the vendor's claim rebuttal is valid, then the commercial recovery firm will abide by our wishes.

Mr. HORN. Mr. Allen, does your system work the same way with the role of the contracting officer?

Mr. ALLEN. Yes, sir, it does. Our statistics as to how much is initially identified as potential overpayment, how much of that potential overpayment is sustained as a legitimate claim by the contracting officer, and then, subsequently, how much of that claim is collected would differ because we are in the pilot program. I can give you those numbers if you would like.

Mr. HORN. What are some of the most common complaints by vendors who are charged with overpayments?

Mr. ALLEN. During our initial pilot program, I think the most common complaint is the one that Mr. Walden would have raised. He said, I am not sure I would want anybody coming into my records 4 years after the fact and then changing our business relationship, in effect. Having gotten past that, because there is the contract language which allows us to do that, we needed to get through a number of issues with regard to what is the proper interpretation of the contract warranty clause as to what discounts should have been offered and were not offered. A whole variety of different things.

Because part of our business was, with regard to the grocery business, if you will, that is, contracts awarded on behalf of the Defense Commissary Agency. Some of the business practices in the grocery business were not typical of government contracting, that is, contractors would come into a grocery store, if you would, and issue vendor credit memos. The contractor said that amounts to a discount offered to you. We needed to go get that documentation and verify as to whether or not that was true. So it was the different areas of dispute arose first from old documents and, second, from different business practices within the commodities we audited.

And I would think that might hold within virtually any marketplace. It would vary substantially by marketplace by commodity.

Mr. HORN. Mr. Allen, the Profit Recovery Group has made recommendations to the Defense Supply Center of Philadelphia on ways to reduce future overpayments. Do you know to what degree these recommendations have been implemented?

Mr. ALLEN. Some of them have been implemented, some of them have not. The ones where we will find it most difficult to implement are the instances where there are changes to the Prompt Payment Act. And, as you know, there were hearings by this committee earlier on that subject.

The second area where it would be most difficult would be changes to systems. You have to get a certain information technology to make those changes, in order to accommodate better recordkeeping and then better audit recovery.

We will seriously consider one of those recommendations because one of the prime benefits out of the recovery auditing is the ability to make systemic decisions. That is how you get from an initial identification of four-tenths of 1 percent overpayments down to one-

tenth of 1 percent on the recurring basis. It is by identifying those systemic issues. And we are very interested in doing that.

Mr. HORN. While we have you on systemic issues, let me ask the three of you here, and Ms. Lee has certainly got her right to get into this, and that is the year 2000 situation. To what degree have the more businesslike operations such as Mr. Allen and Mr. Peterson, to what degree are you on and how far along are you on year 2000 compliance?

Mr. PETERSON. Sir, we are 100 percent.

Mr. HORN. 100?

Mr. PETERSON. Yes.

Mr. HORN. Good. And how about you, Mr. Allen?

Mr. ALLEN. I would have to provide that answer for the record, sir.

Mr. HORN. Since we are looking now, Ms. Snyder, on the sort of quarterly basis, looking at programs, not just departments and their systems, and you are part of HHS, you are a big part of it, you are the tail that makes the dog move in one direction or the other, what is happening on your front with the year 2000?

Ms. SNYDER. The last report that I saw that was provided to the Deputy Secretary is that HCFA systems, mission critical systems, are 100—

Mr. HORN. All right, these are your self-applied and self-reported mission critical. But we are now saying we don't really care about the rest of HHS, we care can they deliver on Medicare?

Ms. SNYDER. We believe we are going to be there 100 percent. The Medicare contractor systems have gone through their first round of certification and passed. They are now in recertification and testing. And the HCFA internal systems are in the same place. The system that I own as the business owner is the Financial Accounting System that has gone through its second round of testing and passed. We believe we are ready.

Mr. HORN. Great. And, that will show in your next quarterly report? Will it? Or was it in this one?

Ms. SNYDER. Sir, I don't know. That is submitted by the Chief Information Officer, but I can certainly provide that for the record. I know those reports lag behind a little bit.

[The information referred to follows:]

We are pleased to submit to you the two most recent HHS Y2K quarterly progress reports, dated May 15, 1999, and August 13, 1999. Both make it clear that all of HCFA's mission-critical internal systems and external claims processing systems were renovated, tested, and certified as compliant by April 1999.



DEPARTMENT OF HEALTH &amp; HUMAN SERVICES

Office of the Secretary

Washington, D.C. 20201

AUG 13 1999

The Honorable Stephen Horn  
Chairman  
Subcommittee on Government Management,  
Information and Technology  
Committee on Government and Reform  
United States House of Representatives  
Washington, D.C. 20515-6143

Dear Mr. Chairman:

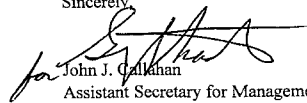
Enclosed is the Department of Health and Human Services' Year 2000 August Quarterly Report. The August monthly progress report is included as part of the Quarterly Report.

We are pleased to show 282 mission critical systems out of the Department's 283 systems, or 99 percent, are compliant. Since the May Quarterly Report, one system, the Payment Management System (PMS) was made Year 2000 compliant.

As of June 30, 1999, the one remaining system, the Resource and Patient Management System (RPMS), has been implemented at all of the sites that are directly operated by the Indian Health Services and at all of the urban Indian health programs that use RPMS. All of the remaining sites to be implemented are programs operated by individual Indian tribes. For these sites, the tribes have chosen to assume the resources and responsibility for these programs under self-determination statutes.

If your staff have any questions on these materials, please have them call Ms. Gay Morris, our Year 2000 Program Manager, on (202) 690-6376.

Sincerely,

  
John J. Callahan  
Assistant Secretary for Management  
and Budget/Chief Information Officer

Enclosure



DEPARTMENT OF HEALTH &amp; HUMAN SERVICES

Office of the Secretary

Washington, D.C. 20201

AUG 13 1999

The Honorable Jim Turner  
Ranking Minority Member  
Subcommittee on Government Management,  
Information and Technology  
Committee on Government and Reform  
United States House of Representatives  
Washington, D.C. 20515-6143

Dear Mr. Turner:

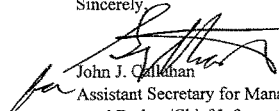
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Sincerely,

  
John J. Callahan  
Assistant Secretary for Management  
and Budget/Chief Information Officer

Enclosure



DEPARTMENT OF HEALTH &amp; HUMAN SERVICES

Office of the Secretary

Washington, D.C. 20201

AUG 13 1999

The Honorable Robert F. Bennett  
Chairman  
Senate Special Committee on the Year 2000 Technology Problem  
United States Senate  
Washington, D.C. 20510-6486

Dear Mr. Chairman:

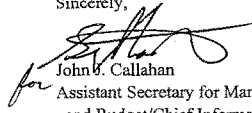
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If your staff have any questions on these materials, please have them call Ms. Gay Morris, our Year 2000 Program Manager, on (202) 690-6376.

Sincerely,

  
John G. Callahan  
Assistant Secretary for Management  
and Budget/Chief Information Officer

Enclosure



DEPARTMENT OF HEALTH &amp; HUMAN SERVICES

Office of the Secretary

Washington, D.C. 20201

AUG 13 1999

The Honorable Christopher J. Dodd  
Ranking Minority Member  
Senate Special Committee on the Year 2000 Technology Problem  
United States Senate  
Washington, D.C. 20510-6486

Dear Senator Dodd:

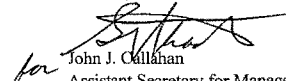
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If your staff have any questions on these materials, please have them call Ms. Gay Morris, our Year 2000 Program Manager, on (202) 690-6376.

Sincerely,

  
John J. Callahan  
Assistant Secretary for Management  
and Budget/Chief Information Officer

Enclosure





THE DEPUTY SECRETARY OF HEALTH AND HUMAN SERVICES  
WASHINGTON, D.C. 20201

AUG 13 1999

The Honorable Jacob Lew  
Director  
Office of Management and Budget  
Washington, D.C. 20503

Dear Mr. Lew:

Enclosed is the Department of Health and Human Services' August Quarterly Report regarding our progress on the Year 2000 date issue and High Impact Program Report.

We are pleased to show 282 mission critical systems out of the Department's 283 systems, or 99 percent, are compliant. As of June 30, 1999, the one remaining system, the Resource and Payment Management System (RPMS), has been implemented at all of the sites that are directly operated by the Indian Health Service and at all of the urban Indian health programs that use RPMS. All of the remaining sites to be implemented are programs operated by individual Indian tribes. For these sites, the tribes have chosen to assume the resources and responsibility for these programs under self-determination.

The August High Impact Program Report is included in Section IV of the August Quarterly Report. We are pleased to report that the Centers for Disease Control and Prevention successfully completed the testing of systems operations between partners.

Your staff may address any questions or suggestions to either Kerry Weems, HHS' Acting Deputy Assistant Secretary for Information Resources Management/Deputy CIO, at (202) 690-6162, or Gay Morris, Year 2000 Program Manager, at (202) 690-6376.

Sincerely,

A handwritten signature in black ink, appearing to read "K. Thurm".

Kevin Thurm

Sincerely,

A handwritten signature in black ink, appearing to read "John J. Callahan".

John J. Callahan  
Assistant Secretary for  
Management and Budget/  
Chief Information Officer

Enclosure

Status of Health and Human Services Year 2000 Efforts:  
Quarterly Progress Report  
 August 13, 1999

I. Progress on Mission Critical Systems

1. Indicate whether you have completed work on all mission critical systems. For a system to be deemed compliant, it must have successfully completed renovation, testing and implementation. All components of the systems must be fully deployed and operational.

<b>Exhibit 1 - Overall Progress as of June 30, 1999</b>					
AGENCY	Total Number of Mission Critical Systems	Number Compliant	Number to be Replaced	Number to be Repaired	Number to be Retired
HHS	289	282	0	1	6
ACF	45	44*	0	0	1
AHCPR	0	0	0	0	0
AOA	2	2	0	0	0
CDC	65	63	0	0	2**
FDA	34	34	0	0	0
HCFA Internal	25	25	0	0	0
HCFA External	78	75	0	0	3***
HRSA	5	5	0	0	0
IHS	5	4	0	1	0
NIH	14	14	0	0	0
OIG	3	3	0	0	0
PSC	8	8	0	0	0
SAMHSA	5	5	0	0	0

\*One of ACF's systems reported as compliant will be retired.

\*\* In this quarter, CDC retired one system; therefore, the number to be retired and the total number decreased by one.

\*\*\*HCFA previously listed 7 systems to be retired. Four of those systems have been retired; therefore, they are not included in this table.

**Total Number of Mission Critical Systems**

The total number of mission critical systems, including those to be retired, is 289 systems. Excluding the six systems still to be retired, the Department has a total of 283 mission critical systems.

**Increase in Compliant Mission Critical Systems**

As of June 30, 1999, 282, or 99 percent, of HHS's 283 mission critical systems are compliant. Between April 30, 1999 and June 30, 1999, one additional mission critical system was made Y2K compliant. Exhibit 1a, below, lists the total number of compliant mission critical systems.

<b>Exhibit 1a - Total Mission Critical Systems as of June 30, 1999</b>			
<b>OPDIV</b>	<b>Total Number Mission Critical</b>	<b>Total Number Compliant</b>	<b>Percent Compliant</b>
ACF	44*	44	100%
AHCPR	0	-	-
AOA	2	2	100%
CDC	63	63	100%
FDA	34	34	100%
HCFA - Internal	25	25	100%
HCFA - External	75	75	100%
HRSA	5	5	100%
IHS	5	4	80%
NIH	14	14	100%
OIG	3	3	100%
OS	0	-	-
PSC	8	8	100%
SAMHSA	5	5	100%
<b>TOTAL</b>	<b>283</b>	<b>282</b>	<b>99%</b>

\*One of ACF's systems reported as compliant will be retired.

### HCFA Systems

All of HCFA's 25 mission critical internal systems have been renovated, end-to-end and future date tested, certified compliant, and implemented. Among other things, these internal systems manage the eligibility, enrollment, and premium status of approximately 39 million Medicare beneficiaries, and make payments to about 400 managed care organizations.

All of the 75 mission critical external claims processing systems, operated by private insurance contractors that process Medicare fee-for-service claims and pay bills, have been fully tested and certified as compliant, and are processing and paying claims today. HCFA's independent verification and validation (IV&V) expert, with oversight from the Department's Office of Inspector General (OIG), has verified the readiness of these external claims processing systems.

2. For those agencies with unfinished mission critical systems, provide a list of all such systems, whether to be replaced, repaired, or retired. The list should include:
  1. The name of the system.
  2. A brief description of its function.
  3. The date when the agency expects to make the system compliant. If there has been a change since previous reports in the date when the system is expected to be compliant, please explain.
  4. A brief description of the implications of the system not being ready and whether there is a contingency plan in place. If there is no contingency plan, indicate when one will be complete.
  5. The reason the system is not yet compliant.

### The Resource and Patient Management System (RPMS)

HHS has only one unfinished mission critical system. The Resource and Patient Management System (RPMS) is the heart of the medical facilities information resource management activities for the Indian Health Service (IHS), Tribal, and Urban health programs. RPMS consists of modules that are developed, maintained, and distributed nationally, and installed locally at the health care facility.

The IHS has made considerable progress in the implementation of the Resource and Patient Management System (RPMS). The IHS completed all of the sites that are directly operated by the IHS, and all of the urban Indian health programs that use RPMS by June 30, 1999. All of the remaining sites to be implemented are programs operated by individual Indian tribes. IHS is projecting that these sites will be completed by September 1999.

At the present time, 25 of 166 tribally operated sites remain to achieve 100 percent implementation in tribally operated programs. For these facilities, the tribes have chosen to assume the resources and responsibility for these programs under self-determination statutes. The IHS has offered and provided technical assistance to the tribes. As sovereign nations, the tribes exercise the right to make all decisions related to their programs, including information technology infrastructure and technical assistance.

IHS health care facilities must have contingency plans as part of the requirement for accreditation by the Joint Commission on Accreditation of Healthcare Organizations (JCAHO).

Since the Year 2000 problem poses a number of new and unique threats to the continuity of information systems, the IHS provided Business Continuity and Contingency Plan (BCCP) templates to each area, site, and medical facility. These templates are being customized by the areas, sites, and medical facilities for their own specific needs. Contingency plans include the identification of potential problems, their impact on mission-critical systems, and policies and procedures to minimize any potential disruption in operations.

## II Other Progress

- A. Provide a description of progress to make non-mission critical systems compliant, including measures that demonstrate that progress.

### Non-Mission Critical Systems

HHS has 886 non-mission critical systems. Of these, 881 or 99 percent are compliant. This is an increase of 10 systems, or one percent, since the May Quarterly Report. Exhibit 2a, below, lists the number of non-mission critical systems by OPDIV and the number compliant.

<b>Exhibit 2a - Non-Mission Critical Systems</b>			
<b>OPDIV</b>	<b>Total Number of Non-Mission Critical Systems</b>	<b>Total Number of Compliant Non-Mission Critical Systems</b>	<b>Percent Compliant</b>
ACF	17	17	100%
AHCPR	1	1	100%
AOA	5	5	100%
CDC	136	136	100%
FDA	234	234	100%
HCFA-Internal	56	56	100%
HCFA-External	5	5	100%
HRSA	9	9	100%
IHS	3	3	100%
NIH	349	347	99%
OIG	3	2	66%
OS	45	44	97%
PSC	17	16	94%
SAMHSA	10	10	100%
<b>HHS Total</b>	<b>890</b>	<b>885</b>	<b>99%</b>

- B. Provide a description of progress to make data exchange compliant with all entities external to your agency. Include:
1. The total number of data exchanges, the number that are compliant on both sides, and the number which have been fixed on the Federal side.
  2. When you expect that all yours data exchanges will be compliant.
  3. A brief description of any difficulties you have encountered in making the exchange compliant.

**Data Exchanges**

HHS has a total of 146,051 external data exchanges. On April 22, 1998, the Department provided a listing of State interfaces to the National Association of State Information Resources Executives (NASIRE). This listing was updated monthly by the Department. Currently, all of HHS' external data exchanges, including State interfaces, are compliant. Exhibit 2b, below, shows the total external data exchanges by OPDIV.

<b>Exhibit 2b - Total Mission Critical and Non-mission Critical Systems with External Interfaces by OPDIV</b>				
OPDIV	Number of Systems	Number of External Interfaces	Number Compliant	Percentage Compliant
ACF	5	270	270	100%
CDC	25	381	381	100%
FDA	1	1	1	100%
HCFA - Internal	24	3,209	3,209	100%
HCFA - External	71	142,015	142,015	100%
IHS	7	10	10	100%
NIH	5	61	61	100%
PSC	9	104	104	100%
<b>Total</b>	<b>147</b>	<b>146,051</b>	<b>146,051</b>	<b>100%</b>

- C. Provide a summary description of progress in assuring that telecommunications systems used by your agency compliant, regardless of whether they are owned or managed by you, by GSA, or by some other entity. Indicate when you expect that these telecommunications systems will be compliant and describe any difficulties you are encountering in keeping to your schedule.

**Telecommunications**

The OPDIVs have inventoried and assessed their telecommunications equipment including hubs, servers, routers, bridges, and switches. Exhibit 2c, on the next page, shows the status of the equipment by OPDIV. Currently, 4,990 of the 5,509 inventoried pieces of equipment are compliant. The remaining equipment is expected to be compliant by October 1, 1999.

Exhibit 2c - DATA COMMUNICATIONS			
OPDIV	Number	Number Assessed	Number Compliant
ACF	205	205	205
AHCPR	46	46	42
AOA	21	21	21
CDC	162	162	162
FDA	1956	1956	1956
HCFA	40	40	39
HRSA	130	130	124
IHS	621	621	330
NIH	2938	2813	2571
OIG	5	5	5
OS	143	143	107
PSC	181	181	181
SAMHSA	109	109	109
<b>TOTAL</b>	<b>6,557</b>	<b>6,432</b>	<b>5,852</b>

HCFA has been working with GSA on telephone communication with its regional offices. Because of concern about the local telecommunications service providers' continuity of service during the Year 2000 date change, HCFA has instituted significant risk mitigation activity for telecommunications. HCFA is installing backup service. HCFA will have its own dedicated backup purchased, installed, tested, and ready to be put into use before January 1, 2000.

GSA has also not been able to provide adequate assurances to IHS on the Y2K readiness of equipment used by smaller telephone companies that service IHS health care facilities. IHS is contacting local telephone companies directly regarding their Y2K compliance status. IHS is also incorporating contingencies for the failure of service from local telephone companies in their BCCP process.

- D. Provide a summary description of efforts to assure that buildings and related systems, such as heating, air conditioning, and security systems are compliant, regardless of whether they are owned or managed by you, by GSA, or by some other entity. Indicate when you expect buildings and related systems that your agency uses will be compliant and described any difficulties you are encountering in keeping to your schedule.

#### Facilities

Exhibit 2d, below, lists the number of facilities owned, direct leased, GSA delegated, and tribally managed for each OPDIV as well as the number that have been assessed and are currently Y2K

compliant. Facilities include office buildings, laboratories, hospitals, clinics, central utility buildings, support buildings, and housing.

As shown in the table, HHS has completed the inventory of its 3,729 buildings and has made significant progress in accomplishing compliance evaluation and remediation activities. During the last quarter, IHS discovered new software problems in several hospital, health center and health station building automation systems while conducting IV&V activities. The problems have been identified as minor in nature and corrective actions are underway. Currently, 3,655 or 98 percent of HHS owned and managed facilities have been determined to be Y2K compliant.

<b>Exhibit 2d - Buildings</b>			
<b>OPDIV</b>	<b>Number</b>	<b>Number Assessed</b>	<b>Number of Facilities Complaint</b>
CDC	213	213	213
FDA	76	76	76
IHS	3,165	3,165	3,091
NIH	271	271	271
OS	1	1	1
PSC	3	3	3
<b>Total</b>	<b>3,729</b>	<b>3,729</b>	<b>3,655</b>

FDA has now completed remediation activities in the two laboratories that were non-compliant during the last reporting period. All of their owned and direct-leased facilities are now Y2K ready.

During the last quarter NIH concluded both the assessment and compliance evaluation of its facilities-related equipment in NIH-owned and leased buildings. In the owned buildings, the majority of the systems that control and monitor heating, ventilation, and air-conditioning (HVAC), fire alarm panels, and other infrastructure support are networked on a campus-wide basis. As of the previous reporting period, eight of the ten systems had been certified as compliant. Evaluation of the last two systems has now been completed and manufacturers/vendors' letters certifying that all ten automated building systems in NIH-owned buildings are Y2K ready have been received.

IHS deals with a complex set of direct managed, Tribal, and Urban (I/T/U) programs and facilities. The remaining devices are scheduled to have remediation activities completed by October 1, 1999.

GSA has established a status area on the GSA Y2K web site for HHS-occupied, GSA-owned and leased buildings. This is monitored closely by headquarters and OPDIV personnel. Additionally, HHS OPDIVS have taken a proactive approach to ensuring that buildings that are



not under their direct control (such as GSA-owned and leased properties) are Y2K compliant. To date, HHS has confirmations of Y2K compliance for more buildings than are shown on GSA's web site. Examples of actions being undertaken by HHS include:

- NIH has formed a Y2K coordination team that is actively working with GSA and its lessors to ensure that the buildings housing its operations are ready for the millennium change. Most of these facilities are now compliant.

- The PSC has gone directly to the lessors of the buildings it occupies and asked for and been provided letters and verbal confirmations that all of their facilities are Y2K compliant.

- CDC engineers have been working directly with the lessors of the buildings it occupies to ensure that their facilities are ready and to determine responsibility and staffing requirements to ensure full functionality on January 1, 2000. CDC has confirmed that all of the buildings it occupies which are owned or leased by GSA are Y2K compliant.

It is anticipated that all buildings not under HHS control will be Y2K compliant by November 1, 1999, or will have staffing and contingency plans in place to handle any facilities system failures.

HHS continues to be represented on the Building Systems Working Group of the Year 2000 Subcommittee of the CIO Council.

- E. Provide a summary description of progress to assure that other systems or equipment, including biomedical equipment and laboratory devices and any other products or devices using embedded chips that your agency uses are compliant. Describe any difficulties you are encountering in ensuring that such equipment is compliant.

**Embedded Systems**

Exhibit 2e, below, lists the number of embedded systems that the OPDIVs have identified, the number assessed and the number compliant. As shown in Exhibit 2e, HHS has inventoried 26,318 and assessed 26,318 systems. Currently, 26,186 or 99 percent of the total number of embedded systems are compliant. The remaining systems are expected to be made compliant by the end of September 1999.

Exhibit 2e - Embedded Systems			
OPDIV	Number	Number Assessed	Number Compliant
ACF*	1	1	1
CDC	1,009	1,009	961
FDA	1,666	1,666	1,624
HCFA*	2	2	2
IHS	22,711	22,711	22,689
NIH	929	929	909
<b>Total</b>	<b>26,318</b>	<b>26,318</b>	<b>26,186</b>

## Exhibit 2e Footnotes

\*The embedded systems are building security systems.

**Biomedical Equipment Clearinghouse**

HHS chairs the CIO Council's Biomedical Equipment Subcommittee. FDA sent letters to manufacturers of biomedical equipment to request information on the Y2K compliance of their products. This information is posted on the Biomedical Equipment Clearinghouse Web Site (<http://www.fda.gov/cdrh/yr2000/year2000.html>) established and maintained by FDA.

For the 4,200 biomedical equipment manufacturers who have submitted information to the clearinghouse, the following breakout is provided:

- 2,554 have stated that their products are not impacted by dates.
- 890 manufacturers have reported that all their products are compliant; in addition, specific information has been provided on 6,489 pieces of compliant products.
- 326 manufacturers have reported 9 non-compliant products.
- 430 manufacturers have submitted internet addresses where their product information is available; of these, 349 have indicated a problem with one or more product.

In conjunction with its operation of the Y2K Biomedical Clearinghouse, FDA has identified devices it considers "potentially high risk devices," or PHRDs. Using this list, FDA is formulating an approach for monitoring all manufacturers of these devices by initiating, with contractor assistance, a random sample audit of the manufacturers of PHRDs. The overall objective of this study is to assure that the manufacturer has systematically:

- identified all devices subject to a possible date related Y2K problem;
- applied risk analyses to determine the appropriate remediation action to be undertaken;
- validated an new hardware or software developed to fix the identified Y2K problem; and
- properly communicated information on the Y2K remediation to affected customers.

The outcome of this audit will be a report on the results. Depending on the nature of the report, FDA will then take appropriate steps to ensure the public is informed and not at risk. Below is a summary of key events and time line for the effort:

- Audits of PHRDs:
  - Awarded contract on 7/1/99 for a total of 80 audits;
  - Obtained OMB approved information collection on 7/30/1999; and
  - Conducted auditor training in mid-July.
- Process for audits of PHRDs:
  - Select random sample to audit;
  - Examine manufacturer's processes to assess Y2K status of products and to develop upgrades;
  - Develop contingency plans if non-compliance found or manufacturers refuse to participate; and
  - Complete assessments by September 21<sup>st</sup> and release report in early October.

F. Please include any additional information that demonstrates your agency's progress.

#### **FDA Outreach**

The FDA has also sent surveys to the consumable medical supply manufacturers, biologics manufacturers, and pharmaceutical manufacturers. These surveys cover approximately 12,000 manufacturers.

Of particular importance is the readiness of the 170 critical drug manufacturers (i.e., those that make sole source, orphan, or the top 200 most prescribed drugs). All critical drug firms will be assessed.

In all categories, the FDA is concerned about those manufacturers who have October or later as compliance completion dates. As a result, the Agency is reviewing what actions it can take (regulatory or non-regulatory) to facilitate the manufacturer's escalation of their Y2K efforts, ensure contingency plans are in place, or, if necessary, recall the product.

The FDA has contacted manufacturers of infant formula and medical foods, which began to submit a summary of their Y2K self assessments and contingency plans to the FDA by mid-July. The FDA has also sent a reminder to the 4,000 domestic seafood firms to take Y2K remediation actions.

#### **HCFA Outreach**

HCFA chairs the Health Care Sector Working Group composed of federal and private industry members and is working with our health care partners (e.g., the American Hospital Association, the American Ambulance Association, the American Health Care Association, the National Association of Rural Health Clinics) to ensure that all health care organizations are Y2K ready.

These associations are contacting their members (e.g., hospitals, clinics, and other health-related organizations) to determine their Y2K readiness.

HCFA is reaching out to health care plans and providers through 60 scheduled events - 23 one day conferences and 37 learning sessions, all of which will have been completed in early September. In general, these sessions discuss Medicare and Medicaid Y2K readiness, the status of the biomedical equipment and pharmaceutical industry, and financial and service assistance to organizations to prepare for the Year 2000 date change. In addition, HCFA is funding nine rural Y2K conferences that are being conducted by other organizations such as the Rural Health Clinics Association and the California Nurses Association. HCFA has established a Y2K telephone site (1-800-958-HCFA) to answer questions for plans and providers who may also access Y2K information at <http://www.hcfa.gov/y2k>.

### III Federally supported, State-run Programs.

- I. Describe efforts to ensure that Federally supported, State-run programs (including those programs run by territories and the District of Columbia) will be able to provide services and benefits. In particular, Federal agencies should be sensitive to programs that will have a direct and immediate affect on individuals' health, safety, or well-being. Include a description of efforts to assess the impact of the year 2000 problem and to assure that the program will operate. In addition, the Department of Health and Human Services, the Department of Labor, and the U.S. Department of Agriculture must provide the following information for those programs listed in Attachment D.

#### **ACF Federally-supported, State-run Programs**

ACF developed a partnership plan for assessment of the States' Y2K efforts in key federally-supported, State-run programs. These programs are Temporary Assistance to Needy Families (TANF), Child Care (CC), Child Support Enforcement (CSE), Child Welfare (CW), and the Low Income Home Energy Assistance (LIHEAP). The goal is to keep State partners focused and on track with Y2K efforts and contingency planning to assure the public will have no disruption of services beginning January 1, 2000. ACF will inform, support, and provide assistance to State and local partners. The plan consists of three different kinds of tasks to prevent disruption in benefits and services. These are identified below:

- Leadership and Guidance - ACF will establish the roles and responsibilities including a commitment of resources, and accountability in collaborations with contractors and internal partners;
- Outreach and Information Sharing - ACF will ensure effective commitment and collaboration with external partners; and
- Technical Assistance and assessments - ACF will plan and implement the assessments; facilitate on-going planning and action by its external partners; conduct follow-up activities to address program problems identified through assessments and other channels.

ACF began its on-site assessment visits on May 24, 1999, and expects to complete the first round of assessments for all States and territories by mid-September. The assessment reports will be sent to the Directors of the Programs, State CIOs, State Y2K coordinators, and Governors.

### HCFA Federally-supported, State-run Programs

The Medicaid Program is administered directly by the States with oversight from HCFA. Although States are responsible for assuring Y2K readiness of their computer systems, HCFA provides technical assistance to State Medicaid agencies, including protocols for Y2K compliance and testing, contingency planning strategies, and information on best practices. HCFA has also taken the extra step of hiring expert consultants who, through site visits, are assessing States' progress against their own goals and standards in becoming Y2K compliant, as well as providing detailed feedback and additional technical support. These contractors are also assessing the adequacy of each State's contingency plans.

The first round of State site visits have been completed. HCFA and its independent contractors visited all 50 States and the District of Columbia as part of the first round of assessments of State Medicaid.

The purpose of the initial visits was to:

- establish an objective assessment of the status of each State's Y2K remediation efforts; and
- provide technical assistance in such areas as risk mitigation, contingency planning, configuration management, and business continuity.

To compare and contrast the relative level of risk of Y2K failure for each Medicaid system in each State, HCFA is using a risk rating based on the evaluation of 42 individual factors that measure the processes, products, and progress of a State's Medicaid Y2K efforts. These include various independent factors that measure project management considerations, among others, that are correlated with the five critical phases identified by the General Accounting Office: Awareness, Assessment, Renovation, Validation, and Implementation.

Scores on individual factors are weighted using a special protocol. An accumulated score is reached by adding the individual factors with the verification and validation experience of the on-site assessors. Each State's Medicaid Management Information System (MMIS), State Children's Health Insurance Program (SCHIP) system, and eligibility system (ES) fall into one of the three risk categories (High, Medium, and Low) based on the accumulated score. Depending on the State's status, second and even third round visits may be conducted.

- **High Risk Systems** tend to share many of the same characteristics, such as usually poor project management, poor planning, and inadequate testing. There often is a lack of progress relative to the State's own schedule, and often no independent validation and verification of the State's status. Other common factors among high risk systems include: a lack of an objective certification process, poor quality assurance measures, and a poor or nonexistent contingency plan to assure system remediation or business continuity in case of failure. The mix of these factors vary from State to State.

- *Medium Risk Systems* tend to exhibit some smaller set of the same characteristics of high risk systems, but are often characterized by better management practices. As a result, there is a better chance that risks will be mitigated in the coming months. For this reason, medium risk sites warrant a follow-up visit to verify the anticipated improvement.
- *Low Risk Systems* usually combine a solid management approach, adequate resources, solid renovation and testing, all with adequate control and independent validation and verification. However, even these systems are not “no risk” since the delivery of Medicaid services are highly decentralized and depend heavily upon the smooth operation of many people and services beyond the States direct authority control.

Second round site visits, devoted to the Y2K efforts of medium- and high-risk States, are currently underway. These visits began in early May and are expected to be completed by mid-September 1999. They focus on the status of States’ validation and implementation phases, end-to-end testing, risk mitigation, business continuity and contingency planning, Day One planning, and outreach activities to beneficiaries and providers. Thus far, in the second round of visits, States have shown substantial progress in their Y2K readiness.

The information gathered during these visits, and the conclusions reached, are discussed with State officials in a debriefing session. Results of each site visit are sent to the State Medicaid Director. A letter from the Secretary is sent to the Governor (and the Mayor of the District of Columbia) with the assessment reports. These results document HCFA’s key findings and recommendations and request the Governor’s leadership in assuring that federal and State systems will work effectively into the Year 2000. The States are also provided with recommendations and other types of technical assistance to strengthen their Y2K remediation efforts.

- The date when each State’s systems supporting the program will be Y2K compliant. Compliant here indicates the date the State has determined when its systems will be able to provide services, whether directly or indirectly, to beneficiaries.

On the next page, the State/Program Compliance Report shows the compliant or projected compliant date expected for the federally-supported, State-run programs for each State.

## STATE/PROGRAM COMPLIANCE REPORT

Not Reported - N/R

Projected Compliant - \*

\*\*LIHEAP Information was taken from the Federally Supported State Run Programs charts dated 7/12/99.  
 C - Y2K Compliant  
 NI - No information was reported.

State	Child Welfare	Child Care	Child Support	TANF	LIHEAP **	IES	MMIS
AL	7/99	7/99	12/99*	9/99*	7/99	7/99	10/99
AK	N/R	N/R	N/R	N/R	N/I	5/99	7/99
AZ	2/98	8/98	12/98	9/98	C	6/99	6/99
AR	2/99*	10/98	2/99*	2/99*	N/I	7/99	5/99
CA	12/98	No System	11/99*	12/98	N/I	12/98	6/98
CO	6/99*	6/99*	6/99*	6/99*	N/I	6/99	6/99
CT	6/99*	4/99	3/99	6/99*	N/I	9/99	6/99
DE	12/95	12/98	12/95	12/98	7/99	10/99	5/99
DC	N/R	N/R	N/R		10/99	5/99	10/99
FL	8/98	7/99*	11/98	8/98	N/I	12/98	6/99
GA	N/R	N/R	6/99	10/99*	5/99	10/99	9/99
HI	4/99*	6/99*	5/99*	11/98	N/I	11/98	12/98
ID	12/98	11/99*	3/99*	10/98	N/I	9/98	12/97
IL	7/99	3/99*	12/99*	9/99*	N/I	6/99	8/99
IN	4/96	6/99*	7/99*	10/99	7/99	4/99	6/99
IA	3/99*	3/99*	N/R	4/99*	N/I	6/99	6/99
KS	9/98	1/99	5/99*	5/99*	C	6/99	11/98
KY	12/98	4/99*	6/99*	6/99*	C	3/99	4/99
LA	7/98	7/99*	9/98	9/98	N/I	7/99	11/99
ME	4/98	No System	3/99	3/99	7/99	5/99	5/99
MD	6/98	5/98	6/98	8/99*	N/I	9/98	8/99
MA	4/99*	9/99*	1/99	6/99*	N/I	3/99	9/99
MI	4/99*	5/99*	1/99	5/99*	C	9/99	3/99
MN	4/99*	No System	N/R	7/99	N/I	5/99	12/98
MS	6/99*	N/R	6/99*	6/99*	N/I	7/99	3/99
MO	4/99	2/99	10/98	5/99	N/I	7/99	7/98

## STATE/PROGRAM COMPLIANCE REPORT

Not Reported - N/R

Projected Compliant - \*

\*\*LIHEAP

Information was taken from the Federally Supported State Run Programs charts dated 7/12/99.

C - Y2K Compliant

NI - No information was reported.

State	Child Welfare	Child Care	Child Support	TANF	LIHEAP	IES	MMIS
MT	6/99*	6/99*	4/99*	7/99	C	7/99	7/97
NE	7/99*	7/99*	6/99*	7/99*	N/I	12/97	7/99
NV	7/99*	6/99*	9/99*	9/99*	N/I	7/99	7/99
NH	5/99*	5/99*	10/99*	12/98	N/I	10/99	8/99
NJ	7/99*	9/99*	6/99*	6/99*	C	7/99	8/99
NM	N/R	N/R	10/99*	10/99*	N/I	3/97	9/99
NY	1/99	11/98	12/98	12/98	N/I	6/99	12/98
NC	1/99	5/96	12/97	9/99*	6/99	9/99	8/99
ND	7/99*	1/98	5/97	12/97	N/I	7/98	7/98
OH	6/98	6/98	9/99*	5/99	N/I	4/99	10/99
OK	10/99*	10/99*	11/99*	10/99*	N/I	9/99	9/99
OR	6/99*	3/99*	6/99*	4/99*	N/I	8/99	8/99
PA	12/98	10/98	7/99	11/98	N/I	12/98	12/98
RI	11/99*	7/99*	3/99*	7/99*	N/I	11/99	9/99
SC	6/99*	10/98	6/99*	5/99*	7/99	6/99	9/99
SD	7/99*	3/99*	3/99*	3/99*	C	3/99	5/99
TN	7/99*	11/99*	8/99*	11/98	N/A	1/99	9/99
TX	N/R	9/98	9/99*	8/99*	N/I	8/99	7/99
UT	10/99*	7/98	10/99*	7/98	C	11/98	12/98
VT	1/99	10/98	6/99*	6/99*	6/99	6/99	6/99
VA	3/99	No System	5/99*	3/99	9/99	6/99	9/99
WA	9/98	3/98	11/98	3/99	C	4/99	4/99
WV	N/R	N/R	N/R	N/R	N/I	11/98	6/99
WI	6/98	3/99*	3/99*	3/99*	N/I	12/98	7/99
WY	12/98	12/98	12/98	12/98	N/I	12/98	4/99



- A list of States, if any, for which the Y2K problem is likely to cause significant difficulties in the State's operation of the program. Also provide a list of States which are not likely to encounter significant difficulties.

#### **HCFA Risk Assessments of Federally-supported, State-run Programs**

During the assessments, accumulated scores were calculated on 42 individual factors resulting in a risk category rating. Just because a State's risk category rating is high does not necessarily mean that the State will have significant difficulties in the State's operation of the program. After the first Round of assessments and seven Round 2 visits, only two States are at High Risk for both the Medicaid Management Information System (MMIS) and the Eligibility System (ES). These two States are North Dakota and South Carolina. Below is a listing of States by risk categories.

- States at High Risk in one category: AL, DE, MA, NH, OH, OK, TN, VT
- States at Medium Risk in both categories: DC, GA, KY, MO, NM, OR, NV, RI, WV, WY
- States at Low Risk in both categories: CA, FL, IA, ID, KS, MD, ME, MI, MS, NE, PA, SD, UT, WA, WI

On the next page, the Risk Status chart shows the status of each State as assessed by HCFA.

**Risk Status of Federally-Funded State Health Care Programs**  
 Data reflect site visits from November 1998 through May 1999, and do not necessarily reflect the current status of state system readiness. State readiness information is subject to frequent changes.

STATE	VISIT DATE <sup>1</sup>	MMIS/SCHIP <sup>2</sup>	ELIGIBILITY	(BCCP) <sup>5</sup>
		RISK SCORE <sup>3</sup>	RISK SCORE <sup>3</sup>	✓=Received/ Under development
		RATING <sup>4</sup>	RATING <sup>4</sup>	
Alabama	May 1999	2000 - High	1500 - Medium	✓
Alaska	March 1999	1400 - Medium	1300 - Low	✓
Arizona	March 1999	1800 - Medium	1100 - Low	✓
Arkansas	March 1999	1000 - Low	1600 - Medium	✓
California	February 1999	1100 - Low	900 - Low	✓
Colorado	March 1999	1400 - Medium	1000 - Low	✓
Connecticut	March 1999	1000 - Low	1700 - Medium	✓
Delaware	March 1999	1200 - Low	2300 - High	✓
District of Columbia	May 1999	1600 - Medium	1800 - Medium	✓
Florida	March 1999	1100 - Low <sup>7</sup>	800 - Low	✓
Georgia	May 1999	1400 - Medium	1800 - Medium	✓
Hawaii	April 1999	1200 - Low	1500 - Medium	✓
Idaho	March 1999	1300 - Low	1200 - Low	✓
Illinois	April 1999	1000 - Low	1500 - Medium	✓
Indiana	April 1999	1500 - Medium	1000 - Low	✓
Iowa	December 1998	Pilot <sup>6</sup> - Low	Pilot <sup>6</sup> - Low	✓
Kansas	March 1999	900 - Low	1200 - Low	✓
Kentucky	April 1999	1700 - Medium	1500 - Medium	✓
Louisiana	May 1999	1100 - Low	1300 - Medium	✓
Maine	May 1999	1100 - Low	1100 - Low	✓
Maryland	May 1999	1200 - Low	Pilot <sup>6</sup> - Low	✓
Massachusetts	May 1999	2200 - High	1000 - Low	✓
Michigan	March 1999	1000 - Low	1000 - Low	✓
Minnesota	April 1999	1000 - Low	1500 - Medium	✓
Mississippi	March 1999	800 - Low	800 - Low	✓
Missouri	March 1999	1400 - Medium	1800 - Medium	✓
Montana	March 1999	800 - Low	1500 - Medium	✓
Nebraska	April 1999	1300 - Low	1300 - Low	✓
Nevada	April 1999	1600 - Medium	1600 - Medium	✓
New Hampshire	March 1999	1100 - Low	2400 - High	✓
New Jersey	December 1998	Pilot <sup>6</sup> - Low	Pilot <sup>6</sup> - Medium	✓
New Mexico	February 1999 <sup>8</sup>	1400 - Medium	1900 - Medium	✓
New York	January 1999	1700 - Medium	1300 - Low	✓
North Carolina	December 1998	Pilot <sup>6</sup> - Low	Pilot <sup>6</sup> - Medium	✓
North Dakota	March 1999	2100 - High	2100 - High	✓
Ohio	March 1999	2100 - High	1000 - Low	✓
Oklahoma	March 1999	2200 - High	1600 - Medium	✓
Oregon	March 1999	1700 - Medium	1700 - Medium	✓
Pennsylvania	November 1998	Pilot <sup>6</sup> - Low	Pilot <sup>6</sup> - Low	✓
Rhode Island	April 1999	1400 - Medium	1700 - Medium	✓
South Carolina	February 1999	2300 - High	3500 - High	✓
South Dakota	April 1999	1100 - Low	1300 - Low	✓
Tennessee	April 1999	2000 - High	1200 - Low	✓
Texas	January 1999	800 - Low	1400 - Medium	✓
Utah	March 1999	1200 - Low	800 - Low	✓
Vermont	April 1999	900 - Low	2300 - High	✓
Virginia	December 1998	Pilot <sup>6</sup> - Medium	Pilot <sup>6</sup> - Low	✓
Washington	February 1999	900 - Low	800 - Low	✓
West Virginia	March 1999	1600 - Medium	1300 - Medium	✓
Wisconsin	February 1999	1300 - Low	1100 - Low	✓

**Risk Status of Federally-Funded State Health Care Programs**

**Data reflect site visits from November 1998 through May 1999, and do not necessarily reflect the current status of state system readiness. State readiness information is subject to frequent changes.**

**NOTES:**

<sup>1</sup> Visit Date: Forty-four (44) states depicted on this chart with visit dates between the November 1998 - April 1999 time frames have received one visit. Seven (7) states that have received a second visit are depicted on the chart with a May 1999 time frame. Second round visits are currently underway and will be completed during mid September 1999. The assessment results of second visits to states will be reflected in subsequent releases of this chart.

<sup>2</sup> MMIS = Medicaid Management Information Systems. SCHIP = State Children's Health Insurance Programs.

<sup>3</sup> Risk Score Ranges (scores for states have been rounded to the nearest hundred):

High = above 1999 points  
Medium = 1400 - 1999 points  
Low = below 1400 points

<sup>4</sup> Risk Score Rating: Refer to HCFA Fact Sheet entitled "Y2K Readiness of Medicaid & the States' Children's Health Programs" under the heading Medicaid Risk Exposure Determination.

<sup>5</sup> BCCP = Business Continuity Contingency Plans.

<sup>6</sup> Pilot: These states were the first to be visited during November and December 1998, and the data gathered was used to calibrate the risk/weighting criteria for subsequent visits.

<sup>7</sup> Florida's SCHIP system is rated at Medium risk.

<sup>8</sup> The initial risk status for New Mexico's MMIS system, as reported to the state, was High. Subsequent analysis determined the risk to be Medium.

### ACF Y2K Readiness Assessments of Federally-supported, State-run Programs

ACF has visited 43 States. Some of the initial reports have been sent to the Program Directors for their review and comment. They have ten days to respond to the report. Then a letter forwarding the report is sent to the Governor, State CIO, and State Y2K coordinator. As reports are being finalized, the first letters to the Governors, State CIOs, and State Y2K coordinators will be sent in mid- to late-August. Thus far, ACF has not discovered any significant problems in the States visited. However, ACF will review business continuity and contingency plans and offer technical assistance to States, if needed.

- For those State likely to have significant difficulties, a brief description of any action that the Department is taking to assure that the program will operate.

### HCFA Response to High Risk Status States

A third round of visits will be conducted in high- and medium-risk States after completion of the second round. In these cases, particular attention will be paid to the States' contingency plans and risk mitigation efforts.

Other activities will be conducted with States not scheduled for second and third round visits. For example, follow-up calls will be made to gauge and monitor progress in specific areas of interest and verify that a State's risk status is not changing. Should there be a change in status, on-site visits will be scheduled.

HCFA has requested business continuity and contingency plans from all States, territories and the District of Columbia. HCFA and its contingency planning contractor are providing technical support on the development and evaluation of State contingency plans.

- For each program, provide an estimate by fiscal year of the Federal share of State costs associated with efforts to achieve Y2K compliance (report totals in millions and tenths):

The Department asked ACF and HCFA to work with the Federally-supported, State-run programs to develop an estimate of the Federal share of State Y2K compliance costs for the information systems that support the program. Estimates were limited to costs for information systems only and are:

- directly attributable to Y2K conversion;
- reflective of known, not speculative costs; and
- limited to costs that have been/will be necessary in order to develop or implement plans to ensure that systems are made compliant.

The cost tables for Child Care (CC), Child Support Enforcement (CSE), Child Welfare (CW), Low Income Home Energy Assistance (LIHEAP), Temporary Assistance to Needy Families (TANF), and Medicaid Management Information Systems (MMIS) are included in Appendix A to this report.

IV High Impact Plans. For each of the 43 high impact programs for which your agency is the lead provide:

1. Key partners in the provision of services, including all those necessary to ensure that program services reach the public.
2. A brief description of the process of testing with key partners, which may include internal testing, data exchanges, and end-to-end testing, and provide a date when this testing process was or will be complete.
3. A date or dates to inform the public of program readiness end-to-end. Include dates even if they have passed. Indicate if dates have changed and explain why.

**High Impact Program Reports**

Exhibit 3, below, shows the OPDIVs and the high impact program administered by the OPDIVs and their partners. The monthly high impact program reports are included in Appendix B. These reports show the milestone schedule for testing systems operations between partners and target dates for announcements of the completed processes. Completion of the last test of systems operations between partners is expected at the end of October.

<b>Exhibit 3 - High Impact Program Partners</b>		
<b>OPDIV</b>	<b>High Impact Program</b>	<b>Partners</b>
ACF	CC, CW, CSE, LIHEAP, and TANF	State and territorial agencies that administer the five high impact programs
CDC	Disease Monitoring and the ability to issue warnings	State and territorial Public Health Laboratories; USDA; FDA; State Health Departments; U.S. Treasury; vaccine manufacturers; healthcare providers; Tuskegee beneficiaries
HRSA	Organ Transplantation	United Network for Organ Sharing (UNOS)
IHS	Indian Health Services	American Indian Tribes; Alaska Indian Health Programs; Urban Indian Health Programs; and Tribal Organizations
HCFA	Medicare Medicaid	Medicare Contractors States

CDC has successfully completed its end-to-end testing. In identifying its six systems for end-to-end testing, CDC carefully reviewed the inventory of information systems in the context of

1) systems with external data exchanges, 2) disease surveillance systems that are time-sensitive, and 3) other systems that support major financial payments and/or other critical resources.

ACF participated in the first scheduled end-to-end test of the Payment Management System on August 5, 1999. Data for grants in all five high-impact programs were produced and submitted to PSC. In the test, PSC submitted authorization for payment to the Federal Reserve Bank. Grantees drew down these test funds and completed the end-to-end test of the grants payment process. The August 5, 1999, end-to-end test simulated operations on January 3, 2000. A test scheduled for August 12, 1999, will simulate operations on February 29, 2000. Test results will be available in late August 1999.

V. Change Management and Verification Efforts

1. Describe how and to what extent internal performance reports, (i.e., compliance of systems repaired and replaced) are independently verified. Provide a brief description of activities to assure independent verification that systems are fixed and to assure that information reported is accurate. Also identify who is providing verification services (for example, Inspectors General or contractors).

All OPDIVs will use outside contractors for their Independent Verification and Validation (IV&V). The contractors that the OPDIVs are working with are listed below.

ACF - AverStar, Inc., SRA, Inc., and Lockheed-Martin	HRSA - Computer Associates and Eagle Technologies
CDC - TRW	IHS - Mitretek
FDA - TRW	NIH - OAO
HCFA - AverStar, Inc., and SETA	PSC - Mitretek and TRW (formerly BDM) SAMHSA - InfoPro

OPDIVs are required to submit their IV&V reports to ASMB for review.

In addition to IV&V contractors, the Office of the Inspector General (OIG) is conducting an on-going audit on the Y2K date conversion project. Along with the IV&V contractors, they conduct on-site visits to Medicare external contractors and review each of the OPDIVs Y2K efforts.

2. Described your agency's change management process to assure that the effect on year 2000 readiness is conducted prior to establishing new requirements or changes to IT systems. <sup>3</sup>

See Section V.3 below under "Moratorium Plans" and Section VI, "Regulatory Review."

3. Described any ongoing testing your agency is undertaking to ensure readiness of systems, such as integration testing, end-to-end testing, and retesting of key systems to further ensure readiness.

**End-to-End Testing**

The PSC is currently performing end-to-end testing on the Grants Payment Process of the legacy Payment Management System (PMS). The grants payment process for high-impact programs will be included in the test. The purpose of this testing is to verify that the grant award data

received from the partners will not be affected by any potential Y2K related problems when processed through PMS. The end-to-end testing will involve PSC, OPDIVs that award grants, grantees, the Federal Reserve Bank and representative banks across the country that have agreed to participate.

The end-to-end testing with PSC's Human Resource Service and the Treasury was successful for both the Civilian and Commissioned Corp Payroll and Personnel Systems. To accommodate availability of OPDIV personnel, end-to-end testing with the OPDIVs is scheduled to be completed by mid-October.

HCFA is giving health care providers the opportunity to test with the claims processing contractors' systems to determine whether provider claims, including future-dated claims, can be successfully submitted to, and accepted and processed by, the contractors. Through its outreach efforts, HCFA is urging providers to take advantage of this testing opportunity.

#### **Re-certification Policies**

All of the OPDIVs have established policies to require re-certification of any mission critical system for Y2K compliance if any change is made to a system after Y2K certification. Most of the OPDIVs will have an Independent Verification and Validation to re-certify the system.

HCFA's re-certification policy extends further than a change management policy. Because of the complexity of the Medicare program and the small system changes required by law that needed to be made after March 31, 1999, HCFA is retesting its internal and external mission critical systems and will be re-certifying as to their readiness. HCFA is requiring all Medicare contractors and shared system maintainers to formally re-certify their Year 2000 compliance between June 28, 1999, and November 1, 1999. The objective of re-certification policy is to ensure that all Medicare systems will operate successfully in all future years without exception.

#### **Moratorium Plans**

All of the OPDIVs have also instituted moratorium plans. The effective dates are listed in Exhibit 4 on the next page. The moratorium halts any changes to systems during these dates to ensure the systems' certified Y2K compliant status. In some cases, exceptions may be allowed during the moratorium through a strict approval process established by the OPDIV for the issuance of a waiver. For example, an exception may be granted to make a change to a system mandated by legislation.

Exhibit 4 - Moratorium Plans	
OPDIV	EFFECTIVE DATE
ACF	10/1/99 - 1/30/2000
AHCPR	8/1/99 - 3/1/2000
AoA	11/10/99 - 1/31/2000
CDC	9/1/99 - 1/15/2000
FDA	10/1/99 - 1/31/2000
HCFA	10/1/99 - 3/31/2000
HRSA	10/1/99 - 2/29/2000
IHS	10/1/99 - 3/31/2000
NIH	10/1/99 - 1/30/2000
OIG	10/1/99 - 1/3/2000
OS	10/1/99 - 1/30/2000
PSC	10/15/99 - 1/30/2000
SAMSHA	9/30/99 - 1/30/2000

VI Regulatory Review.

Describe your agency's process for reviewing regulations to consider the effect of the regulation on the Year 2000 readiness or regulated entities and to consider alternatives to minimize that effects.

**ACF**

ACF conducted a thorough review of program requirements that might have an impact on State and grantee partners' ability to achieve Y2K compliance. The review showed that:

- For most ACF programs, January is not a key time frame, since grants processing and crucial reporting occur at other times of the year.
- For several ACF programs, grantees are not highly automated.
- For many program requirements that might be considered to fall within the Y2K time frame, all or most States' and grantees' systems are Y2K compliant.
- Some requirements are outside the control of ACF (e.g., Child Support Enforcement has some IRS mandates).
- Some requirements already include Y2K provisions to relieve States in the case of dire Y2K issues (e.g., TANF).

ACF is revisiting these concerns throughout the summer as more specific information on State and local Y2K compliance status is gathered through on-site assessments. If required, ACF will



consider relieving States of program requirements should they prove to be an unexpected Y2K burden. In addition, any new regulations or other program requirements that must be imposed during the Y2K timeframe will take Y2K issues into account. ACF will follow guidance issued in OMB's memo dated May 14, 1999, to mitigate any negative effects on customers and partners.

#### **FDA**

FDA recently conducted a regulatory review. The focus was on Good Manufacturing Practices since these are the regulations that most directly impact the manufacturer. It was found that no new GMP regulations are pending during the period of Y2K vulnerability. The Office of Policy, which has a central role in FDA's Y2K Outreach program, is also a key part of the regulatory review and development process and can be expected to actively address the impact of Y2K on new regulations as they come to light. In addition, the Agency concluded that existing GMPs could not be modified without impacting unduly on the Agency's ability to ensure that its regulated products are safe and effective. Furthermore, those GMPs are the means by which FDA will take actions against those manufacturers whose products fail as a result of Y2K.

#### **HCFA**

In the late Spring of 1998, HCFA performed a thorough and intensive review of all upcoming projects, including the activities required by the Balanced Budget Act of 1997 (BBA). Some of these projects would have required changes to HCFA's internal computer systems and the computer systems managed by the Medicare contractors. None of the projects would have required changes to State Medicaid systems.

HCFA developed a strategy to minimizing system changes in the short term (while Year 2000 date renovations are under way) by looking for other means to implement legislative requirements. After completing its review, HCFA determined that a number of BBA provisions did not require systems changes. These include:

- Implementation of the Medicare+Choice program and
- Implementation of the beneficiary incentive program.

About two-thirds of the BBA provisions affecting HCFA did not have to be delayed because the systems changes required to implement them had already been completed or were already underway and could be completed before major systems changes had to be frozen for Y2K. These include:

- Routine payment updates for FY 1999, including inpatient hospital coding and price changes;
- Implementing the resource-based practice expense system;
- Paying outpatient rehabilitation therapy services using the physician fee schedule;
- New prevention benefits and other coverage requirements (e.g., diabetes test strips, bone mass measurement);
- Skilled nursing facility prospective payment rates, effective July 1, 1998 (without consolidated billing for Part B residents);

- Transfer of payments for certain Diagnostic Related Groups to post-acute care providers; and
- The competitive bidding demonstration for durable medical equipment.

For those projects that would have required major systems changes, HCFA made the difficult decision to delay those projects to make sure that its systems and those managed by the Medicare contractors would continue to operate on January 1, 2000. These projects include:

- Prospective payment systems for outpatient hospital care;
- Consolidated billing for Medicare Part B services provided in skilled nursing facilities; and
- A new fee schedule for ambulance services.

In addition, the \$1,500 payment caps on outpatient physical and occupational therapy will be applied on a provider-specific basis rather than a per beneficiary basis.

HCFA had some initial concerns that Y2K priorities might delay scheduled Medicare payment updates for doctors, hospital and other providers in fiscal and calendar year 2000. However, we recently determined that payment updates can be made in October and mid-January as long as Y2K readiness efforts continue on track. Only system table updates will be made in October to update pricing for institutional providers.

By law, Medicare payment updates for Part A providers, including inpatient hospitals, skilled-nursing facilities, home-health agencies and hospices are supposed to occur on October 1 of each year, while payment updates for physicians and other Part B providers and suppliers are supposed to occur on January 1 of each year. Because of the Y2K compliance status of contractors systems, HCFA is now expecting to make Part A payment updates on October 1, 1999, but to minimize system disruptions, there will be no changes in ICD-9-CM codes (International Classification of Diseases, 9th Revision, Clinical Modification) for Fiscal Year 2000. HCFA expects to make Part B payment updates on January 17, 2000, but will apply the updates retroactively to all claims for services on or after January 1, 2000.

HCFA has also reviewed Medicaid regulations. As of this date, there are no pending Medicaid regulations that would impact State Medicaid systems through December 1999.

In addition to the above decisions on specific legislative and regulatory provisions, on March 26, 1999, HCFA imposed a moratorium on the release of new software once initial HCFA certification has been achieved. The moratorium was effective immediately, but allows for limited exceptions during the period leading up to September 30, 1999, to accommodate changes mandated by legislation. The moratorium would be essentially absolute beginning October 1, 1999, until lifted by the Chief Information Officer. The moratorium, in effect, institutes a change management control process for the duration of the project.

VII Business Continuity and Contingency Plans (BCCPs).

Provide information on the progress in developing and testing BCCPs in your agency. Include:

1. Assurances that local and regional offices have developed and tested business continuity and contingency plans in coordination with headquarters offices. Also provide the total number of such facilities which require BCCPs and the number that have such plans in place.

All of the OPDIVs that have local and regional offices have involved them in the development of business continuity and contingency planning. IHS has worked not only with the Area offices but also with medical facilities to ensure they have Y2K BCCPs in addition to the the continuity of operations (COOP) and disaster plans required as part of the Joint Commission on Accreditation of Health Care Organizations (JCAHO) accreditation process. Members of the Human Services Sector are exploring options to hold a meeting/conference of regional Y2K coordinators for each program office to promote further coordination of their activities at the regional level and increase overall effectiveness with respect to BCCPs as well as oversight of outreach activities.

2. An estimate of costs associated with the development of your agency's BCCP.

Exhibit 5, below, shows the costs for BCCP development by OPDIV. The total HHS costs for BCCP development is \$8,267,962.

<b>Exhibit 5 - Costs for Development of Business Continuity and Contingency Plans</b>	
<b>OPDIV</b>	<b>Costs</b>
ACF	\$187,720
AHCPR	\$105,000
AOA	\$37,000
CDC	\$192,000
FDA	\$950,000
HCFA	\$1,600,000
HRSA	\$1,200,000
IHS	\$2,527,955
NIH	\$672,000
OIG	*
OS	*
PSC	\$787,700
SAMHSA	\$8,587
<b>TOTAL</b>	<b>\$8,267,962</b>

## Footnote Exhibit 5

\* OIG and OS have not incurred external costs such as contractors to assist in the development of the BCCP. Hours and funding associated with this activity are attributed to operational costs.

3. An estimate of costs associated with contingency implementation for activities that are planned to be implemented regardless of how Y2K affects your agency's operations. For example, if your agency will be printing paper forms or requiring employee overtime as a risk-mitigation strategy, these costs should be reported.
  - a. Do not report costs associated with activities that will be implemented only if a problem occurs.

Exhibit 5a, below, shows the estimated costs for each OPDIV of Day One risk mitigation activities and BCCP implementation regardless of how Y2K affects operations. The total estimated cost for Day One and BCCP preparatory activities is \$98,860,229. This estimate does not include the entire cost for the invoking of BCCPs.

<b>Exhibit 5a - Estimated Costs for Implementation Regardless of How Y2K Affects Operations</b>			
<b>OPDIV</b>	<b>DAY ONE</b>	<b>BCCP</b>	<b>TOTAL</b>
ACF	\$118,792	\$482,500	\$601,292
AHCPR*	\$619,000	see note below	\$619,000
AOA	\$49,700	---	\$49,700
CDC	\$492,000	\$20,000	\$512,000
FDA	\$2,293,752	\$91,375	\$2,385,127
HCFA -Internal**	see note below	\$3,400,000	\$3,400,000
HCFA-External**	see note below	\$79,600,000	\$79,600,000
HRSA	\$50,000	---	\$50,000
IHS	\$9,817,600	---	\$9,817,600
NIH***	\$1,033,400	see note below	\$1,033,400
OIG	\$21,000	\$16,000	\$37,000
OS****	\$266,200	---	\$266,200
PSC	\$66,954	\$411,030	\$477,984
SAMHSA	\$10,926	---	\$10,926
<b>TOTAL</b>	<b>\$14,839,324</b>	<b>\$84,020,905</b>	<b>\$98,860,229</b>

## Footnotes Exhibit 5a

\*AHCPR Day One estimate includes the minimally necessary systems infrastructure and labor needed to support Day One setup, testing of plan, and performance on Day One. The infrastructure put in place will also support the possible invocation of the BCCP.

\*\*HCFA included in their BCCP estimate \$.3 million for Day One activities for internal systems and \$2.4 million for Day One activities for external systems.

\*\*\*NIH Day One estimate includes \$611,100 preparation costs for possible invoking of BCCP.

\*\*\*\*The OS estimate includes the costs for the HHS Command Center.

- b. Agencies should ensure that the activities discussed -- those that will be implemented regardless of Y2K-related problems -- are consistent with the assumptions outlined in OMB Memorandum 99-16, "Business Continuity and Contingency Planning for the Year 2000," May 13, 1999. If an agency is using different assumptions to develop its cost estimates, then the agency must explain the assumption and justify their use.

The costs reported in Section VII.3.a - those that will be implemented regardless of Y2K-related problems - only use the assumptions outlined in OMB Memorandum 99-16, "Business Continuity and Contingency Planning for Year 2000," dated May 13, 1999.

- 4. Describe how your agency is coordinating your BCCP with your agency's Continuity of Operations (COOP) planning efforts.

During the development of BCCPs and in the process of finalizing these plans, the Continuity of Operations (COOP) plans are being reviewed to ensure that the plans are coordinated.

VIII Other Management Information.

- 1. Report your estimates of costs associated with Year 2000 remediation, including both information technology<sup>6</sup> costs as well as associated with fixing non-IT systems. Report totals in millions of dollars (For amounts under \$10 million, report to tenths of a million.)
- 2. If there have been dramatic changes in cost, please explain.

Exhibit 6, on the next page, reports estimates of cost associated with Year 2000 efforts.

**Department of Health and Human Services**  
**Y2K Total Cost Estimates - FY 1996 to FY 2000**  
(Dollars in Millions)

	FY 1996	FY 1997	FY 1998	FY 1999	FY 2000	TOTAL
ACF Total	\$ -	\$ 0.500	\$ 3.960	\$ 25.571	\$ 1.101	\$ 31.132
AHCPR Total	-	0.010	0.040	1.795	0.619	2.464
AoA Total	-	0.008	-	0.646	0.050	0.704
CDC Total	-	3.000	9.400	10.855	1.610	24.865
FDA Total	0.200	2.000	7.250	29.502	3.385	42.337
HCFA - Internal	0.700	6.600	17.900	38.500	14.800	78.500
HCFA - External	6.100	6.900	130.200	218.200	218.200	579.600
HCFA - Total	6.800	13.500	148.100	256.700	233.000	658.100
HRSA Total	-	1.200	1.400	12.750	1.900	17.250
IHS Total	-	2.500	2.500	39.930	10.818	55.75
NIH Total	0.040	9.200	11.200	11.725	4.261	36.426
OIG Total	-	0.075	-	5.400	3.487	8.962
OS Total	-	-	0.500	3.580	0.266	4.346
PSC Total	-	0.200	6.500	9.587	1.380	17.667
SAMHSA Total	0.150	0.020	0.020	0.140	0.011	0.341
HHS Total	\$ 7.190	\$ 32.213	\$ 190.870	\$ 408.181	\$ 261.888	\$ 900.342

REVISED: August 9, 1999

**Previous Quarterly Report estimates have changed as follows:**

FY 1999 -- HCFA has identified surplus funds of \$30.9 million, reducing its overall funding level to \$256.7 million. Of the \$30.9 million, \$20.9 million has been redistributed to other OPDIVs for Y2K priority items. The most recent distribution of funds were provided as follows:

HRSA: +\$2.750 M for a variety of Y2K activities, CDC: +\$4.055 million for Renovation, Validation, Implementation, and Embedded Chips, NIH: +\$900,000 to augment Y2K funding in several areas, AoA: +\$45,800 for completion of its testing initiative, PSC: +\$1.304 million for various Y2K activities, and FDA: +\$1.574 million for Emergency Rapid Response activity.

FY 1999 -- PSC's cost estimate increased from last quarterly report as a result of receiving additional supplemental funds.

FY 2000 -- SAMHSA includes an increase of \$11,000 to finance Day One plans for PC/LAN support and applications contractors to conduct testing of systems. This rise also includes overtime pay for some staff.

FY 2000 -- HCFA redistributed funding between cost categories.

FY 2000 -- Includes known costs for Day One and BCCP that will occur regardless of how Y2K affects operations; thus, totals in the FY 2000 column do not necessarily match the cost estimates in the OPDIV quarterly reports.

TOTAL -- HCFA Contingency costs (\$311.2 million) have been re-estimated to \$85.3 million.

NOTE: In some cases, Y2K cost estimates reported represent estimated needs and exceed currently approved funding levels.

3. Described any concerns with availability of key personnel, including ensuring that key staff will be available during the weeks before and after the transition to the Year 2000.

HHS has presented a proposal for Year 2000 Day One Overtime Compensation to the Office of Personnel Management, the President's Council on Year 2000 Conversion, OMB, and other government agencies to further attract and ensure that critical staff are available during the Day One time period.

4. Described any problems that are affecting progress.





**Y2K FEDERAL COSTS FOR STATE-ADMINISTERED PROGRAMS  
CHILDCARE**

STATE	FY 1996	FY 1997	FY 1998	FY 1999	FY 2000
AL				\$38,000	\$38,000
AK					
AZ					
AR		\$12,031	\$150,372	37,593	199,996
CA					
CO					
CT					
DE					
DC					
FL			125,000	1,165,000	1,290,000
GA					
HI					
ID					
IL					
IN			37,500		37,500
IA					
KS			110,000	200,000	70,000
KY					
LA					
ME					
MD			100,000	100,000	100,000
MA	\$290,000	580,000	1,159,000	1,159,000	290,000
MI	290,000	580,000	1,159,000	1,159,000	290,000
MN					
MS					
MO					
MT			20,661	8,862	29,523
NE					
NV					
NH					
NJ					
NM					
NY			100,000	200,000	100,000
NC					
ND					
OH					

**Y2K FEDERAL COSTS FOR STATE-ADMINISTERED PROGRAMS  
CHILDCARE**

STATE	FY 1996	FY 1997	FY 1998	FY 1999	FY 2000
OK					
OR					
PA					
PR					
RI					
SC				\$7,200	\$2,400
SD				4,757	9,656
TN	\$20,500	\$24,600	\$32,800	108,650	20,500
TX					
UT					
VT					
VI					
VA					
WA					
WV			10,000	10,000	5,000
WI					
WY					
<b>TOTAL</b>	<b>\$600,500</b>	<b>\$1,196,631</b>	<b>\$3,004,333</b>	<b>\$4,198,062</b>	<b>\$2,482,575</b>

ND - Has a total of \$19,521 the percentage wasn't specified for State and Federal

OH - Has a total of \$373,000 the percentage wasn't specified for State and Federal.

WY - Has a total of \$100,866

1997 - \$3,326      1998 - \$52,775      1999 - \$30,687      2000 - \$14,078

**Y2K FEDERAL COSTS FOR STATE-ADMINISTERED PROGRAMS  
CHILD SUPPORT ENFORCEMENT**

STATE	FY 1996	FY 1997	FY 1998	FY 1999	FY 2000
AL				\$340,000	\$340,000
AK				65,000	23,000
AZ			\$300,000	100,000	400,000
AR					
CA		\$1,800,000	12,970,000	14,730,000	29,500,000
CO		91,515	420,932	1,306,545	76,380
CT			9,207	34,155	43,362
DE	\$85,500			198,000	198,000
DC					
FL			34,000	2,349,000	51,000
GA					
HI			3,300	140,250	58,080
ID			66,811	70,576	137,387
IL					
IN				485,000	214,500
IA			186,230	173,307	57,769
KS					
KY					
LA			17,000	90,000	107,000
ME					
MD		800,000	800,000	700,000	2,300,000
MA		22,500	230,000	577,000	111,000
MI	31,000	63,000	125,000	125,000	31,000
MN		22,500	230,000	111,000	363,500
MS		66,000	66,000	132,000	264,000
MO			70,000		70,000
MT			115,500	130,584	246,084
NE		195,000	390,000	390,000	97,500
NV					
NH					
NJ					
NM					
NY			100,000	400,000	200,000
NC					
ND					
OH		100,000	100,000	1,400,000	1,600,000

**Y2K FEDERAL COSTS FOR STATE-ADMINISTERED PROGRAMS  
CHILD SUPPORT ENFORCEMENT**

STATE	FY 1996	FY 1997	FY 1998	FY 1999	FY 2000
OK					
OR					
PA					
PR					
RI					
SC					
SD			\$45,021	\$91,406	\$163,712
TN			14,120	318,039	35,591
TX			32,093	2,447,844	2,479,937
UT			200,000	1,100,000	100,000
VT					
VI					
VA				227,279	146,439
WA			260,000	60,000	320,000
WV			9,900	132,000	13,200
WI				300,000	340,000
WY					
<b>TOTAL</b>	<b>\$116,500</b>	<b>\$3,160,515</b>	<b>\$16,795,114</b>	<b>\$28,723,985</b>	<b>\$40,088,441</b>

ND - \$50,733 amount wasn't specified for State and Federal  
WY - \$22,000 amount wasn't specified for State and Federal  
1998-\$8,800 1999-\$6,600 2000-\$6,600

**Y2K FEDERAL COSTS FOR STATE-ADMINISTERED PROGRAMS  
CHILD WELFARE**

STATE	FY 1996	FY 1997	FY 1998	FY 1999	FY 2000
AL				\$230,000	\$230,000
AK					
AZ			\$1,000,000		1,000,000
AR				1,000,000	1,000,000
CA			850,000		850,000
CO			4,490	4,800	9,290
CT					
DE					
DC					
FL					
GA					
HI					
ID			2,636	1,804	4,440
IL					
IN					
IA			91,294	100,292	33,431
KS			60,000	120,000	40,000
KY					
LA		537,000	6,118,000	2,030,000	1,004,000
ME					
MD					
MA					
MI	\$4,000	8,000	15,000	15,000	4,000
MN					
MS				150,000	150,000
MO			200,000	200,000	400,000
MT		2,554	32,296	21,303	56,153
NE					
NV					
NH					
NJ					
NM					
NY			200,000	700,000	700,000
NC					
ND					
OH			600,000		600,000

**Y2K FEDERAL COSTS FOR STATE-ADMINISTERED PROGRAMS  
CHILD WELFARE**

STATE	FY 1996	FY 1997	FY 1998	FY 1999	FY 2000
OK					
OR					
PA					
PR					
RI					
SC		\$10,867	\$12,878	\$120,000	\$150,000
SD			11,679	23,712	35,391
TN					
TX					
UT				90,000	10,000
VT					
VI					
VA					
WA		24,000	46,000	16,000	86,000
WV		5,000	10,000	15,000	2,500
WI				50,000	50000
WY					
<b>TOTAL</b>	<b>\$4,000</b>	<b>\$587,421</b>	<b>\$9,254,273</b>	<b>\$4,887,911</b>	<b>\$6,415,205</b>

ND - \$4,332 the amount wasn't specified for State and Federal

Y2K FEDERAL COSTS FOR STATE-ADMINISTERED PROGRAMS  
LIHEAP

STATE	FY 1996	FY 1997	FY 1998	FY 1999	FY 2000
AL					
AK					
AZ					
AR					
CA	\$257,862	\$187,298	\$18,500	\$15,000	\$478,660
CO					
CT					
DE					
DC					
FL					
GA					
HI					
ID					
IL					
IN					
IA					
KS			740,000	1,400,000	520,000
KY					
LA					
ME					
MD					
MA	25,000	50,000	101,000	101,000	25,000
MI	25,000	50,000	101,000	101,000	25,000
MN					
MS					
MO			300,000		300,000
MT			7,144	250	7,394
NE					
NV			1,400		1,400
NH		4,696	6,817	23,296	21,841
NJ					
NM					
NY			33,333	33,333	33,334
NC			94,800		94,800
ND					
OH				15,000	15,000

**Y2K FEDERAL COSTS FOR STATE-ADMINISTERED PROGRAMS  
LIHEAP**

STATE	FY 1996	FY 1997	FY 1998	FY 1999	FY 2000
OK					
OR					
PA					
PR					
RI					
SC					
SD			\$39,870		\$39,870
TN					
TX			432	\$396	828
UT					
VT	\$15,000	15,000	28,000	35,000	28,000
VI					
VA					
WA					
WV				5,000	5,000
WI			90,000	270,000	30,000
WY					
<b>TOTAL</b>	<b>\$322,862</b>	<b>\$306,994</b>	<b>\$1,562,296</b>	<b>\$1,999,275</b>	<b>\$1,626,127</b>

ND - \$3,697 amount wasn't specified for State and Federal.



Y2K FEDERAL COSTS FOR STATE EXPENDITURES  
MMIS

STATE	FY 1996	FY 1997	FY 1998	FY 1999	FY 2000
AL			\$980,239	\$2,441,132	
AK					
AZ		\$26,300	687,800	350,000	
AR		1,100,000	1,900,000		
CA	\$1,900,000	6,900,000	5,600,000	2,400,000	\$400,000
CO					
CT					
DE			1,197,787	510,286	
DC					
FL					
GA		400,000	3,800,000	2,000,000	6,200,000
HI				1,725,000	
ID					
IL					
IN		3,308	143,851	843,730	212,625
IA			293,552	380,350	
KS		449	352,808	1,189,143	236,119
KY					
LA					
ME					
MD				2,000,000	1,200,000
MA					
MI		541,980	3,326,880	812,970	
MN		100,000	200,000	800,000	500,000
MS			3,227,666		
MO					
MT					
NE		150,000	1,275,000	1,425,000	150,000
NV				200,000	
NH				331,339	189,115
NJ					
NM				4,700,000	
NY	430,000	860,000	2,580,000	430,000	
NC			2,500,000	800,000	
ND					
OH		600,000	500,000	2,000,000	500,000

**Y2K FEDERAL COSTS FOR STATE EXPENDITURES  
MMIS**

STATE	FY 1996	FY 1997	FY 1998	FY 1999	FY 2000
OK					
OR		\$1,200,000	\$5,500,000	\$9,400,000	\$2,200,000
PA					
PR					
RI				30,400	44,000
SC					
SD				150,000	
TN					
TX		840	1,961,634	7,037,522	648,423
UT					
VT					
VI					
VA				5,648,764	405,092
WA			421,000	400,100	
WV	1,248,152	2,491,202	3,398,424	3,670,388	487,971
WI		200,000	300,000	400,000	
WY			205,200	140,719	
<b>TOTAL</b>	<b>\$3,578,152</b>	<b>\$14,574,079</b>	<b>\$40,351,841</b>	<b>\$52,216,843</b>	<b>\$13,373,345</b>

Y2K FEDERAL COSTS FOR STATE-ADMINISTERED PROGRAMS  
TANF

STATE	FY 1996	FY 1997	FY 1998	FY 1999	FY 2000
AL				\$480,000	\$480,000
AK					
AZ			\$300,000		300,000
AR		\$2,225	26,700	6,675	35,600
CA			140,000	5,000,000	150,000
CO		72,175	720,679	1,127,673	57,000
CT		435	35,653	252,769	41,597
DE					
DC					
FL		37,000	2,730,000	2,058,000	2,972,800
GA					
HI			414,782	194,568	128,227
ID					
IL					
IN		75,000	75,000	475,000	1,162,500
IA					
KS			740,000	1,400,000	520,000
KY					
LA			124,000	530,000	654,000
ME					
MD		1,100,000	1,500,000	1,400,000	4,000,000
MA					
MI	\$321,000	643,000	2,570,000	2,570,000	643,000
MN		6,700	65,600	361,800	24,300
MS				450,000	50,000
MO			540,000	240,000	780,000
MT			175,986	123,792	299,778
NE					
NV					
NH					
NJ					
NM					
NY			300,000	800,000	400,000
NC					
ND					
OH		300,000	300,000	600,000	300,000

**Y2K FEDERAL COSTS FOR STATE-ADMINISTERED PROGRAMS  
TANF**

STATE	FY 1996	FY 1997	FY 1998	FY 1999	FY 2000
OK					
OR					
PA					
PR					
RI					
SC		\$43,365	\$193,354	\$270,000	\$150,000
SD			30,134	61,181	91,315
TN			514,135	199,865	714,000
TX		500,000	2,600,000	3,500,000	1,500,000
UT					
VT					
VI					
VA					
WA			22,000	22,000	44,000
WV			16,500	22,000	5,500
WI			280,000	580,000	240,000
WY					
<b>TOTAL</b>	<b>\$321,000</b>	<b>\$2,779,900</b>	<b>\$14,414,523</b>	<b>\$20,873,123</b>	<b>\$15,743,617</b>

ND \$78,779 the breakdown amounts for State and Federal wasn't specified.

WY \$292,036 the breakdown below wasn't specified for State and Federal.

1997-\$9,984      1998-\$158,320      1999-\$86,779      2000-\$36,953

APPENDIX B

Abstract of Plan for Assuring the Year 2000 Readiness of High Impact Federal Programs – August 1999

Agency	Program	Partners for Program Delivery	Milestone Schedule for Key Plan Activities	Beginning and Ending Dates for Testing Systems Operations Between Partners	Have Complementary Business Continuity and Contingency Plans been Developed? If not, When?	Date that Program Event Announcing Completed Process will be Scheduled?
DHHS/ACF	<ul style="list-style-type: none"> <li>• Temporary Assistance for Needy Families (TANF);</li> <li>• Child Care (CC);</li> <li>• Child Welfare (CW);</li> <li>• Child Support Enforcement (CSE); and</li> <li>• Low Income Heating Energy Assistance Program (LIHEAP)</li> </ul>	<p>State and Territorial Agencies that administer the five impact programs TANF, CC, CW, CSE and LIHEAP.</p> <p>The number and type of States &amp; territorial agencies that administer these programs vary across the nation. Agencies include but are not limited to human services departments, revenue departments, State attorney general, and housing departments. In some states (i.e. California) partners include county level agencies.</p>	<ul style="list-style-type: none"> <li>• Contract Awarded on 4/20/99</li> <li>• Planning, Schedule &amp; Training (6/4/99-completed)</li> <li>• Onsite Assessments of Partner Agency Y2K Preparedness (8/24/99 through 09/04/99) -- are currently underway.</li> <li>• Reports resulting from the onsite assessments are in process and will be issued to State/Territorial partners as completed. Deadline for all reports to be issued is mid September.</li> <li>• ACF's technical assistance and guidance strategy for State agencies is currently being developed to address critical concerns of date changes impacting service delivery as identified in the assessments.</li> </ul>	<ul style="list-style-type: none"> <li>• During Onsite Assessments (05/24/99 through 09/17/99)</li> <li>• Verified the issuance of program funds through DHHS and Federal Reserve System to Major Banking Institutions.</li> <li>• Currently verifying State and territorial agencies access to those major banking institutions.</li> </ul>	<ul style="list-style-type: none"> <li>• Assessment of State and territorial BCCPs currently underway.</li> <li>• Initial ACF BCCP and Day 1 Plans completed 04/09/99.</li> <li>• Ongoing review continues to date.</li> <li>• Plans will be reviewed and revised as additional information is obtained from partner agencies during onsite assessments.</li> <li>• Qtrly issuance of Agency BCCP/Day 1 Plans (06/15/99) – completed 6/7/99</li> <li>• Qtrly Issuance of Agency BCCP/Day 1 Plans (09/15/99)</li> <li>• Final Issuance of Agency BCCP/Day 1 Plans (12/15/99)</li> <li>• Not necessary</li> </ul>	<p>Announce completion of Onsite Assessments of State Agency Y2K Preparedness. (09/27/99)</p> <p><i>Proposed:</i> Interactive panel with State partners through internet technology.</p>
Grants Payment Process		States and other local levels of grantee partners	Working Group Meeting June 30, 1999-completed	August 5, 1999 (simulate 3/3/2000) – completed August 11, 1999 (simulate 2/29/2000)	Not necessary	TBD

CDC Abstract of Plan for Assuring the Year 2000 Readiness of High Impact Federal Programs - August 1999

Agency	Program	Partners for Program Delivery	Milestone Schedule for Key Plan Activities	Beginning and Ending Dates for Testing Systems Operations Between Partners	Have Complementary Business Continuity and Contingency Plans been Developed? If not, When?	Date that Program Event Announcing Completed Process will be Scheduled?
Disease Monitoring	Public Health Laboratory Information System	State and Territorial Public Health Laboratories	Planned Test Date and Site: May 1999 at Mississippi State Health Department	May 6-13, 1999. Test completed and successful.	Not necessary.	Not necessary.
Disease Monitoring	National Molecular Subtyping Network for Foodborne Disease Surveillance	Four State public health labs, a USDA lab, and an FDA lab.	May 1999 at Virginia State Health Lab	May 25, 1999 Test completed and successful	Not necessary.	Not necessary.
Vaccine Ordering and Financial management & payments	Vaccines for Children Data System	State Health Departments, vaccine manufacturers, U.S. Treasury	State of Georgia. May 1999	May 17-28, 1999 7/27/1999 - TOPS successfully processed all test transactions.	Yes	Not necessary.
Disease Monitoring	Vaccine Adverse Event Reporting System	Healthcare providers, State public health agencies, FDA	At contractor (McKesson) site. May 1999	May 10-11, 1999. Test completed and successful.	Not necessary.	Not necessary.
Financial management & payments	Total Online Processing System (TOPS)	HHS/FSC, Treasury	Off-site Disaster Recovery Site. May 28, 1999	May 28, 1999 7/27/1999 Transactions successfully generated. Test completed.	Yes	Not necessary.
Beneficiary payments & Financial management & payments	Tuskegee Study Billing and Tracking System	Tuskegee beneficiaries, healthcare providers, U.S. Treasury	At CDC. May 1999	7/27/1999 - TOPS successfully processed all test transactions.	Not necessary.	Not necessary.

HCFA Abstract of Plan for Assuring the Year 2000 Readiness of High Impact Federal Programs – August 1999

Agency	Program	Partners for Program Delivery	Milestone Schedule for Key Plan Activities	Beginning and Ending Dates for Testing Systems Operations Between Partners	Have Complementary Business Contingency Plans been Developed? If not, When?	Date that Program Event Announcing Completed Process will be Scheduled?
HCFA	Medicare	Medicare contractors	<p>Medicare contractors certify their systems by April 1999 – completed</p> <p>Recertify by November 1999</p> <p>Submit BCCPs to HCFA for initial review by April 1999 - completed</p> <p>Submit revised BCCPs to HCFA for re-review by July - completed</p> <p>Submit Day One plans by end of July 1999 - completed</p> <p>Onsite Assessments of State Y2K Readiness</p> <p>First Round of site visits by April 30 – completed</p> <p>Second Round of site visits – May through mid-September –have begun</p> <p>Third Round of site visits – Sept through Dec</p> <p>States to submit BCCPs to HCFA for review by June 1 – all States have responded</p> <p>Working Group Meeting June 30, 1999 -completed</p>	<p>July 1, 1999 through October 31, 1999</p>	<p>HCFA will review Medicare Contractor BCCPs – May – completed</p> <p>BCCPs which needed revisions were reviewed in July/August – completed</p>	TBD
	Medicaid	States	<p>First Round of site visits by April 30 – completed</p> <p>Second Round of site visits – May through mid-September –have begun</p> <p>Third Round of site visits – Sept through Dec</p> <p>States to submit BCCPs to HCFA for review by June 1 – all States have responded</p>	<p>During onsite assessments HCFA will determine whether States are testing with partners (May-Sept)</p>	<p>HCFA will review State BCCPs – ongoing process</p> <p>HCFA will provide technical assistance as need is identified in the review of State BCCPs.</p>	TBD
	Grants Payment Process for Medicaid	States	<p>Working Group Meeting June 30, 1999 -completed</p>	<p>August 5, 1999 (simulate 3/3/2000) –completed</p> <p>August 11, 1999 (simulate 2/29/2000)</p>	<p>Not necessary</p>	TBD



Health Resources and Services Administration  
 Year 2000 Readiness of High Impact Federal Program  
 Abstract Plan Report  
 August 1999

Agency	Program	Partners for Program Delivery	Milestone Schedule for Key Plan Activities	Beginning and ending Dates for Testing Systems Operations Between Partners	Have complementary Business continuity and contingency Plans been Developed? If Not when?	Date that Program Event Announcing Completed Process will be scheduled
HRSA	Organ Transplantation: OPTN - Mission Critical System (waitlist and matching programs)	HRSA partner: United Network for Organ Sharing (UNOS)  UNOS partners: 61 Organ Procurement Organizations; 272 Transplant Centers; 159 Histocompatibility Labs	OPTN compliance - Jan 1999  IV & V completion - May 10, 1999  On-Site Regional Systems Demos - Sept. 1998 - June 1999 -completed  Training Workshops - Spring 1999 - completed  BCCP - July 1999  Day One Business Resumption Plan - June 1999 -completed  Public Awareness Campaign - Ongoing	June 1999 - August 1999  End-to-End Testing scheduled for completion - August 1999	Completion date - July 1999  Day One Business Resumption Plan - June 1999 -completed	IV & V - May 1999  Press Release announcing OPTN compliance - May 21, 1999  Announcement of end-to-end testing completion - TBD

IHS Abstract of Plan for Assuring the Year 2000 Readiness of High Impact Federal Programs - August 1999

Agency	Program	Partners for Program Delivery	Milestone Schedule for Key Plan Activities	Beginning & Ending Dates for Testing System Operations Between Partners	Have Complementary BCCP been Developed? If not, when?	9/99 that Program Event Announcing Completed Process Will be Scheduled?
IHS	Indian Health Services	American Indian Tribes Alaska Indian Health Programs Urban Indian Health Programs Tribal Organizations	Systems NPIRS - 3/29/99 RPMS - 6/30/99 Critical Infrastructure Biomedical - 10/1/99 Facilities - 10/1/99 PCs - 10/4/99 Telephones - 12/30/99 Telecommunications - 9/30/99	RPMS Begin: 1/1/99 Ending: 9/31/99 Arizona Medicaid FI - 6/10/99 - completed Blue Cross/Blue Shield of Texas (Medicare FI) - 5/6/99 - completed New Mexico Medicaid Fiscal Intermediary - 7/16/99 - completed North Carolina Medicaid Intermediary - 6/10/99 - completed North Dakota Medicaid Intermediary - 6/10/99 - completed South Dakota Medicaid Intermediary - 6/10/99 - completed Arizona Medicaid Fiscal Intermediary - Inpatient Encounters - 6/10/99 - completed PNC Bank - 7/6/99 - completed U.S. Treasury Financial Management Service - 9/30/99 Internal Revenue Service - 1/1/99 - completed	Complete BCCP - 8/31/99 Test BCCP - 9/30/99 IHS developed BCCP templates designed to allow each respective Area, Site or Medical Facility to identify and define core business processes that are dependent upon laboratory equipment, biomedical devices, infrastructure components, telecommunications resources, and RPMS software and computer equipment.	National - 9/99 Alaska - 9/99 Aberdeen - 9/99 Albuquerque - 9/99 Bernidji Area - 9/99 Billings Area - 9/99 California - 9/99 Navajo - 9/99 Nashville - 9/99 <sup>1</sup> Oklahoma - 9/99 Phoenix - 9/99 Portland - 9/99 Tucson - 9/99



DEPARTMENT OF HEALTH &amp; HUMAN SERVICES

Office of the Secretary

Washington, D.C. 20201

MAY 14 2000

The Honorable Stephen Horn  
Chairman  
Subcommittee on Government Management,  
Information and Technology  
Committee on Government and Reform  
United States House of Representatives  
Washington, D.C. 20515-6143

Dear Mr. Chairman:


Enclosed is the Department of Health and Human Services' Year 2000 May Quarterly Report and the April monthly progress report.

We are pleased to show 282 mission critical systems out of the Department's 284 systems, or 99 percent, are compliant. The Health Care Financing Administration has reported all of its 25 internal mission critical systems and all of its 75 external mission critical systems as compliant.

We would also like to highlight the progress of non-mission critical systems and interfaces:

- 98 percent of the Department's 871 non-mission critical systems are compliant;
- 100 percent of the Department's 1,141 State interfaces are compliant; and
- 99 percent of the Department's 146,053 total mission critical and non-mission critical external interfaces are compliant.

If your staff have any questions on these materials, please have them call Ms. Gay Morris, our Year 2000 Program Manager, on (202) 690-6376.

Sincerely,  
  
John J. Callahan  
Assistant Secretary for Management  
and Budget/Chief Information Officer

Enclosure



DEPARTMENT OF HEALTH &amp; HUMAN SERVICES

Office of the Secretary

Washington, D.C. 20201

MAY 14

The Honorable Robert F. Bennett  
Chairman  
Senate Special Committee on the Year 2000 Technology Problem  
United States Senate  
Washington, D.C. 20510-6486

Dear Mr. Chairman:

Enclosed is the Department of Health and Human Services' Year 2000 May Quarterly Report and the April monthly progress report.

We are pleased to show 282 mission critical systems out of the Department's 284 systems, or 99 percent, are compliant. The Health Care Financing Administration has reported all of its 25 internal mission critical systems and all of its 75 external mission critical systems as compliant.

We would also like to highlight the progress of non-mission critical systems and interfaces:

- 98 percent of the Department's 871 non-mission critical systems are compliant;
- 100 percent of the Department's 1,141 State interfaces are compliant; and
- 99 percent of the Department's 146,053 total mission critical and non-mission critical external interfaces are compliant.

If your staff have any questions on these materials, please have them call Ms. Gay Morris, our Year 2000 Program Manager, on (202) 690-6376.

Sincerely,

A handwritten signature in black ink, appearing to read "John J. Callahan".

John J. Callahan  
Assistant Secretary for Management  
and Budget/Chief Information Officer

Enclosure



THE DEPUTY SECRETARY OF HEALTH AND HUMAN SERVICES  
WASHINGTON, D.C. 20201

MAY 13 1999

The Honorable Jacob Lew  
Director  
Office of Management and Budget  
Washington, D.C. 20503

Dear Mr. Lew:

Enclosed is the Department of Health and Human Services' May Quarterly Report regarding our progress on the Year 2000 date issue. The high rates of compliance in many areas demonstrate the success of the Department's hard work on the Year 2000 Conversion Project.

We are pleased to show 282 mission critical systems out of the Department's 284 systems, or 99 percent, are compliant. The Health Care Financing Administration has reported all of its 25 internal mission critical systems and all of its 75 external mission critical systems as compliant.

We would also like to highlight the progress of non-mission critical systems and interfaces:

- 98 percent of the Department's 871 non-mission critical systems are compliant;
- 100 percent of the Department's 1,141 State interfaces are compliant; and
- 99 percent of the Department's 146,053 total mission critical and non-mission critical external interfaces are compliant.

Your staff may address any questions or suggestions to either Kerry Weems, HHS' Acting Deputy Assistant Secretary for Information Resources Management/Deputy CIO, at (202) 690-6162, or Gay Morris, Year 2000 Program Manager, at (202) 690-6376.

Sincerely,

Kevin Thum

Sincerely,

John J. Callahan  
Assistant Secretary for  
Management and Budget/  
Chief Information Officer

Enclosure

Status of Health and Human Services Year 2000 Efforts:  
Quarterly Progress Report  
 May 15, 1999

- i. Overall Progress. Provide a report of the status of agency efforts to address the year 2000 problem, which includes an agency-wide status of the total number of mission-critical systems.

Exhibit 1 presents compliance status and strategies for all HHS Mission Critical Systems by OPDIV as of April 30, 1999.

<b>Exhibit 1 - Overall Progress as of April 30, 1999</b>					
AGENCY	Total Number of Mission-Critical Systems	Number Compliant	Number to be Replaced	Number to be Repaired	Number to be Retired
HHS	290	282	0	2	6
ACF	45	45	0	0	0
AHCPR	0	0	0	0	0
AOA	2	2	0	0	0
CDC	66	63	0	0	3
FDA	34	34	0	0	0
HCFA Internal	25	25	0	0	0
HCFA External	78	75	0	0	3
HRSA	5	5	0	0	0
IHS	5	4	0	1	0
NIH	14	14	0	0	0
OIG	3	3	0	0	0
PSC	8	7	0	1	0
SAMHSA	5	5	0	0	0

**Total Number of Mission Critical Systems**

The total number of mission critical systems, including those to be retired, is 290 systems. This is a decrease of four systems from the 294 reported in the February Quarterly Report because HCFA retired four external systems previously scheduled to be retired. Excluding the six systems still to be retired, a total of 284 mission critical systems must be operational into the next

millennium. This is a decrease of 3 systems from the 287 mission critical systems reported in the February Quarterly Report. The change is because HCFA will retire three external mission critical systems that were previously scheduled for repair. The three systems are being retired because three contractors are leaving the Medicare program. Their workloads are being transitioned to Y2K-compliant contractors.

**Total Number of Compliant Mission Critical Systems**

As of April 30, 1999, the total number of compliant mission critical systems has increased from December 31, 1998 by 39 systems to a total of 282 systems. The increase is due to the following increases of compliant mission critical systems:

- CDC increased by six,
- FDA increased by four,
- HCFA (External) increased by twenty-one,
- HRSA increased by one,
- NIH increased by two,
- PSC increased by four, and
- SAMHSA increased by one.

II. Progress of Systems Under Repair. Provide a report of the status of agency efforts to address the year 2000 problem which includes the status of systems under repair.

- a. In the first row, indicate the dates your agency has set for completing each phase. In each report, restate these dates and indicate if there has been a change.

Exhibit 2, on the next page, reports the milestones and the progress of systems under repair, as of April 30, 1999. The milestone records the date on which the last mission critical system within an OPDIV is expected to complete each phase. It does not, therefore, demonstrate typical progress nor indicate the level of accomplishment in each phase prior to organization-wide completion of this phase.

Dates in italics indicate milestones that have changed since the last report.

Exhibit 2 - Progress of Systems Under Repair as of April 30, 1999					
	Total No. Mission Critical Systems	Assessment	Renovation	Validation	Implementation
ACF Milestones	//////////	Dec. 1996	Sept. 1998	Dec. 1998	Dec. 1998
Current Number Complete	3	3	3	3	3
CDC Milestones	//////////	Jan. 1997	Dec. 1998	Dec. 1998	Mar. 1999
Current Number Complete	15	15	15	15	15
FDA Milestones	//////////	April 1997	Mar. 1999*	Mar. 1999*	Mar. 1999*
Current Number Complete	20	15	20	20	20
HCFA Milestones Internal	//////////	June 1998	Oct. 1998	Dec. 1998	March 1999
Current Number Complete - Internal	25	25	25	25	25
HCFA Milestones External	//////////	June 1998	Dec. 1998	Mar. 1999	Mar. 1999
Current Number Complete - External	75**	82***	75	75	75
HRSA Milestones	//////////	Dec. 1997	May 1998	Oct. 1998	Dec. 1998
Current Number Complete	1	1	1	1	1
IHS Milestones	//////////	Sept. 1998	Jan. 1999	Mar. 1999	June 1999
Current Number Complete	1	1	1	1	0
NIH Milestones	//////////	Sept. 1997	Dec. 1998	Dec. 1998	March 1999
Current Number Complete	10	10	10	10	10
PSC Milestones	//////////	June 1998	Sept. 1998	Mar. 1999	June 1999
Current Number Complete	6	6	6	5	5
SAMHSA Milestones	//////////	Sept. 1998	Nov. 1998	Dec. 1998	Dec. 1998
Current Number	1	1	1	1	1



Exhibit 2 Footnotes:

\*The milestone date was modified this quarter to reflect the change of three systems' strategy from replace to repair.

\*\*The total number of mission critical external systems to be repaired decreased from 78 to 75, because three systems previously identified for repair will be retired. This reflects the fact that three contractors are leaving the Medicare program. Their workloads are being transitioned to Y2K-compliant contractors.

\*\*\*Four systems were retired and this quarter three more are scheduled to be retired, leaving HCFA with a total of 75 mission critical systems in this category.

- b. Provide a description of progress for fixing or replacing mission-critical systems. (former 2c1.) Please ensure that your report on the completion of phases is consistent with the CIO Council's best practices guide and GAO's assessment guide, Year 2000 Computing Crisis: An Assessment Guide.

Exhibit 2b reports progress on repair and replacement of mission critical systems by OPDIV as of April 30, 1999.

<b>Exhibit 2b - Total Mission Critical Systems as of April 30, 1999</b>			
<b>OPDIV</b>	<b>Total Number Mission Critical</b>	<b>Total Number Compliant</b>	<b>Percent Compliant</b>
ACF	45	45	100%
AHCPR	0	-	-
AOA	2	2	100%
CDC	63	63	100%
FDA	34	34	100%
HCFA - Internal	25	25	100%
HCFA - External	75*	75	100%
HRSA	5	5	100%
IHS	5	4	80%
NIH	14	14	100%
OIG	3	3	100%
OS	0	-	-
PSC	8	7	87.5%
SAMHSA	5	5	100%
<b>TOTAL</b>	<b>284</b>	<b>282</b>	<b>99%</b>

\* HCFA will retire three systems originally under repair, decreasing the total number from 78 to 75 systems, because three contractors are leaving the Medicare program. Their workloads are being transitioned to Y2K-compliant contractors.

Exhibit 2b Note - The number of systems is the total number of mission critical systems minus those being retired. The total number of mission critical systems compliant includes mission critical systems originally assessed as compliant plus those systems that have been repaired or replaced and are now compliant.

#### Increases in Compliant Mission Critical Systems

As of April 30, 1999, 99 percent of HHS's mission critical systems are compliant. This percentage increased by approximately 14 percentage points from 85 percent reported in the February Quarterly Report. Between December 31, 1998 and April 30, 1999, 39 additional mission critical systems were made Y2K compliant, through either repair or replacement.

- c. Provide a description of progress in fixing non-mission critical systems, including measures that demonstrate that progress.

#### Non-Mission Critical Systems

The primary focus for achieving Y2K compliance has been on mission critical systems. HHS has 886 non-mission critical systems. Of these, 871 or 98 percent are compliant. This is an increase of 10 percent since the February Quarterly Report. Exhibit 2d, below, lists the number of non-mission critical systems by OPDIV and the number compliant as of April 30, 1999.

Exhibit 2c - Non-Mission Critical Systems As of 4/30/99			
OPDIV	Total Number of Non-Mission Critical Systems	Total Number of Compliant Non-Mission Critical Systems	Percent Compliant
ACF	17	17	100%
AHCPR	1	0	0%
AOA	5	5	100%
CDC	136	136	100%
FDA	234	234	100%
HCFA-Internal	56	56	100%
HCFA-External	5	5	100%
HRSA	9	9	100%
IHS	3	1	33%
NIH	345	340	98%
OIG	3	0	0%
OS	45	42	93%
PSC	17	16	94%
SAMHSA	10	10	100%
<b>HHS Total</b>	<b>886</b>	<b>871</b>	<b>98%</b>

- d. Provide a description of the status of efforts to inventory all data exchanges with outside entities and the method for assuring that those organizations will be or have been contacted, particularly State governments. Provide a description of progress on making data exchanges compliant.

**State Interfaces**

All OPDIVs have compiled inventories of system interfaces, including data exchanges with private sector partners, States, and local and Tribal governments. HHS has a total of 1,141 State interfaces. Of the HHS total number of State interfaces, 1,141 or 100 percent of the interfaces are compliant. This is an increase of twenty-three percentage points from the 77 percent reported in the February Quarterly Report.

The Department provided a listing of State interfaces to the National Association of State Information Resources Executives (NASIRE) on April 22, 1998. The Department has updated monthly the status of the State interfaces listed on the GSA website.

Exhibit 3, below, lists the number of State interfaces by OPDIV and the number currently compliant.

<b>Exhibit 3 "Summary of Mission Critical and Non-Mission Critical State Interfaces by OPDIV"</b>				
<b>OPDIV</b>	<b>Number of Systems</b>	<b>Number of State Interfaces</b>	<b>Number Compliant</b>	<b>Percentage Compliant</b>
ACF	5	270	270	100%
CDC	12	321	321	100%
HCFA - Internal	3	325	325	100%
HCFA - External	35	182	182	100%
IHS	2	8	8	100%
PSC	2	35	35	100%
<b>Total</b>	<b>65</b>	<b>1,141</b>	<b>1,141</b>	<b>100%</b>

**Total External Interfaces**

HHS has a total of 146,053 external interfaces, of which HCFA accounts for 97 percent or 142,015 of these interfaces. Currently, 146,051 or 99 percent of the total number of interfaces are compliant. This is an increase of 15 percent from the 84 percent reported in the February Quarterly Report.

The reported number of HCFA data exchanges decreased substantially from the number reported in the February Quarterly Report due to HCFA's extensive verification and validation of the information that has been reported in the monthly data exchange reports from Medicare

contractors. This work has eliminated duplicative data. Furthermore, HCFA has verified that the reports describe real physical exchanges of data rather than the number of providers affected by the business transaction. For example, a real physical data exchange between HCFA and a billing agent is one data exchange though it may have previously been reported as hundreds of providers represented by the billing agent.

OPDIVs have contacted exchange partners to communicate the use of the National Institute of Standards and Technology (NIST) four-digit year or to establish agreements for other arrangements. The OPDIVs that have non-compliant data exchanges continue to update the compliance status of their data exchanges.

Exhibit 4, below, lists the total number of external interfaces for mission critical and non-mission critical systems by OPDIV and the number compliant.

<b>Exhibit 4 "Total Mission Critical and Non-mission Critical Systems with External Interfaces by OPDIV as of 4/30/99"</b>				
<b>OPDIV</b>	<b>Number of Systems</b>	<b>Number of External Interfaces</b>	<b>Number Compliant</b>	<b>Percentage Compliant</b>
ACF	5	270	270	100%
CDC	25	381	381	100%
FDA	1	1	1	100%
HCFA - Internal	24	3,209	3,209	100%
HCFA - External	71	142,015	142,015	100%
IHS	7	12	10	83%
NIH	5	61	61	100%
PSC	9	104	104	100%
<b>Total</b>	<b>147</b>	<b>146,053</b>	<b>146,051</b>	<b>99%</b>

- e. Provide a description of efforts to address the year 2000 problem in other areas, including biomedical and laboratory equipment and any other products or devices using embedded chips.

**Biomedical Equipment Clearinghouse**

HHS chairs the CIO Council's Biomedical Equipment Subcommittee. As a member of the Subcommittee, FDA has targeted 1,932 manufacturers whose medical devices are most likely to have a Y2K issue.

As of April 12, 1999, 1,549 of those manufacturers have submitted data to the web site, with the following Y2K compliance status:

- Products all compliant - 441
- Products that do not use a date - 678
- Products with date-related problems - 260
- Product status specified at manufacturer's web site (assumption is that there are some non-compliant products) - 219
- Other - 50 (there were questions regarding the submitted data that require follow up by FDA)
- Non-respondents - 284

The database currently contains data from over 4,300 manufacturers; the majority of manufacturers that make Y2K-vulnerable products have reported product status, including all members of Health Industry Manufacturers Association (HIMA) who manufacturer such products. The HIMA membership accounts for over 90% of the biomedical equipment sales in the U.S., based on dollars.

**HHS Embedded Systems**

Exhibit 5, below, lists the number of embedded systems that the OPDIVs have identified, as well as the number that have been assessed and the number currently compliant. As shown in the table, HHS has inventoried 26,905 embedded systems and assessed 26,229 systems. Currently, 24,429 or 91 percent of these are compliant.

<b>Exhibit 5 - Embedded Systems</b>			
<b>OPDIV</b>	<b>Number</b>	<b>Number Assessed</b>	<b>Number Compliant</b>
ACF*	1	1	1
CDC	1,009	1,009	931
FDA	1,666	1,666	1,480
HCFA*	2	2	0
IHS	23,298	22,622	21,108
NIH**	929	929	909
<b>Total</b>	<b>26,905</b>	<b>26,229</b>	<b>24,429</b>

Exhibit 5 Footnotes

\* The embedded systems are building security systems.

\*\*Ten systems are building systems.

Because of HHS's focus on health care and scientific research, HHS's primary concern regarding embedded chips is biomedical equipment, which includes medical devices and scientific laboratory equipment. A very small number of building security systems with embedded chips are included in this inventory. In some cases, embedded systems are listed as compliant based on manufacturer's certification. A sample of these systems will undergo verification testing to confirm Y2K compliance.

CDC has completed the assessment of their inventory of laboratory equipment. Remediation of the 78 remaining non-compliant pieces of equipment is scheduled for completion by the end of June, 1999. FDA has assessed their scientific and laboratory equipment and determined that all of the pieces of equipment are "stand-alone" and are not used for biomedical applications or other integrated analytical or IT systems. Also, the dating functions are, for the most part, limited to display and printing purposes. FDA's target date for ensuring its scientific equipment can function in the Year 2000 is the end of September 1999.

IHS has completed its inventory and assessment. A small percentage (4.7 percent) of devices need additional research to determine their compliance status. IHS has targeted the most prevalent high-risk devices in their hospitals and health clinics for immediate repair and replacement. Business continuity and contingency planning modules for various classes of devices are being developed for dissemination to local programs.

NIH Clinical Center equipment inventories are complete. Department Chiefs are reviewing remediation strategies for the identified noncompliant equipment. Signed certification forms from Principal Investigators indicating that they have judged the potential Y2K impact on their date/time-sensitive equipment, and have taken necessary remediative actions are required from all NIH components. NIH has also planned audit activities that will have an emphasis on high-risk areas. Furthermore, NIH has initiated activities to assist NIH scientists for ensuring compliance of biomedical equipment, including meeting with Scientific Directors to discuss the overall compliance strategy and assisting Principal Investigators (PIs) by providing guidance, resources, and tools to collect data, and assess and remediate equipment.

- f. Provide a description of efforts to address the year 2000 problem for buildings that your agency owns or manages. If your buildings are owned or managed by GSA, you do not have to report on those buildings. Please indicate instead whether or not you are a member of the Building Systems Working Group of the Year 2000 Subcommittee of the CIO Council.

### Facilities

Exhibit 6, on the next page, lists the number of facilities owned, direct leased, GSA delegated, and tribally managed for each OPDIV as well as the number assessed and the number currently compliant. Facilities include office buildings, laboratories, hospitals, clinics, central utility buildings, support buildings, and housing. As shown in the table, HHS has completed the inventoried of its 3,729 buildings. Currently 3,420 or 92 percent of these are Y2K compliant. The number of facilities reported in all categories has increased significantly to reflect an ongoing outreach program by the Indian Health Service to assist in evaluating and remediating activities for the 2,404 tribally owned and leased buildings.

<b>Exhibit 6 - Buildings</b>			
<b>OPDIV</b>	<b>Number</b>	<b>Number Assessed</b>	<b>Number of Facilities Compliant</b>
CDC	213	213	213
FDA	76	76	74
IHS	3,165	3,165	3,131
NIH	271	271	See Narrative Below
OS	1	1	1
PSC	3	3	3
<b>Total</b>	<b>3,729</b>	<b>3,729</b>	<b>3,420</b>

NIH has completed the assessment of its facilities related equipment in NIH-owned and NIH-leased buildings. In NIH-owned properties, systems that control building automation, heating, ventilation and air conditioning (HVAC), fire alarm panels, and other infrastructure support do not function independently in individual buildings, but are networked into a campus-wide system. Consequently, the NIH "Number of Facilities Compliant" is misleading. NIH has assessed its ten building systems affected by embedded microchips and found eight to be compliant based on manufacturers' certification. Verification testing is on-going and is scheduled to be completed by June 1999. The vendor for the two non-compliant systems (lighting control and HVAC) expects to have all components of the systems upgraded to be Y2K compliant by June 1999. Until remediation activities have been completed on these remaining two systems NIH cannot consider any of its owned facilities compliant.

During the previous quarter, CDC completed remediation activities in all 213 buildings for which it has responsibility. Work is continuing with building managers and lessors to determine responsibility and staffing requirements to ensure full functionality of all facilities on January 1, 2000.

IHS has completed assessment activities for facilities it owns and all tribally-owned or tribally-leased facilities. The results of this work indicate that only 3% of the equipment evaluated were date sensitive with 1% non-compliant and the remaining 2% operating equipment satisfactorily but with reports and displays outputted by these systems being affected. Of the forty-nine hospitals under IHS oversight, thirteen were found to have building automation systems that are non-compliant. Remediation actions have been initiated. Twenty-one of the 261 health centers evaluated were also found to have non-compliant systems or ones that produced faulty reports and displays.

FDA continues to work towards correcting deficiencies in its two remaining non-compliant laboratories. The revised target date for completion is now May 30, 1999.

HHS continues to be represented on the Building Systems Working Group of the Year 2000 Subcommittee of the CIO Council.

- g. Provide a description of efforts to address the year 2000 problem in the telecommunications systems that your agency owns or manages. If your systems are owned or managed by GSA, you do not have to report on those systems. Please indicate instead whether or not you are a member of the Telecommunications Working Group of the Year 2000 Subcommittee of the CIO Council.

#### **Telecommunications**

As previously reported, much of the HHS telecommunications services and equipment, both long distance and local, are provided by contracts managed by the General Services Administration (GSA). The contracts that provide the bulk of these services are the Federal Telecommunications Service 2000 (FTS2000) and the Washington Interagency Telecommunications Service 99 (WITS-99). The FTS2000 contract expired in December 1998 and the WITS contract expired in January 1999. GSA has extended FTS2000 to January 2001 and WTS-99 to July 1999. The follow-on contracts to FTS2000 and WTS-99 specify that the successful vendors will be Y2K compliant prior to final award.

ACF, CDC, FDA and SAMHSA have completed their telecommunications effort as of March 31, 1999.

AHCPR's voice mail system and all of its hubs are compliant. AHCPR has one compliant router and the second router will be Y2K compliant in September 1999.

HCFA continued its progress in the area of telecommunications readiness during the past quarter. HCFA developed ten risk mitigation/contingency plans in five major areas of voice and data communications services. In conducting that work HCFA obtained Y2K readiness briefings/updates from AT&T and GSA, which provide voice services to HCFA offices in the regions and Washington, D.C. Given the rather general nature of the GSA plans at this time, HCFA developed specific plans to assess its progress at various points throughout 1999.

Conversion of dial-up mainframe users from non-compliant Renex protocol converter service to IBM Global Services (IGS) and the Medicare Data Communications Network (MDCN) moved ahead with HCFA taking advantage of the conversion to enhance network security. This new process provides an encrypted logon between end-users and their local IGS point-of-presence, and a secure login to the hcfa.gov domain, so that both the mainframe logon and the mainframe session are encrypted. To date over 800 dial-up users have been registered in the new system.

HCFA has established independent Y2K test environments at seven sites for testing the Medicare standard/shared systems. All required connectivity between those sites, HCFA, and HCFA's independent testing contractor is running over a separate Y2K compliant sub-network. In January, and again in March, 1999, the entire Y2K sub-net was tested using Y2K scenarios; once being IPL'd (future date advanced in a future date environment) into 2000 and once IPL'd to 12/29/99 and allowed to run into 2000. The network (circuits, switches, routers, and associated management software for access, authorization, routing and auditing) operated successfully on all dates without any problems encountered in sending or receiving data. As the sub-net uses the



same devices and software as the production data wide area network, HCFA has been able to independently test the network itself.

IHS' non-compliant Telematics routers will be replaced to support Frame Relay or point-to-point where available. Sites requiring X.25 will be converted to MCI or SPRINT for X.25 support. IHS has an IDIQ contract, which allows for the purchase of replacement routers. IHS, with assistance from HHS, is in the process of developing a plan to replace the AT&T X.25 service using the FTS2001 contract. As AT&T plans to drop X.25 service as of September 30, 1999, IHS will first convert to SPRINT X.25 using the FTS2000 contract then convert to the FTS2001 X.25 services using either SPRINT or MCI at a later date.

NIH's Center for Information Technology (CIT) provides the networking infrastructure (NIHnet Backbone) that supports all of NIH. The NIHnet Backbone provides the connectivity for the Institutes and Centers (Ics) Local Area Networks. Most of NIH's networking hardware and software that are date dependent are compliant. For non-compliant components, remediation efforts are underway and are expected to be completed by the end of July 1999. Most of NIH's voice telecommunications services and products are provided by the DHHS contract entitled DHHS Program Support Center (PSC) Telecommunications Improvement Project (TIP). NIH is working with PSC to ensure that everything covered by the TIP contract will be compliant.

PSC's 5ESS Telephone Switch, the Wide Area Network (WAN), and the PSC LAN Servers are Y2K compliant. The IV&V certification process for the Switch and network communications has been completed. PSC's Octel Voice Mail system is also Y2K compliant.

Most of HRSA's PBXs, switches and routers, and all the voice mail systems are operated by PSC. HRSA completed assessment of its internal systems in October 1998 and is replacing non-compliant systems.

- h. Provide a description of the status of the year 2000 readiness of each government-wide system operated by your agency (e.g., GSA will report on FTS 2000).

HHS operates no government-wide systems.

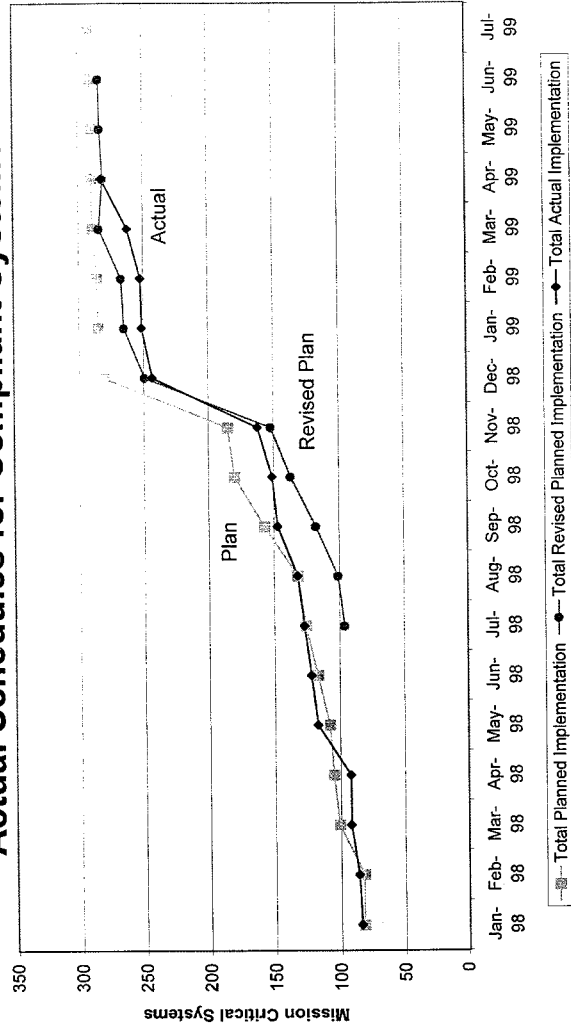
- i. Please include any additional information that demonstrates your agency's progress. This could include charts or graphs indicating actual progress against your agency's schedule, lists of mission critical systems with schedules, success stories, or other presentations.

#### **Tracking of Planned versus Actual Progress**

HHS tracks its actual progress against its planned progress for the implementation of mission critical systems. Exhibit 7, on the next page, shows actual as well as planned progress based on monthly system inventory reports provided to the Department by each OPDIV. As shown in the graph, HHS' progress is only slightly behind its ambitious planned schedule, but now much more clearly on track to avert systems problems arising from the millennium date change. Most planned implementation dates for repaired or replacement systems were clustered around December 31, 1998. The data shows that this has been a critical and successful period of risk reduction in the HHS Y2K program. Similar graphs are maintained for each OPDIV.

# HHS Year 2000

## Mission Critical Implementation Planned and Actual Schedules for Compliant Systems



**Y2K Outreach**

The Department chairs two Sector Outreach Committees of the President's Council for Year 2000 Conversion: the Health Care Sector Outreach Committee, led by HCFA, and the Human Services Sector Outreach Committee, led by ACF. Every three weeks these committees meet with their partners and providers to discuss goals and activities, and with the Deputy Secretary and the Chief Information Officers to report on accomplishments and raise issues. Periodically, the Deputy Secretary meets with the all OPDIV Heads to discuss Y2K issues, including outreach. In addition he has met, and will continue to meet, with the Chief Executive Officers of the health care associations (e.g., American Medical Association, American Hospital Association).

**Health Care Sector**

The Health Care Sector is composed of representatives of HHS (i.e., CDC, FDA, HCFA, IHS, and NIH) and the Department of Agriculture, the Department of Defense, the Department of Labor, the Department of Veterans Affairs, and the Nuclear Regulatory Commission. It also is composed of representatives of various national health care associations that help ensure Y2K awareness among their association's members. These associations include the American Ambulance Association (AAA), the American Association of Health Plans (AAHP), the American Hospital Association (AHA), the American Medical Association (AMA), the American Clinical Laboratory Association (ACLA), the American Health Care Association (AHCA), the American Pharmaceutical Association (APA), the Association of State and Territorial Health Officials (ASTHO), the Blue Cross Blue Shield Association (BCBSA), the Health Industry Manufacturers Association (HIMA), and the Joint Commission on Accreditation of Health Care Organizations (JCAHCO). It also includes the National Council for Prescription Drug Programs (NCPDP), the National Association of Community Health Centers, Inc. (NACHC), the National Association of Chain Drugstores (NACD), the National Association for Medical Equipment Suppliers, the National Association of Rural Health Clinics (NARHC), and the National Rural Health Association (NRHA). Additional organizations (e.g., the National Association of County and City Health Officials and the American Public Health Associations) plan to join the Sector.

CDC, FDA, HCFA, the Department of Labor, the Department of Defense, the Department of Veterans Affairs, the American Ambulance Association, and the American Hospital Association have developed six-month outreach plans. OPDIV staffs refined their plans to include more specific events, deliverables, and milestones. The Health Care Sector, like the Human Services Sector, is developing a sector-wide strategy for assessing the Y2K readiness of key sector partners.

During the last quarter, the HHS health care sector components conducted numerous outreach activities. The following depicts only some of the highlights of their most recent efforts.

**CDC** has posted all Y2K quarterly reports, white papers, assessments, outreach efforts, and other Year 2000 activities on the web at <http://www.cdc.gov/y2k/y2khome.htm>. (This website can be reached through the CDC home page.) Additionally, CDC systems managers have provided their findings regarding Y2K compliant software on the CDC website for easy access and distribution worldwide.

In February, CDC completed the first State health department readiness assessment and received more than a 50% response rate, and, after analyzing the data, provided the summary findings to the President's Council on Y2K Conversion. In April, CDC hosted a visit of the Japanese Ministry of Health representatives, and working with HCFA, FDA, HHS/OS, and others provided information to the Japanese health officials.

**FDA** has developed a response to the public's concern about the availability of medical products (e.g., pharmaceuticals, medical supplies). They have placed a notice in the Federal Register to inform industry of the intent to request information, develop a survey, and establish an audit program. FDA has been assisting in the planning for White House Summits on Pharmaceuticals and on consumable Medical Supplies.

**HCFA** drafted a Federal Register notice to announce the mailing of letters to providers, the availability of HCFA speakers to talk with provider groups about the Y2K issue, and the April 5, 1999, deadline for providers to begin submitting claims in Y2K compliant formats, as well as the availability of software for providers to use to generate such formats. They also hosted a Y2K Action Week in 12 cities (i.e., Boston, New York, Philadelphia, Atlanta, Chicago, Dallas, Kansas City, Denver, San Francisco, Seattle, Baltimore, and Washington). Examples of attendance for the outreach meetings are Kansas City where 176 people attended and Atlanta where 220 people attended. Lessons learned included the need to educate the providers on the complexity of the problem and its effect on their total business operations. HCFA also hosted a Managed Care Millennium Conference Y2K Action week in early April.

HCFA's toll free Y2K Information Line for Providers has received numerous calls about computer problems and billing issues, primarily from hospitals.

**IHS** has engaged in a number of outreach activities, including train-the-trainer and site visits to reinforce Y2K awareness. IHS has developed a Y2K video and brochure on the background of Y2K, the potential problems it can create, and a practical approach for addressing the issue that was sent to various tribes and health care organizations. They also scheduled their Y2K Awareness week to coincide with "The Gathering of Nations" in late April where a large number of Native American groups hold national conferences and meetings in the Albuquerque area.

**NIH** continues to conduct and/or participate in a number of internal and external outreach activities. External outreach activities include membership on the Biomedical Equipment Subcommittee and Buildings Work Group of the Government-wide committee. NIH also

participates in two other committees of the President's Council on Y2K Conversion: the Education Sector Committee and the Science and Technology Outreach Committee.

The Department has not limited its outreach activities to the American audience only. HHS hosts international Y2K delegations interested in Y2K and health care. The most recent delegation, sponsored by the United States Information Agency, was composed of 14 representatives from French-speaking Africa and from Laos who were interested in Y2K contingency planning for health care organizations.

### **Human Services Sector**

#### **Community Communications**

The Human Services Sector is composed of ACF, AOA, HCFA (Medicaid), HRSA, and SAMHSA. In addition to the current local number (202- 401-7041), the Human Services Sector instituted a "layered Toll-Free Number" (888-HHS-Y2K1), supported by a Help Desk, for Y2K issues. To augment the help desk, ACF revised the Human Services website (<http://y2k.acf.dhhs.gov>) to incorporate the latest information (e.g., the SBA Y2K Action week and providing a link to the appropriate URL).

To increase the visibility for their services, ACF prepared and sent a post card to approximately 12,500 human services providers informing them of available Y2K resources and how to access them. ACF also prepared business cards containing similar information to be distributed at Y2K conferences/meetings where sector representatives have been asked to speak. ACF continues to receive and answer information requests on their Y2K e-mail inquiry line ([Y2Kinquiry@ACF.DHHS.gov](mailto:Y2Kinquiry@ACF.DHHS.gov)) as well as by telephone.

ACF has also placed their revised "Y2K Information Guide For Human Services Providers" on the web and prominently displayed a link to view or download it from the first page of the web site. Demand for the Guide has been so overwhelming that 25,000 more guides, revised to be more generic and applicable to the entire Sector's audience, have been printed.

#### **State Issues**

The Y2K computer problem potentially affects all information systems for State health and human services. Specifically, program areas in which the Department and the States are collaborating are: Medicaid, Temporary Assistance for Needy Families (TANF), Child Support Enforcement (CSE), Child Care (CC), Child Welfare (CW), and the Low Income Home Energy Assistance Program (LIHEAP). These issues are the focus of the outreach efforts of the Administration for Children and Families (TANF, CSE, CC, CW, LIHEAP) and the Health Care Financing Administration (Medicaid). A description of these activities may be found in Section II. j. of this report.

### **Most Recent Outreach Activities by the Human Resources Sector**

For other State and non-State human services programs and systems, efforts on outreach, including stressing the importance of dealing with the problem and having contingency/business continuity plans ready should failures occur, will continue.

#### **ACF**

**Child Care Bureau** - The Bureau convened a National American Indian and Alaska Native Child Care Conference, March 21-24, 1999 attended by 50 participants. A presentation on Y2K contingency planning was made as a part of two (repeated) workshops on program reporting requirements. Only two of the Tribal staff indicated that they had begun testing on their hardware and software. Gila River Indian Community has a commitment from Intel to provide them with new computers for their Tribal programs and Tribal children.

The Bureau developed two Power Point presentations on, "How to Develop a Y2K Contingency Plan for State Child Care and Development Fund Programs and for Tribal Child Care Programs."

#### **HRSA**

HRSA disseminates Y2K information through targeted direct mailings, through the Human Services Sector, and other program specific web sites, speeches, conferences and the Human Services Y2K Helpdesk.

HRSA prepared a Y2K Assessment Tool called, "**The Workbook for Addressing the Year 2000 Bug in Community and Migrant Health Centers,**" that has been provided to each of the Migrant and Community Health Centers. The Y2K Assessment Tool is also on the HRSA web site (<http://www.hrsa.gov>) and at (<http://www.bphc.hrsa.gov>). The workbook provides a step-by-step approach for health center grantees to reference and document their progress in the assessment, renovation, validation, and implementation phases of their Y2K project schedule. HRSA is sharing best practices through the web sites and providing technical assistance with contractor assistance, including the HRSA Business Continuity and Contingency Plan (BCCP), Day One Plans, the Y2K Assessment Tool, and the Y2K Guide.

#### **SAMHSA**

On March 24, 1999, SAMHSA managers, supervisors, and team leaders were advised of the Human Services Sector outreach activities, including helpdesk, website, e-mail inquiry address, information guides, postcards, business cards, upcoming mailings to grantees and contractors, and the SBA-sponsored Y2K action week forums that have been initiated by HCFA. Staff were encouraged to widely announce the availability of these activities at outside meetings and to

attend the HCFA forum on March 29 at HHHH. On March 26, 1999, SAMHSA established its Y2K website at [www.samhsa.gov/y2k.htm](http://www.samhsa.gov/y2k.htm).

#### **Other Sector Participation**

In addition to the Health Care and Human Services Sectors, HHS is represented on the Food Safety, Education, Employment-Related Protections, Emergency Management/Disaster Response, and Science and Technology Outreach Sector Committees. HHS continues to participate on the Interagency American Indian Year 2000 Outreach Working Group.

- j. Describe efforts to ensure that Federally-supported, State-run programs (including those programs run by Territories and the District of Columbia) will be able to provide services and benefits. In particular, Federal agencies should be sensitive to programs that will have a direct and immediate effect on individuals' health, safety, or well-being. Include a description of efforts to assess the impact of the Year 2000 problem and to assure that the program will operate. In addition, provide the following information for those programs listed in Attachment D (if the information is not available, provide dates when it will be available).
  1. The date when each State's systems supporting the program will be Y2K compliant.
  2. A list of States, if any, for which the Y2K problem is likely to cause significant difficulties in the State's operation of the program. Also, provide a list of States which are not likely to encounter significant difficulties.
  3. For those States likely to have significant difficulties, a brief description of any action that the Department is taking to assure that the program will operate.

#### **State Issues**

The Y2K computer problem potentially affects all information systems for State health and human services. Specifically, program areas in which the Department and the States are collaborating are: Medicaid, Temporary Assistance for Needy Families (TANF), Child Support Enforcement (CSE), Child Care (CC), Child Welfare (CW), and the Low Income Home Energy Assistance Program (LIHEAP). HHS has been working with and surveying program and information systems in the States. This outreach includes teleconferences and site visits by the Health Care Financing Administration (HCFA) for the Medicaid program, and through a mail-out survey for human services programs by the Administration for Children and Families (ACF).

#### **Medicaid**

As of April 16, the HCFA IV&V contractor, assisted by Regional and Central Office staff, completed 45 State visits. Five more visits were conducted during the week of April 19 - 23. By the end of April, visits to all 50 States, including the District of Columbia, were completed. Information on the planned dates for Y2K compliance of State Medicaid Management Information Systems and Integrated Eligibility Systems is shown in the chart on page twenty-one.

Follow-up IV&V on-site visits to States in the medium to high risk categories will begin in May, continuing through October. GAO has accompanied the IV&V team to several states (e.g.,

California, New Mexico, Massachusetts and South Carolina) to assess the activities performed by HCFA's IV&V contractor.

HCFA has initiated a process of obtaining an outside contractor to review the contingency plans of State Medicaid programs. This project will focus on monitoring and overseeing State plans and providing technical assistance to HCFA and States as to the status of State contingency plans, through review, recommendations and on-site assistance where it is warranted.

Letters, including copies of the results of the on-site visit prepared by HCFA's IV&V contractor have been sent to State Medicaid Directors and to the Governors of California, Connecticut, District of Columbia, Georgia, Iowa, Louisiana, Maine, Maryland, Missouri, North Carolina, New Jersey, New Mexico, New York, Pennsylvania, South Carolina, Texas, Virginia, and Wisconsin. States have been asked to respond to the IV&V findings. These letters will be used in focusing on the follow-up visits to States during the May - October visits. On a monthly basis, letters will continued to be mailed to the State Medicaid Directors as well as to the State Governors and their Chief Information Officers and Y2K Coordinators.

HCFA is also requesting State agencies to submit their business continuity and contingency plans to HCFA by June 1, 1999. HCFA will review these plans to gain a better understanding of the States' plans.

#### **State Human Services Programs and Systems**

On December 23, 1998, the Assistant Secretary for Management and the Assistant Secretary for Children and Families wrote to the State Chief Information Officers, asking them to follow up on a report from the General Accounting Office on the "Readiness of State Automated Systems to Support Federal Welfare Programs. The Department also asked them to report on the Y2K readiness (including the existence of a contingency plan) of their human services systems (i.e., TANF, CSE, CC, CW) and to establish a monitoring process. They were asked to provide an initial status report on January 31, and follow up reports on April 1, July 1, September 1, and December 1. The Department has received 48 survey submissions from the States and the District of Columbia concerning TANF, CC, CSE, CW. States that have not submitted their initial Y2K reports are: Connecticut, District of Columbia, and West Virginia. ACF is now receiving the second round of reports, which was due on April 1.

Finally, since the Y2K computer problem potentially affects all information systems for State health and human services, the Secretary wrote to each State Governor on January 29 encouraging them in their efforts, and again on March 31 reporting on the Department's Y2K activities with regard to the States, including results of the reports from the ACF survey and from the HCFA Medicaid on-site visits, where available. ACF plans to provide offer on-site technical assistance to State agencies and to work closely with them to develop complementary Federal and State Y2K contingency plans. ACF has awarded a contract to obtain services in assessing the Y2K status of State human services systems and supporting ACF's outreach to the States. Follow-up visits will



continue through the remainder of 1999. The Department will share the detailed reports on the results of the site visits, addressing both findings and its recommendations, with the Governors periodically.

Summary results from States responding to a Department of Health and Human Services survey of the Y2K readiness of State Temporary Assistance for Needy Families (TANF), Child Support Enforcement (CSE), Child Care (CC) and Child Welfare (CW) programs and systems, can be found on the following page.

States	State Reported Systems Data - (Compliance Date of Last Subsystem)												Exhibit 8					
	Child Care			Child Support Enforcement			Child Welfare			TANF			Contingency Plans		Medicaid - MMS		Medicaid - JES	
	Contingency Plans	Child Support Enforcement	Child Welfare	Contingency Plans	Child Support Enforcement	Child Welfare	Contingency Plans	TANF	Contingency Plans	Medicaid - MMS	Medicaid - JES							
ALABAMA	Jul-99	Jun-99	Dec-99	Jun-99	Jul-99	Jun-99	Jun-99	Sep-99	Jun-99	Oct-Dec 99	Jul-Sep 99							
ALASKA	*	Aug-99	UA	Aug-99	UA	Aug-99	UA	UA	Aug-99	Jul-Sep 99	Apr-Jun 99							
ARIZONA	Aug-98	UA	Dec-98	UA	Feb-98	UA	Aug-98	UA	Sep-99	Apr-Jun 99	Apr-Jun 99							
ARKANSAS	Oct-98	UA	Feb-99	UA	Feb-99	UA	Feb-99	UA	1998	1998	1998							
CALIFORNIA	*	Nov-99	May-99	May-99	Dec-98	Jul-99	Sep-99	UA	Jul-99	Apr-Jun 99	1998							
COLORADO	Jun-99	UA	Jun-99	UA	Jun-99	UA	Jun-99	UA	UA	Apr-Jun 99	Apr-Jun 99							
CONNECTICUT	Apr-99	Jul-99	Mar-99	Jun-99	Jun-99	Jun-99	Jun-99	Jun-99	Jun-99	Apr-Jun 99	Apr-Jun 99							
DELAWARE	1998	UA	1995	UA	1995	Oct-99	1998	UA	UA	Apr-Jun 99	Jul-Sep 99							
DISTRICT OF COLUMBIA	UA	UA	UA	UA	UA	UA	UA	UA	UA	Jul-Sep 99	Apr-Jun 99							
FLORIDA	UA	UA	Nov-98	May-99	Aug-98	May-99	Aug-98	UA	UA	Apr-Jun 99	1998							
GEORGIA	*	Sep-99	Jul-99	Mar-99	NA	NA	Jan-99	Mar-99	Mar-99	Oct-Dec 99	1998							
HAWAII	Jun-99	Sep-99	May-99	Feb-99	Apr-99	Feb-99	Nov-98	Jul-99	Jul-99	1998	1998							
IDAHO	Nov-98	Jun-99	Mar-99	Jun-99	Dec-98	Jun-99	Oct-98	Jun-99	Jun-99	1998	1998							
ILLINOIS	Mar-99	Mar-99	UA	May-99	Oct-99	Apr-99	Sep-99	UA	UA	Jul-Sep 99	Jul-Sep 99							
INDIANA	Jul-99	Apr-99	Jul-99	Mar-99	Apr-96	Apr-96	Oct-99	Mar-99	Mar-99	Apr-Jun 99	Apr-Jun 99							
IOWA	Mar-99	Jun-99	Mar-99	Jun-99	Mar-99	Jun-99	Jun-99	Jun-99	Jun-99	Apr-Jun 99	Apr-Jun 99							
KANSAS	Jan-99	Jul-99	May-99	Jul-99	UA	Jul-99	May-99	Jul-99	Jul-99	1998	Apr-Jun 99							
KENTUCKY	Apr-99	Jun-99	Jun-99	UA	Dec-98	UA	Jun-99	Jun-99	Jun-99	Apr-Jun 99	Jan-Mar 99							
LOUISIANA	Jul-99	Sep-99	Sep-98	Sep-99	Jul-98	Sep-99	Sep-98	UA	UA	Oct-Dec 99	Jul-Sep 99							
MAINE	NA	NA	Aug-99	UA	Apr-98	UA	Apr-99	UA	UA	Apr-Jun 99	Apr-Jun 99							
MARYLAND	May-98	Sep-99	Jun-98	Sep-99	Jun-99	Sep-99	Aug-99	Sep-99	Sep-99	Apr-Jun 99	1998							
MASSACHUSETTS	Sep-99	UA	Jan-99	UA	Apr-99	UA	Jun-99	Apr-99	Apr-99	Apr-Jun 99	Apr-Jun 99							
MICHIGAN	May-99	Jul-99	Jan-99	Jul-99	Apr-99	Jul-99	May-99	Jul-99	Jul-99	Jul-Sep 99	Jul-Sep 99							
MINNESOTA	*	Apr-99	Jul-99	Jul-99	Mar-99	Mar-99	Apr-99	Apr-99	Apr-99	1998	Apr-Jun 99							
MISSISSIPPI	UA	UA	Jun-99	Jul-99	Jun-99	Jul-99	Jun-99	Jul-99	Jul-99	Jan-Mar 99	Jul-Sep 99							
MISSOURI	Feb-98	Aug-99	Oct-98	Oct-98	Apr-99	Apr-99	Mar-99	Aug-99	Aug-99	1998	Jul-Sep 99							
MONTANA	Jun-99	Sep-99	May-99	Sep-99	Jun-99	Sep-99	Jun-99	Jun-99	Jun-99	Apr-Jun 99	Apr-Jun 99							
NEBRASKA	Jul-99	UA	Jun-99	Jun-99	Jul-99	UA	Jul-99	UA	UA	1998	1998							
NEVADA	Jun-99	Jun-99	Sep-99	Jun-99	Apr-99	Jul-99	Sep-99	UA	UA	Jul-Sep 99	Jul-Sep 99							

States	State Reported Systems Data - (Compliance Date of Last Subsystem)									
	Child Care	Child Support	Child Welfare	TANF	Contingency Plans	Medical - MMS	Medical - IES			
NEW HAMPSHIRE	UA	Oct-99	UA	May-99	UA	Jul-Sep 99	Oct-Dec 99			
NEW JERSEY	Sep-99	Jun-99	Sep-99	Jul-99	UA	Jul-Sep 99	Apr-Jun 99			
NEW MEXICO	UA	Oct-99	UA	UA	UA	Jul-Sep 99	Jul-Sep 99			
NEW YORK	Nov-98	Jul-99	Jan-99	Jul-99	Dec-98	1998	Apr-Jun 99			
N. CAROLINA	May-96	UA	1997	UA	Sep-99	UA	Jul-Sep 99			
N. DAKOTA	Jan-98	Jul-99	May-97	Jul-99	1997	UA	Jul-Sep 99			
OHIO	Jun-98	Oct-99	May-99	Jun-98	Oct-99	Apr-Jun 99	Apr-Jun 99			
OKLAHOMA	Oct-99	Sep-99	Nov-99	Oct-99	Oct-99	Jul-Sep 99	Jul-Sep 99			
OREGON	Mar-99	Jun-99	Jun-99	Jun-99	Apr-99	Jul-Sep 99	Jul-Sep 99			
PENNSYLVANIA	Oct-98	Oct-99	Oct-99	Dec-98	Oct-99	1998	1998			
RHODE ISLAND	Jul-99	Jul-99	UA	UA	Jul-99	Jul-Sep 99	Oct-Dec 99			
S. CAROLINA	Oct-98	Jun-99	Jun-99	Jun-99	May-99	Jun-99	Jul-Sep 99			
S. DAKOTA	Jul-99	Jul-99	Jul-99	Jul-99	Jul-99	Apr-Jun 99	Jan-Mar 99			
TENNESSEE	Nov-99	Jan-99	Aug-99	Jun-99	UA	Jan-Mar 99	Jan-Mar 99			
TEXAS	Sep-98	UA	May-99	Sep-99	UA	Feb-99	Jul-Sep 99			
UTAH	UA	UA	UA	UA	Aug-99	UA	Jan-Mar 99			
VERMONT	Oct-98	Jun-99	Jun-99	Jun-99	Jun-99	May-99	Apr-Jun 99			
VIRGINIA	*	Jun-99	May-99	Jun-99	Jun-99	Jun-99	Jul-Sep 99			
WASHINGTON	Mar-98	Jan-99	Nov-98	Jan-99	Jan-99	Jan-99	Apr-Jun 99			
WEST VIRGINIA	UA	UA	UA	UA	UA	UA	Apr-Jun 99			
WISCONSIN	Mar-99	May-99	Mar-99	Jun-99	Mar-99	May-99	Jul-Sep 99			
WYOMING	Mar-99	Sep-99	UA	Sep-99	UA	Apr-Jun 99	1998			

\*Alaska Child Care has not been identified as a mission critical system, therefore no Y2K project information statistics have been kept.  
 \*California does not currently have a Statewide automated system for either Child Care or TANF.  
 The eventual automation will be accomplished through the Statewide Automated Welfare System (SAWS).  
 SAWS consists of four consortia in 88 counties. Each consortium will have a component in its automated system, but are in different development stages.  
 \*Georgia has no Statewide systems for Child Care or Child Welfare and is dependent on manual delivery.  
 \*Minnesota's Child Care program is operated by the Minnesota Department of Children, Families, and Learning. Information is not available at this time.  
 \*Virginia's Child Care systems are local, not State centralized.

UA means that the data were not provided by the States.  
 NA means that the State reported that the data requested were not applicable to them.

Results from on-site reviews in States. State written survey responses, contacts with State associations and normal business contacts with States indicate that on the whole States are actively remediating the Y2K problem in their human services programs and systems, which provide vital human services to needy families, children and individuals. A number of States have reported that their human services systems are Y2K ready. Most States report that their human services systems will be Y2K ready during the 1999 calendar year. As the millennium change approaches, the emphasis in State human services programs and systems will be on contingency/business continuity planning and reaching out to local governments and communities concerning their Y2K readiness.

#### **Other Human Services Programs**

For the human services programs on aging, AOA, through informal discussions with State program managers, has determined that services will be maintained even if there are failures in local program support computer systems. The States Units on Aging (SUA) do not have computer systems that are critical for the delivery of services.

#### **For the Future**

For the remainder of 1999, HCFA will continue to conduct on-site assessments of State Medicaid systems, and provide technical assistance, with particular emphasis on contingency/business continuity planning. The Administration for Children and Families (ACF) will continue to survey States' efforts in the Temporary Assistance for Needy Families, Child Support Enforcement, Child Care and Child Welfare programs. ACF will shortly undertake a major initiative to conduct on-site assessments of States' efforts in these programs and the Low Income Home Energy Assistance Program (LIHEAP). Emphasis will be placed on contingency/business continuity planning and assisting local governments and communities with becoming Y2K ready.

#### III. Verification Efforts.

- a. Describe the process by which mission critical systems are identified as Y2K compliant for purposes of this report.

The information provided in Section III of the February Quarterly Report remains current.

- b. Describe how and to what extent internal performance reports, (i.e., compliance of systems repaired and replaced) are independently verified. Provide a brief description of activities to assure independent verification that systems are fixed and to assure that information reported is accurate. Also identify who is providing verification services (i.e., Inspectors General or contractors).

All OPDIVs will use outside contractors for their Independent Verification and Validation (IV&V). The contractors that the OPDIVs are working with are listed below.

ACF - AverStar, Inc., SRA, Inc., and Lockheed-Martin	HRSA - Computer Associates and Eagle Technologies
CDC - TRW	IHS - Mitretek
FDA - TRW	NIH - OAO
HCFA - AverStar, Inc., and SETA	PSC - Mitretek and TRW (formerly BDM)
	SAMHSA - InfoPro

OPDIVs are required to submit their IV&V reports to ASMB for review.

The Office of the Inspector General (OIG) is conducting an on-going audit on the Y2K date conversion project. Along with the IV&V contractors, they conduct on-site visits to Medicare external contractors. HCFA has been working with its IV&V contractor, AverStar, the OIG, and GAO to make its retesting and recertification process even more rigorous.

IV. Organizational Responsibilities.

- a. Describe how your Department/Agency is organized to track progress in addressing the year 2000 problem. (If you have provided this information in the past, only provide it again where it has changed.) Include in your description the following:
  - Describe the responsible organization(s) for addressing the year 2000 problem within your Department/Agency and provide an organizational chart.
  - Describe your Department/Agency's processes for assuring internal accountability of the responsible organizations. Indicate how frequently the agency head or Chief Operating Officer is briefed on year 2000 progress. Include any quantitative measures used to track performance and other methods to determine whether the responsible organizations are performing according to plan. Include a discussion of the oversight mechanism(s) used to assure that replacement systems are on schedule.
  - Describe the management actions taken and by whom when a responsible organization falls behind schedule.

The information previously provided in Section IV of the August Quarterly Report remains current. The Deputy Secretary and the Assistant Secretary for Management and Budget continue to hold bi-weekly meetings with senior OPDIV representatives and CIOs on Y2K efforts. The Department's senior officials, as well as the OPDIV heads, CIOs, and senior managers continue to actively work together to conduct end-to-end testing, develop and test contingency plans, establish a moratorium for systems changes and recertify systems after any changes.

V. Business Continuity and Contingency Planning.

Describe your agency's approach to and progress in developing its Business Continuity and Contingency Plan (BCCP). Agencies should use the GAO document, Year 2000 Computing Crisis: Business Continuity and Contingency Planning, (August 1998), as a guide to such planning. Describe the measures of progress being used to assure that local plans are developed and tested (e.g. status of management assurances that plans are complete and have been tested) and provide a status of those measures. Please also include the following information in the description of your planning activity. (If you do not have the information requested, state when it will be available.):

1. Identify the high-level core business functions addressed in your BCCP.
2. Provide a master schedule and key milestones for development, testing, and implementation of your BCCP.

The core business functions and schedules for the Operating Divisions' Business Continuity and Contingency plans are listed below.

**Core Business Functions**

**ACF Core Business Functions**

All mission-critical systems support, in some aspect, one or more of the following Core Business Functions:

- Provide grants to human services sector grantees for the delivery of human services.
- Support, track, and assist States in enforcing child support orders.
- Collect and maintain information on vulnerable populations receiving human services.
- Provide technical assistance to grantees and States in support of their human services delivery efforts.

**AHCPR Core Business Functions**

AHCPR is charged with supporting research designed to improve the quality of health care, reduce its cost, and broaden access to essential services. AHCPR's broad programs of research bring practical, science-based information to medical practitioners and to consumers and other health care purchasers.

AHCPR's BCCP focuses primarily on the following core business functions:

- Grants Management Processing
- Intramural Research Applications
- Internal and External Business Functions

**AOA Core Business Functions**

AOA's core business function is the award and management of grants, both discretionary and formula grants.

**CDC Core Business Functions**

CDC's mission of promoting health and quality of life by preventing and controlling disease, injury, and disability continues to be increasingly dependent on IT, electronic communications, and digital media. CDC has identified potential risks and contingency plans to ensure the continuity of CDC's operations and mission. As part of their contingency planning, CDC has identified the following seven major business functions:

- Public health surveillance;
- Health statistics;
- Research;
- Public health services;
- Health communications;
- Strategic planning;
- Resource management.

**FDA Core Business Functions**

The mission of the FDA is to protect, promote, and enhance the health of the American people. FDA is responsible for ensuring that:

- Foods are safe, wholesome and sanitary; human and veterinary drugs, biological products, and medical devices are safe and effective; cosmetics are safe; and electronic products that emit radiation are safe;
- Regulated products are honestly, accurately and informatively represented.
- These products are in compliance with the law and FDA regulations; noncompliance is identified and corrected; and any unsafe or unlawful products are removed from the marketplace.

In order to perform this mission, the work of the Agency has been organized into seven core program areas, which are managed by the Agency's Centers/Offices. Each Center/Office performs a broad range of critical business processes in support of the Agency's overall mission.

As part of the contingency planning, FDA has identified five core business processes:

- Conduct product review and approval on products;
- Conduct post-market surveillance and adverse event reporting;
- Develop Methods and Good Manufacturing Practices;
- Conduct scientific research;
- Perform compliance monitoring and auditing.

#### **HCFA Core Business Functions**

Based on an extensive business impact analysis of over 280 business processes, HCFA will develop specific contingency and/or risk mitigation plans for the approximately 50 business functions facing highest risk/impact to continuity. These plans are HCFA's strategy for protecting eleven core business functions with an emphasis on our four guiding principle areas:

- Continue Payments,
- Safeguard the Trust Funds,
- Protect Quality Care for Beneficiaries, and
- Sustain Beneficiary Entitlement and Enrollment

#### **HRSA Core Business Functions**

HRSA's primary core business function is the awarding of grants to grantees providing critical primary health care services to the underserved. HRSA also maintains significant network and data banks including the Organ Procurement and Transplant Network (OPTN) and the National Practitioner Data Bank (NPDB).

#### **IHS Core Business Functions**

The mission of IHS, in partnership with American Indian and Alaska Native people, is to raise their physical, mental, social, and spiritual health to the highest level. The goal of IHS is to assure that comprehensive, culturally acceptable personal and public health services are available and accessible to American Indian and Alaska Native people.

IHS' core mission areas by priority are the following:

- Provide Health Services
- Improve Health Status
- Assure Partnerships and Consultations with I/T/Us
- Perform Core Functions and Advocacy

IHS' approach to development and implementation of a BCCP consists of a streamlined, template approach. This is designed to allow each respective Area, Site, or Medical Facility's Y2K coordinator or director or designee to identify and define core business processes that are dependent upon laboratory equipment, biomedical devices, infrastructure components, telecommunications resources, and RPMS software and computer equipment. These processes are integral in delivering high quality, uninterrupted or minimally disrupted patient care, and in supporting revenue generation.



**NIH Core Business Functions**

NIH has completed a draft of its Y2K BCCP that describes how NIH will continue to conduct its critical business processes into the Year 2000 in the event of unanticipated Y2K system failures. These business processes are organized into the following core program areas that are critical to the accomplishment of the NIH mission to support and conduct research:

- Intramural Research - e.g. laboratory research, patient and animal care
- Extramural Research - e.g. grants management and research and development contracts
- Administration - e.g. financial management, acquisition, and logistics support
- Infrastructure - e.g. computer center, telecommunications/networks, and research laboratory/facility support

The draft Y2K BCCP describes NIH's Y2K planning approach, its critical business processes and the mission critical systems that support them, and provides guidance for completing Y2K contingency plans for each core program area. NIH has selected TRW (formerly BDM) to provide assistance with Y2K BCCP activities based on their Y2K contingency planning experience at FDA.

**OIG Core Business Functions**

The OIG core business functions are the following:

- Conduct audits, investigations and inspections
- Provide Secretarial protection

**PSC Core Business Processes**

PSC has developed core business functions for each of its service areas: Administrative Operations Service, Financial Management Service, Human Resource Service, and Office of the Director. The core business functions include the following:

- Provide space and building management services for Parklawn Building, Personal Property Facility and Park Building.
- Provide pharmaceutical, medical, and dental supplies to both HHS and external customers.
- Provide telecommunications, network, and desktop computing services to both HHS and external customers.
- Provide electronic funding and cash management service to organizations receiving HHS grants and contracts, as well as grants from nine other Federal agencies.
- Process personnel and pay-related transactions and maintain personnel/pay records for both HHS and external customers (civil service employees).

**SAMHSA Core Business Functions**

SAMHSA's primary core business function is the awarding of grants and contracts to develop and disseminate knowledge on service delivery, and to improve the quality and availability of substance abuse prevention and treatment as well as mental health services.

**Milestones and Schedules of Business Continuity and Contingency Plans**

**ACF Milestones and Schedule**

ACF submitted an extensive BCCP for the entire agency on April 15, 1999. ACF has also submitted disaster recovery/contingency plans, developed in conjunction with the ACF program offices, for each of ACF's mission critical systems. The IV&V contractor assisted and supported the development of the contingency plans. These plans identify specific triggers, timeframes, dependencies, and remediation actions for specific Y2K-related partial or complete system failures.

ACF believes the plans will adequately ensure business continuity should any or all of these systems experience Y2K-related problems. GATES and AFCARS are dependent upon the disaster recovery procedures of NIH DCRT in the case of an infrastructure failure. However, a BCCP was developed for GATES that provides comprehensive information on the failure scenarios that might affect the system. In addition, Central and Regional offices that have responsibility for various pre- and post-GATES grant-making work have analyzed failure scenarios that might occur in this work. TROS, EVS, and FPLS are dependent upon the disaster recovery procedures of SSA MISF in the case of an infrastructure failure. CSENet and RHYMIS operate on their own respective infrastructures (the systems are essentially networks of PCs) and are not dependent upon outside entities. BCCPs were developed for these systems to provide comprehensive information on the failure scenarios that might affect these systems.

In addition, ACF is developing partnership plans to assist States and localities deliver services in five key programs: TANF, Child Support Enforcement, Child Care, Child Welfare, and LIHEAP. ACF will report on plan activities throughout the year.

**AHCPR Milestones and Schedule**

AHCPR's contingency plan is to modify the existing GIANT and other Agency legacy business systems software, modify data files, and provide a work around for non-Y2K COTS software to provide the Agency the needed functions of these applications. The schedule for the BCCP is below:

- BCCP Detailed Plan in place April 1999
- BCCP Design Phase complete May 1999
- BCCP Development Phases complete June 1999
- BCCP Implementation Phase complete August 1999

**AOA Milestones and Schedule**

The Business Continuity and Contingency Plan for AOA’s mission critical systems is the AOA Continuity of Operations Plan, in effect since 1995. The Plan entails the manual process of awarding grants and making grant actions, including the manual transfer of data to the CORE accounting system.

**CDC Milestones and Schedule**

CDC has approached the Year 2000 contingency planning on a multi-tier level based on the probability of needing to invoke the plan and the consequences of each systems’s failure. The framework consists of four levels:

- Tier 1 - Enterprise Contingency Plan
- Tier 2 - Individual Plans for Mission Critical, High Time Sensitivity Systems
- Tier 3 - Individual Plans for Mission Critical, Low Time Sensitivity Systems Not Currently Year 2000 Compliant
- Tier 4 - Mission Critical and Low Time Sensitivity Systems Currently Year 2000 Compliant

Due to the nature of CDC’s mission based largely on collecting, processing, analyzing, and reporting on retrospective health event data related to public health, many of the agency’s mission critical systems are not subject to a high degree of time-sensitivity (Tier 3 and Tier 4 systems). In other words, system disruptions of days, weeks, and in some cases even months, can be endured without catastrophic consequences. Consequently, these systems have been identified and the contingency plans for them consist primarily of suspending processing while remediation takes place, switching to manual processing, or an alternative back-up system.

CDC has completed the contingency plans for all Tier Levels. The plan is available at the following web site: <http://www.cdc.gov/y2k/y2khome.htm>. This plan will be updated to ensure that CDC’s business processes are fully discussed and appropriately ranked for business continuity and contingency planning purposes.

**FDA Milestones and Schedule**

Below is the listing of the FDA schedule for contingency planning including activities that FDA has completed:

- |   |          |
|---|----------|
| • Identify core program areas   | Complete |
| • Develop draft strategic business continuity and contingency plan    | Complete |
| • Develop system-level contingency plans for mission critical systems | Complete |

- Develop a high level contingency plan for its technical infrastructure Complete - August 31, 1998
- Conduct business impact analysis on critical business processes Complete - September 15, 1998
- Develop low-level contingency plans Complete - October 31, 1998
- Develop detailed business continuity and contingency plans for critical business processes Complete - December 15, 1998
- Pilot test of contingency plan for the Center for Veterinary Medicine's Pre-Market Review and Approval Process and Post-Surveillance reporting process Complete - April 12, 1999
- Complete testing of all business process contingency plans September, 1999

#### **HCFA Milestones and Schedule**

HCFA is continuing to follow a four phase model (initiation, business impact analysis, contingency planning and validation) in developing its Business Continuity and Contingency Plan. During this past quarter HCFA completed the third phase, develop contingency plans. On April 1, 1999, HCFA released its Agency-wide Year 2000 Business Continuity and Contingency Plan (BCCP), Version 4.

In the upcoming quarter, HCFA will focus on phase four: Validation and Testing. HCFA plans to validate the appropriateness of its contingency plans by applying testing scripts to the individual contingency plans. HCFA expects to refine the plans based on the outcomes. The goal is to complete the final phase by June 30, 1999.

As part of HCFA's emphasis on partners, HCFA is conducting a review of Medicare Carrier and Fiscal Intermediary contingency plans. In October 1998, HCFA instructed Medicare contractors to undertake a contingency planning program. On April 8, 1999, HCFA began examining all Medicare Carrier and Fiscal Intermediary contingency plans, placing emphasis on reasonableness and completeness of individual plans. HCFA plans to provide guidance and assistance to those organizations that appear to have not adequately staffed and completed contingency planning. Also, HCFA is requiring all Medicare managed care organizations to submit contingency plans to HCFA by July 15, 1999.

HCFA has increased its level of effort for review and assistance offered to State Medicaid Agencies. The goal is to offer as much assistance as possible to help ensure continuity of Medicaid payments and continued access to services. HCFA has provided State agencies instructions to prepare business continuity and contingency plans and is requesting State agencies to submit their plans by June 1, 1999. HCFA will review these plans to gain a better understanding of States' plans to assure continuity of their health care programs in the unlikely event of systems failures. HCFA has contracted for Medicaid-related Independent Verification & Validation (IV&V) services to assess the status of States. Site visits are in progress. HCFA is also establishing a contract to provide technical assistance to States on contingency planning.

**HRSA Milestones and Schedule**

The objective of HRSA's Business Process and Contingency Plan will be to safeguard HRSA's ability to produce a minimum acceptable level of outputs and services if problems occur with business systems that may be affected by Year 2000 induced computer system problems.

HRSA's Schedule of Contingency Planning Activities

- Preliminary Business Impact Analysis Completed August 1998
- 
- Draft Business Continuity and Contingency Plan October/December 1998  
(Internal Review January/February 1999)
- 
- Technical Infrastructure Risk Assessment and Contingency Plan February 1999
- 
- Comprehensive Business Continuity and Contingency Plan
  - contract awarded to Mitretek April 1999
  - working plan in place August 1999

HRSA is committed to the Independent Validation and Review examining the Contingency Plan of each of the mission critical systems. Each of HRSA's mission critical systems currently has a contingency plan in place.

The IV&V process for each system began in March 1999 and should be completed by June 15, 1999. The following systems will have an IV&V: GEMS, BCHDANET, HEALIS, National Practitioner Data Bank, and OPTN.

**IHS Milestones and Schedule**

IHS submitted Prototype BCCP planning documents on March 31, 1999. IHS distributed Prototype BCCP templates for Headquarters, Area, hospitals and clinics to all Area Y2K Coordinators and also made them available on IHS' web site. IHS national staff made site visits to Phoenix, Aberdeen, California, and Billings Area to provide training and assistance. A two-day BCCP training was provided to Navajo Area on March 31, 1999 and another is scheduled for Alaska Tribes at the end of April.

IHS milestone schedule is below:

- Complete BCCP June 30, 1999
- Test BCCP July 30, 1999

**NIH Milestones and Schedule**

<u>Milestone</u>	<u>Target Date</u>
• Identify core program areas	Complete
• Develop system-level Y2K contingency plans for mission critical systems	Complete
• Develop draft NIH-wide Y2K BCCP	Complete
• Receive comments back from functional managers on draft Y2K BCCP	Complete
• Complete Y2K business impact analysis on critical business processes	April 1999
• Complete Y2K business process continuity contingency plans for critical business processes	June 1999
• Complete testing of business process contingency plans	July 1999

**OIG Milestones and Schedule**

<u>Milestone</u>	<u>Target Date</u>
• Identify core program areas	Completed
• Develop draft strategic business continuity and contingency plan	Completed
• Conduct Business Impact Analysis on critical business processes	Completed
• Develop Business Continuity and Contingency Strategic Plan (V 1.0)	Completed
• Develop Business Process Continuity Plans (V 1.0)	April 30, 1999
• Assess/Test Business Process Continuity Plans (V 1.0)	May 31, 1999
• Update Business Process Continuity Plans (V 2.0)	June 15, 1999
• Update Business Continuity and Contingency Strategic Plan (V 2.0)	June 30, 1999
• Test Business Continuity and Contingency Strategic Plan (V 2.0)	July 31, 1999

**PSC Milestones and Schedule**

The PSC has adopted the structured approach to Y2K business continuity planning as defined by the General Accounting Office (GAO).

PSC's initial step in the development of its BCCP was identifying the PSC lines of business, the core business processes essential to each Service. For each core business process in the BCCP, the BCCP identifies business-essential systems and infrastructure components used to carry out each process. Also, it identifies Y2K failure scenarios relevant to the core business process, estimates the degree of impact on the business process as high, medium, or low, and identifies the nature of the impact. Within each Service, staff have been identified and are performing the required analyses and developing approaches for addressing risks.

Business Continuity Plans, PSC systems or infrastructure contingency plans are scheduled to be completed and tested by May 28, 1999.

**SAMHSA**

SAMHSA's current Business Continuity and Contingency Plan calls for manual processing if a Year 2000 failure occurs until the Year 2000 problem is corrected. To ensure that SAMHSA will be able to continue with its critical business processes, the Division of Grants Management (DGM) and Division of Contracts Management (DCM) are currently updating these plans for Year 2000 impact. As part of this business impact update, DGM and DCM will define the minimum acceptable level of outputs and services for each critical process.

**VI. Exception Report on Systems.**

Provide a brief status of work on each mission critical system which is not year 2000 compliant that is either (1) being replaced and has fallen behind the agency's internal schedule by two months or more, or (2) being repaired and has fallen behind the agency's milestones by two months or more.

- a. If this is the first time this system is reported, include:
  1. An explanation of why the effort to fix or replace the system has fallen behind and what is being done to bring the effort back on schedule.
  2. The new schedule for replacement or completion of the remaining phases.
  3. A description of the funding and other resources being devoted to completing the replacement or fixing the system.

Please see Section VII.

- b. If this system has been previously reported and remains behind schedule, include:
1. An explanation of why the system remains behind schedule and what actions are being taken to mitigate the situation.
  2. A summary of the contingency plan for performing the function supported by the system should the replacement or conversion effort not be completed on time. Indicate when the contingency plan would be triggered, and provide an assessment of the effect on agency operations should the system fail. If you do not yet have a contingency plan, indicate when it will be in place.
- If your agency has completed an agency-wide plan which includes this information, provide a copy of in lieu of providing the information.

The HCFA systems reported on in the February Quarterly Report have been certified as Y2K compliant.

VII. Systems scheduled for implementation after March 1999.

Please include a list of those mission critical systems where repair *or* replacement cannot be implemented by the March 1999 deadline. The list should include:

- a. The titles of the systems.
- b. A brief description of what the system does.
- c. The reason that the system cannot be implemented by the deadline.
- d. A summary of the contingency plan for performing the function supported by the system should the replacement or conversion effort not be completed on time. Indicate when the contingency plan would be triggered, and provide an assessment of the effect on agency operations should the system fail, including anticipated problems. If you do not yet have a contingency plan, indicate when it will be in place.

**HCFA mission critical external system**

Of the 75 systems certified, one (1) contractor certification was not accepted by HCFA until April 23, 1999. This contractor is Mutual of Omaha - Part A Intermediary on the Arkansas Standard Part A System (APASS). Mutual of Omaha has implemented its Y2K compliant system. Additional future date testing was completed April 23, 1999.

**IHS mission critical system**

The Resource and Patient Management System (RPMS) is scheduled for completion at the end of June 1999.

The Resource and Patient Management System (RPMS) is the heart of the medical facilities information resource management activities for the IHS, Tribal, and Urban health programs. RPMS consists of modules that are developed, maintained, and distributed nationally, and installed locally at the health care facility.

IHS has three unique and extremely important challenges, which dramatically affect the implementation of RPMS throughout all IHS, Tribal, and Urban facilities. First, many of the



people served by the IHS live in some of the most remote areas in 35 different States across the nation. Secondly, unlike many organizations where implementation of Y2K compliant software is installed at only a single or few facilities, RPMS implementation is required at 101 IHS operated facilities and 175 Tribal and Urban facilities. Finally, IHS is not only addressing the Year 2000 issues in the IHS direct facilities for which we are responsible, but IHS is also actively involving all of the Tribes and Urban programs who have elected to assume responsibility under Indian Self Determination for the delivery of services in their own communities.

IHS has engaged in an unprecedented outreach effort to raise awareness and provide information and technical assistance to the Tribal and Urban facilities for which IHS has little authority or control. To support outreach activities to Tribal and Urban Indian programs, a Y2K resource kit with videos, brochures, and references was produced and distributed to nearly 1100 addresses. A Y2K web site was established (<http://www.ihs.gov/y2k>) that is continuously updated to provide a common source of pertinent information for IHS, Tribal, and Urban Indian programs. IHS is projecting that IHS direct facilities will complete implementation by April 30, 1999, and have set a target date for Tribal and Urban facilities to complete implementation by June 30, 1999. Thus, these facilities will be Y2K ready well in advance of the new millennium.

IHS health care facilities have contingency plans for their Automated Information Systems (AIS) which must be in place by June 30, 1999. Since the Year 2000 problem poses a number of new and unique threats to the continuity of information systems, current contingency plans are being reviewed for appropriateness and updated as needed. Contingency plans include the identification of potential problems, their impact on mission-critical systems, and policies and procedures to minimize any potential disruption in operations. National, area, and facility level Automated Information Business Resumption Teams (AIS/BRT) composed of technical experts are developing and implementing Year 2000 contingency plans for AIS systems. Membership of the AIS/BRT includes the RPMS Systems Manager, Information Security Officer, supervisor of telecommunications, and network manager. The AIS/BRT will coordinate their efforts with the Business Continuity Planning Workgroup (BCPW) so that AIS contingency plans are integrated into the over-all health care facility's Year 2000 Contingency Plan.

#### **PSC mission critical system**

The Legacy Payment Management System (PMS) is scheduled for implementation at the end of June 1999.

The Payment Management System (PMS) offers a complete package of grant payment management services that includes payments, grant accounting, cash management, interface with agency financial management systems, specialized accounting reports and transaction, and detail accounting transaction documentation for core accounting systems. The PMS interfaces with the HHS operating divisions and cross-serviced agencies.

It was anticipated that the Re-engineered Payment Management System would be fully operational well before January 1, 2000, thus avoiding any Year 2000 (Y2K) compliance issues.

Unfortunately, progress on this initiative has been slower than anticipated. In the Fall of 1998, the ASMB in conjunction with PSC determined it was necessary to reevaluate which system would be the Y2K compliant system. To that end, PSC acquired expert outside advice and the resultant decision was to remediate the Legacy PMS. PSC is focusing all its efforts on that activity. Until the Y2K compliance of the Legacy PMS is certified, in-house resources have been redirected away from the Re-engineered developmental effort.

A fully documented contingency plan for the legacy Payment Management System is contained in PSC's BCCP. A summary of those contingencies follows:

- Use paper forms and manual transmission modes to process transaction if customer systems and FMS infrastructure are down.
- Use backup systems on PCs if FMS software is down.
- Reroute transactions to alternate facilities if primary Federal Reserve or Treasury sites are down.
- Use two processing routes (ACH, ECS) as backup to each other if one is down.
- Equip essential personnel with PCs to work at home if telephone service is down or facility is not accessible.

The contingency plan will be triggered when the system is down for two (2) days.

VIII. Other Management Information.

- a. On the first row, report your estimates of costs associated with year 2000 remediation, including both information technology costs as well as costs associated with non-IT systems. Report totals in millions of dollars. (For amounts under \$10 million, report to tenths of a million.)
- b. If there have been dramatic changes in cost, please explain.

On the next page, Exhibit 9, shows the current cost estimates, with explanations of changes, for the Year 2000 remediation, contingency planning and implementation, IV&V, and outreach.

Exhibit 9

Department of Health and Human Services  
 Y2K Total Cost Estimates - FY 1996 to FY 2000  
 (Dollars in Millions)

	FY 1996	FY 1997	FY 1998	FY 1999	FY 2000	Total
ACF Total	\$ -	\$ 0.500	\$ 3.960	\$ 22.425	\$ 0.500	\$ 27.385
AHCPR Total	\$ -	\$ 0.010	\$ 0.040	\$ 1.795	\$ -	\$ 1.845
AOA Total	\$ -	\$ 0.008	\$ -	\$ 0.600	\$ -	\$ 0.608
CDC Total	\$ -	\$ 3.000	\$ 9.400	\$ 6.800	\$ 1.610	\$ 20.810
FDA Total	\$ 0.200	\$ 2.000	\$ 7.250	\$ 22.928	\$ 2.000	\$ 34.378
HCFA - Internal	\$ 0.700	\$ 6.600	\$ 17.900	\$ 36.600	\$ 28.600	\$ 90.400
HCFA - External	\$ 6.100	\$ 6.900	\$ 68.100	\$ 234.366	\$ 121.400	\$ 436.866
HCFA - Supplemental	\$ -	\$ -	\$ 62.100	\$ -	\$ -	\$ 62.100
HCFA - Total*	\$ 6.800	\$ 13.500	\$ 148.100	\$ 270.966	\$ 150.000	\$ 589.366
HCFA - Contingency	\$ -	\$ -	\$ -	\$ -	\$ 311.200	\$ 311.200
HRSA Total	\$ -	\$ 1.200	\$ 1.400	\$ 10.000	\$ 1.900	\$ 14.500
IHS Total	\$ -	\$ 2.500	\$ 2.500	\$ 39.930	\$ 1.000	\$ 45.930
NIH Total	\$ 0.040	\$ 9.200	\$ 11.200	\$ 10.825	\$ 3.328	\$ 34.593
OIG Total	\$ -	\$ 0.075	\$ -	\$ 5.400	\$ 3.450	\$ 8.925
OS Total	\$ -	\$ -	\$ 0.500	\$ 3.880	\$ -	\$ 4.380
PSC Total	\$ -	\$ 0.200	\$ 6.500	\$ 8.983	\$ 1.380	\$ 17.063
SAMHSA Total	\$ 0.150	\$ 0.020	\$ 0.020	\$ 0.140	\$ -	\$ 0.330
HHHS Total	\$ 7.190	\$ 32.213	\$ 190.870	\$ 404.672	\$ 476.368	\$ 1,111.313

Previous Quarterly Report estimates have changed as follows:

FY 1999 -- Includes \$41.405 M add'l Y2K emergency funding as follows (instead of \$69.055 M requested in last report):  
 ACF \$16.2 M; AHCPR \$1.375 M; FDA \$9.6 M; HRSA \$0.0; IHS \$14.23 M.

FY 1999 -- FDA includes a decrease of \$6 M which was reported in the last report as an increase for voice and IV&V but is now included in the \$9.6 M increase (see note above).

FY 2000 -- OIG "most likely" estimate is \$3.45 million; \$5.2 million is a "pessimistic" estimate.

NOTE: In some cases, Y2K cost estimates reported represent estimated needs and exceed currently approved funding levels.

- c. If there have been significant changes to your agency's schedule, changes in the number of mission critical systems, changes to the number of systems behind schedule, please explain.

The changes in the number of mission critical systems are described in Section I of this report.

- d. Are there any concerns with the availability of key personnel?

Because of the concern for adequate staffing, the Department has taken additional steps to recruit and retain Y2K staff. The Office of Personnel Management (OPM) has granted a revision of the delegation of authority to the Department waiving dual compensation rules for retirees. The revision expands covered job categories beyond systems analysts, to include project managers, analysts, and health insurance specialists. With this expanded authority, HHS may hire up to 75 re-employed annuitants. PSC has hired one re-employed annuitant. HCFA has hired 41 re-employed annuitants. HCFA recruitment of these re-hires is primarily for work in regional offices supporting on-site efforts and oversight of Medicare contractors.

- e. Are there any other problems affecting progress?

HCFA is concerned about the possibility of Medicare contractors, fiscal intermediaries, and carriers leaving the program and notifying HCFA of their intent after June 1999. If this were to occur, then workload would have to be transferred to another contractor.

HHS also has a concern about the compliance status of State and local governments and entities that operate programs on behalf of the Federal government. Section II. j. provides information on HHS' work on this issue.

- f. Change Management Section: Minimizing Regulatory and Information Technology Requirements that Could Affect Progress on Fixing the Year 2000 Problem

HHS is reviewing statutory or regulatory requirements for HHS programs, particularly Federally-supported, State-run programs to identify any that should be postponed because these activities could complicate the Year 2000 efforts, divert resources from fixing systems, or otherwise aggravate the problem. The Department will inform the Office of Management and Budget and the President's Council for Year 2000 Conversion of those identified and the steps necessary to implement the postponement.

Mr. HORN. Well, you are right. They do. We only had two major programs that were 100 percent and that was Social Security and the Weather Service. So you can get your Social Security check down in Miami and the weather will be nice, so—[laughter.]

Ms. SNYDER. OK.

Mr. HORN. Except if you have been in Miami in the summer, you know there is no weather nice down there.

Ms. Snyder, in your statement you say you are currently using commercial off-the-shelf software to identify many of the same payment errors that would be identified by a recovery auditor. What benefits are you deriving from this software and how would a private recovery audit firm impact your efforts?

Ms. SNYDER. We have delivered a benefit from our correct coding initiative we started in 1996. I believe the cumulative savings have been identified at around \$830 million, about \$280 million annually. We also recently purchased or leased, if you will, some additional software edits which we are just now working through to make sure they satisfy Medicare policy before implementing them. So we don't yet know what the return on that particular investment will be, although we anticipate that it will be a good return on the investment.

It is an interesting question in how would recovery audit affect that. I think it is two different parts of the continuum, if you will. Most of these edits are focused at a pre-pay review and so they are to catch the error before it actually happens. So those edits are aimed at pre-payment. The post-pay audit would be looking at payments that got through that edit screen and went out the door and that we would need, then, to recover.

So I think they are two different parts of overpayment reduction.

Mr. HORN. Now has any of this been discussed with your authorizing committee or your Appropriations subcommittee, in terms of the systems you have developed and the attempt to remove the errors on overpayments? Has that question come up before either your authorizers or your appropriators?

Ms. SNYDER. I know that there have been discussions with them, certainly, over time. I haven't been party to any of those discussions, but I know that there have been questions about automated edit savings, recoveries, and that sort of question.

Mr. HORN. To improve a particular computer system and their human resources that go with that, do you have to go to the Appropriation subcommittees? Or do you have the authority, long-range, within Medicare, to do that?

Ms. SNYDER. There are really two types of funding authorities that we have. One, our administrative accounts are subject to the general appropriations process, which is where most of our software development would occur, would be in that annual appropriations process. We also have the mandatory funding and the Medicare Integrity Program, which is an appropriation that is funded for a period of time, for a continuing, indefinite, authorization.

Mr. HORN. Now, as I understand your filing here in your written statement, you note that in fiscal year 1998, the Department of Health and Human Services reported estimated improper payments of \$12.6 billion. This amount was down from \$20.3 billion in fiscal year 1997 and \$23.2 billion in fiscal year 1996. What initia-

tives, just for the record, were used by the Department of Health and Human Services to reduce the estimated amounts of improper payments? How would you sum that up?

Ms. SNYDER. I would say that it was a combination of efforts. As you know, our error rate and our payments are a series of complicated kind of computations. I think probably, in terms of importance, probably the correct documentation and billing, talking to providers to get them to understand how to bill certainly had, we think, a huge impact. We did a number of seminars. We went out to medical schools and talked to residents who were getting ready to establish practices about how to bill. So a lot of those kinds of educational efforts. We also——

Mr. HORN. Well, that is a very important point. Has any software ever been provided by Medicare for medical school graduates? Or do they just leave that to the private sector and go find your own?

Ms. SNYDER. There are two answers to that question. One, we provide billing software free of charge so that people will know how to bill through billing agents and to our intermediaries and carriers. But one of the things that we have done that I think is really innovative and it is going to have a pay-off is to put what is essentially computer-based instruction online for people to be trained in, again, how to bill claims, what are the right codes to use, and how do you get into the Medicare system.

I think we have reached over 10,000 people at hundreds of sites in hospitals. We have done 44 live seminars to work on this problem. We have reached more than 19,000 people this year alone. And if you look at our website, you might find it interesting. There is a pre-test and a post-test. We have actually been able to measure knowledge increase from taking it. And if you are interested in the pre-test or the post-test, you can find it at [www.Medicaretraining.com](http://www.Medicaretraining.com). And this is——

Mr. HORN. Mr. Kaplan will write that down and will give me a thorough analysis of that. You want to give him that again?

Ms. SNYDER. It is [www.Medicaretraining—one word—.com](http://www.Medicaretraining—one word—.com). And it has been a very successful web location. People are going into it and using it, physicians and hospitals.

Mr. HORN. Well, that is very helpful. In your statement, you said that you currently use commercial off-the-shelf software to identify many of the same payment errors that would be identified by a recovery auditor. And I guess the question would be what benefits are you deriving from the software and how would a private recovery audit firm impact them? As I mentioned earlier that do we need a new development for this particular audit approach or is it satisfactory in the private sector already and being used by people?

Ms. SNYDER. My assumption would be that recovery auditors would have their own software tools to apply to a recovery audit and would not need special development. What would be important is that recovery auditors understand the use of the definitions of medical necessity and how Medicare claims are treated for purposes of payment, which would be different than just applying software to that evaluation. That is to look behind the face of the claim.

Mr. HORN. My last question to you, Ms. Snyder, is, according to the April 1999 article in the Bureau of National Affairs Medicare

report, the Health Care Financing Administration has yet to issue guidance for health care providers to return funds they inappropriately received from Medicare. According to the article, providers that voluntarily identify overpayments attempt to send checks back to HCFA, only to have them returned. So, can you give us a sense of how vast that particular situation is in terms of dollars at stake? Or, how many people are involved in that?

Ms. SNYDER. I would need to get back with more specifics.

Mr. HORN. OK, without objection, it would be put at this point in the record.

[The information referred to follows:]

A copy of our June 1999 Program Memorandum, that gives instructions on tracking and reporting procedures for unsolicited/voluntary refund checks from providers/suppliers, is provided here as an attachment to the transcript.

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**PROGRAM MEMORANDUM**  
**INTERMEDIARIES/CARRIERS**


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 Department of Health  
 and Human Services

 Health Care Financing  
 Administration

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 Transmittal No. AB-99-33

 Date JUNE 1999
 

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**CHANGE REQUEST 791**
**SUBJECT: Tracking and Reporting Procedures for Unsolicited/Voluntary Refund Checks from Providers/Suppliers - Interim Instructions**

The purpose of this Program Memorandum (PM) is to provide general information and guidance on how to process unsolicited/voluntary refund checks received from providers/suppliers, including physicians and other practitioners. "Unsolicited/voluntary refunds" will be referred to as "voluntary refunds" throughout the remainder of this PM. The process includes identifying, tracking, and reporting of these voluntary refunds.

**I. General Information**—All Medicare contractors receive voluntary refunds (i.e. monies received not related to an open accounts receivable). Fiscal intermediaries generally receive voluntary refunds in the form of an adjustment bill, but may receive some voluntary refunds as checks or reported as credit balances. (Further guidance on credit balances will be forthcoming.) Carriers generally receive checks. Substantial funds are returned to the trust funds each year through such voluntary refunds.

**II. OIG Initiatives**—The Office of the Inspector General (OIG), working with the Department of Justice and the Health Care Financing Administration (HCFA), has two initiatives to help combat health care fraud and abuse and to encourage health care providers to comply with the rules and regulations of Federal health care programs. These initiatives are: Compliance Program Guidances and Corporate Integrity Agreements (CIAs). The Compliance Program Guidances are voluntary while the CIAs are mandatory. Both initiatives are designed to ensure that the providers/suppliers refund inappropriately received Medicare monies back to the trust funds. Due to these new initiatives, it is anticipated that Medicare contractors will experience an increase in the number of voluntary refunds.

Compliance Program Guidances are tailored to provide guidance, recommendations, and suggestions to health care providers/suppliers to assist in developing effective internal controls that promote adherence to applicable Federal and State law and the program requirements of Federal, State, and private health programs. These Guidances describe the fundamental elements of a compliance program. Among the suggestions and recommendations is that the health care provider/supplier should establish an internal self-monitoring process which will aid them in detecting potentially fraudulent and/or abusive practices which result in overpayments due to the Medicare program. Currently, Compliance Program Guidances have been published for the following entities: hospitals; home health agencies; clinical laboratories; and third-party medical billing companies. OIG will be issuing compliance program guidance for additional entities in the future.

CIAs are entered into between a health care provider/supplier and OIG as part of a global settlement of a fraud investigation. Under the CIA (which can be for a period ranging from 3 to 5 years), the provider/supplier is required to undertake specific compliance obligations, such as designating a compliance officer, undergo training, and auditing. The provider/supplier must report regarding their compliance activities on an annual basis to OIG, which is responsible for monitoring the agreements.

HCFA-Pub. 60AB



### III. Receiving and Processing Voluntary Refund Checks--

- Do not return any check submitted by a provider/supplier that is payable to the Medicare program.
- The following instructions do not supersede the present Carriers Manual - Part 2, §14017 and the Intermediary Manual - Part 2, §3974.1B that reference procedures for handling unsolicited refunds where there is a strong suspicion of fraud or an active investigation.
- Deposit all provider/supplier checks within 24 hours of receipt in accordance with the Carriers Manual - Part 1, §4414.3 and the Intermediary Manual - Part 1, §1416.3. This PM instruction will supersede the present Carriers Manual - Part 2, §7114.1 and the Intermediary Manual - Part 2, §2220.4 instructions.
- Upon deposit, apply monies against any established account(s) receivable. Make appropriate adjustments to the claims and/or the claim history file for the identified claims as you would normally do. Any unidentified portion of the check should be recorded in the account entitled "Other Liabilities" (suspense) per the HCFA-750 instructions. After performing the necessary research to identify the associated claims for the remaining monies, apply the check to that account(s) receivable from the "Other Liabilities" account.
- To assist you in capturing the information for HCFA reporting to the OIG, we have provided Exhibit 1 (Overpayment Refund) which the OIG will be forwarding to all entities with whom it has a CIA to assist HCFA in capturing data when the provider identifies a refund is due. Retain hard copies of these to prepare the reporting needed in Exhibit 2 (Voluntary Refund Checks). You are not required to automate either exhibit.

#### Exception - Checks with Conditional Endorsements

Conditional endorsements are statements on the face of the check or associated correspondence with the check which might suggest that the payer has discharged its obligation by writing, "payment in full" or "paid in full" or like phrases that the payer intends as satisfaction/extinguishment of the debt. Guidelines from the General Accounting Office (GAO) suggest that agencies must be extremely careful to avoid an unintended "accord and satisfaction", i.e., an agreement to accept in full payment an amount less than the amount claimed.

The following instruction applies to checks with a conditional endorsement:

- (1) To ensure that repayment of Medicare funds is handled properly, Medicare contractors will deposit such a check within 4 business days from receipt in the mail room.
- (2) Until the check is deposited, record the amount in "Undeposited Collections", per the HCFA-750 instructions.
- (3) Contractors must immediately notify the debtor by certified mail, the following statement: "This is to acknowledge the receipt of the repayment in the amount of \$XX, check number XX. The matter is being investigated, however, the amount of the repayment may be insufficient to discharge the obligation and the debt may not be fully extinguished." This may require more than one letter if the sender of the check is not the debtor or if the entity on whose account the check is drawn is not the debtor. In

those cases, somewhat different letters will need to be sent in order to be fully responsive to the proposed resolution. Letters must be dated and issued prior to the date of any check deposit. The infrequent receipt of checks with conditional endorsements should not negatively impact your production process. The standard letters needed to meet this requirement should be generated from a personal computer. Therefore, no system changes are required for your current automated letter processing.

- (4) Simultaneously, the Medicare contractor should telephone the regional office (RO) for guidance concerning acceptance of the check and any further actions necessary.

**IV. HCFA Reporting Requirements**--HCFA, will require at a minimum, during FY 1999, that the data requested on the voluntary refund check report (Exhibit 2) for the 3 month period subsequent to the effective date of this PM and an additional report through September 30, 1999 furnished to Office of Financial Management, Financial Services Group, Division of Financial Integrity. Exhibit 2 can be done on an Excel spreadsheet, therefore no system changes are required at this time to capture the data.

Exhibit 2 (Voluntary Refund Checks - Corporate Integrity Agreement) displays the reporting requirements for those providers/suppliers identified as having a "Corporate Integrity Agreement" with OIG. The following data should be captured: the provider name(s) and address(es), and the total dollar amount of refunds per provider during the reporting period. All voluntary refunds from providers/suppliers identified on the list provided by OIG should be reported on this report, in addition to those that identify themselves as having a CIA.

**V. Administrative Issues**--Central office will furnish the ROs a current list of the estimated 350 providers having a CIA with the OIG at this time. The list will consist of the provider/supplier name(s), number(s), type of facility, contractor specific identification name(s) and number(s), City, State, the years the agreement is in effect, and the effective date of the CIA. The ROs will furnish the contractors the list of CIAs, along with instructions that the list should be reviewed whenever a voluntary refund is received. This listing will assist contractors in meeting HCFA reporting requirements whenever providers/suppliers under a CIA do not identify refunds as such. Updated CIA listings will be furnished to the ROs, for distribution to the contractors, as received from OIG.

Contractors are to publish an article in their newsletter within 30 days of issuance of this PM. This article should inform all providers that if the data, as contained in Exhibit 1 (Overpayment Refund) were furnished when returning voluntary refund checks the monies would be credited timely and accurately. The article should also advise providers that if they are subject to a CIA they should report that when sending in a voluntary refund for credit and reporting to OIG.

**The effective date of all requirements within this Program Memorandum will be 30 days after issuance date.**

**These instructions are to be implemented within your current operating budget.**

**Contact person for this Program Memorandum is Maria Parmer (410) 786-5465 (or e-mail: mparmer@hcfa.gov).**

**This Program Memorandum may be discarded June 30, 2000.**

**OVERPAYMENT REFUND**

**TO BE COMPLETED BY MEDICARE CONTRACTOR**

Date: \_\_\_\_\_  
 Contractor Deposit Control # \_\_\_\_\_ Date of Deposit: \_\_\_\_\_  
 Contractor Contact Name: \_\_\_\_\_ Phone # \_\_\_\_\_  
 Contractor Address: \_\_\_\_\_  
 Contractor Fax: \_\_\_\_\_

**TO BE COMPLETED BY PROVIDER/PHYSICIAN/SUPPLIER**

*Please complete and forward to Medicare Contractor. This form, or a similar document containing the following information, should accompany every voluntary refund so that receipt of check is properly recorded and applied.*

PROVIDER/PHYSICIAN/SUPPLIER NAME \_\_\_\_\_  
 ADDRESS \_\_\_\_\_  
 PROVIDER/PHYSICIAN/SUPPLIER # \_\_\_\_\_ CHECK NUMBER# \_\_\_\_\_  
 CONTACT PERSON: \_\_\_\_\_ PHONE # \_\_\_\_\_  
 AMOUNT OF CHECK \$ \_\_\_\_\_ CHECK DATE \_\_\_\_\_

**REFUND INFORMATION**

**For each Claim, provide the following:**  
 Patient Name \_\_\_\_\_ HIC # \_\_\_\_\_  
 Medicare Claim Number \_\_\_\_\_ Claim Amount Refunded \$ \_\_\_\_\_  
 Reason Code for Claim Adjustment: \_\_\_\_\_ (Select reason code from list below. Use one reason per claim)  
*(Please list all claim numbers involved. Attach separate sheet, if necessary)*

*Note: If Specific Patient/HIC/Claim #/Claim Amount data not available for all claims due to Statistical Sampling, please indicate methodology and formula used to determine amount and reason for overpayment:* \_\_\_\_\_

**For Institutional Facilities Only:**  
 Cost Report Year(s) \_\_\_\_\_  
 (If multiple cost report years are involved, provide a breakdown by amount and corresponding cost report year.)

**For OIG Reporting Requirements:**  
 Do you have a Corporate Integrity Agreement with OIG? Yes No

**Reason Codes:**

<b>Billing/Clerical Error</b>	<b>MSP/Other Payer Involvement</b>	<b>Miscellaneous</b>
01 - Corrected Date of Service	08 - MSP Group Health Plan Insurance	13 - Insufficient Documentation
02 - Duplicate	09 - MSP No Fault Insurance	14 - Patient Enrolled in an HMO
03 - Corrected CPT Code	10 - MSP Liability Insurance	15 - Services Not Rendered
04 - Not Our Patient(s)	11 - MSP, Workers Comp. (Including Black Lung)	16 - Medical Necessity
05 - Modifier Added/Removed	12 - Veterans Administration	17 - Other (Please Specify)
06 - Billed in Error		
07 - Corrected CPT Code		

			EXHIBIT 2
<b>VOLUNTARY REFUND CHECKS</b>			
<i>Corporate Integrity Agreement</i>			
CONTRACTOR'S NAME			
CONTRACTOR'S NUMBER(S)			
REPORTING PERIOD	FROM	TO	
DATE OF REPORT			
PROVIDER NAME (S)	PROVIDER NUMBER (S)		TOTAL AMOUNT OF REFUNDS
			\$
THIS REPORT SHOULD BE USED TO REPORT ALL VOLUNTARY REFUND CHECKS RECEIVED FROM PROVIDERS/SUPLIERS HAVING CORPORATE INTEGRITY AGREEMENTS WITH OIG			

Mr. HORN. And then has the Health Care Financing Administration developed guidance for the acceptance of these returned overpayments?

Ms. SNYDER. Yes, sir. We have. We have issued those instructions to our contractors.

Mr. HORN. And, so that has already gone out, that guidance? There is nothing else to do on that part?

Ms. SNYDER. I believe that there will be more to do and that we need to followup to make sure that the guidance is, indeed, being followed. We have given the instructions.

Mr. HORN. OK, so we will hold the record open to get your response as to the degree to which it has been passed on to the contractors and the degree of achievement of the guidance that has been to-date.

Ms. Lee, do you have any comments, listening to this dialog?

Ms. LEE. No, sir.

Mr. HORN. OK. Well, you have all been fine witnesses and we appreciate you coming. I think we have got a lot of detail in the record to give us a feel about how this system might work should it become law, so thank you very much for coming.

We now go to the last panel of the day, panel three. And most of the audience has already left, so panel three, we can stay here for hours. OK, we have Mr. Dinkins, Mr. Kenny. Let us see. What happened to Mr. Kenny. He is accompanying you. OK. And Mr. Wilwerding is OK. Mr. Lyons, Mr. Booma, and Mr. Koehler. Good. Anybody behind you that needs to be sworn in besides Mr. Kenny? Anyone behind you? We might as well get them on the record. Clerk will get their names.

Anyhow, raise your right hands, please.

[Witnesses sworn.]

Mr. HORN. OK, the clerk will note that the six prime witnesses and their back-up of three are sworn in. So we will start with Mr. Dinkins, the executive vice president of the Profit Recovery Group International. And he is accompanied by Mr. Jack Kenny, the director for government of the Profit Recovery Group International. So, Mr. Dinkins, we are delighted to have you here.

**STATEMENTS OF PAUL DINKINS, EXECUTIVE VICE PRESIDENT, PROFIT RECOVERY GROUP INTERNATIONAL, ACCOMPANIED BY JACK KENNY, THE DIRECTOR FOR GOVERNMENT, PROFIT RECOVERY GROUP INTERNATIONAL, INC.; DOUGLAS R. WILWERDING, CHIEF EXECUTIVE OFFICER AND PRESIDENT, OMNIUM WORLDWIDE INC.; TERENCE LYONS, DIRECTOR OF ACCOUNTING, WALGREEN CO.; STEPHEN R. BOOMA, HEALTH CARE CONSULTANT; AND ROBERT KOEHLER, ATTORNEY-AT-LAW, PATTON BOGGS, ON BEHALF OF THE AMERICAN LOGISTICS ASSOCIATION**

Mr. DINKINS. Thank you, Mr. Chairman, for the opportunity to testify before this committee.

Profit Recovery Group provides a unique perspective because we are the largest and only public company in recovery auditing. We audit several trillion dollars in transactions annually; serve over 3,000 clients, including over half of the Fortune 1,000 here in the United States; and we have over 2,300 employees in 23 countries.

Recovery auditing is a professional service pioneered by my company roughly 28 years ago to identify and recover overpayments made to suppliers of goods and services. This practice has recovered billions of dollars in the private sector that would otherwise have remained undetected. The service is risk-free. Professional fees are paid from the proceeds of the recovered funds. The contingency fee basis for payment is the best possible approach we think because it focuses on performance and puts all of the risk on the contractor.

It is a fact that every organization experiences overpayments. Overpayments typically occur as a result of human and systemic errors. Recovery auditing is most commonly applied by PRG in large environments. Error rates are typically small, however a small error rate becomes very meaningful in a large environment. For example, most large, private-sector organizations have an accuracy level of 99.9 percent in the private sector. The error rate of 0.1 percent becomes meaningful as it represents \$1 million of loss for every \$1 billion of purchase.

As you have heard from prior testimony, government has already been benefiting from recovery auditing. The Army-Air Force Exchange System has employed recovery audit services since the early 1980's. AAFES makes purchases of roughly \$5 billion per year and the most recently completed audit of 1998 produced \$25 million in recovered moneys. To date, PRG has recovered over \$114 million for AAFES.

We are now finalizing a recovery audit demonstration program for the Department of Defense. Approximately \$25 million in overpayments have been identified to date with over \$4 million of this amount recovered or in the process of being offset. The balance is in various stages of recovery. This represents a rate of recovery of 0.40 percent or roughly \$4 million per \$1 billion of purchase. And, Mr. Chairman, this rate of recovery is pretty much synonymous with what we experienced at AAFES.

The program within DOD is now being expanded to the balance of the Defense Working Capital Fund. In our view, the expansion was limited to the Defense Working Capital Fund because it is a revolving fund and all recovered moneys go back to the fund. We recommend expansion of the program to the balance of the appropriated fund areas quickly to optimize benefits. Prior to the bill under review, there has been no incentive for an agency to conduct recovery audits in appropriated fund areas because moneys recovered would otherwise go back to Treasury.

Summarizing the benefits to government, everyone wins. Agencies will have money returned. General government, through the Treasury, will recover funds. The taxpayer sees his money well-spent. And the Congress improves executive management. Hence, it seems impossible to question the value of expanding the process.

Mr. Chairman, while we have suggestions to improve the language in this legislation, let me say at the outset that we very strongly support this bill. We believe that the concept has been well-tested over decades in the private sector—roughly 9 years at AAFES and in the current demonstration program.

There are several recommendations in my written testimony and I would like to focus on only two of them. First, in section 3562,

we suggest changes to section 3. We respectfully submit that where the private sector has attempted to implement internally its own recovery audit programs, it is done only after years of experience with a professional service. Even private sector companies that have developed some internal capability have done so in conjunction with ongoing external professional services.

Next, in section 3564. This section is written with recoveries of appropriated funds in mind. Revision is suggested and required to specify how moneys from revolving funds would be treated, such as the Defense Working Capital Fund; AAFES, which is not an appropriated fund; or HCFA, which is a trust fund. It is our understanding that all moneys, less contractor fees, should go back to these revolving funds.

In summary, Mr. Chairman, we believe this legislation is both well-crafted and well-intentioned. With the incorporation of the recommendations proposed in our testimony, this bill will provide a powerful tool for all segments of government to recover overpayments, correct problems, enhance payment processes, and adopt private sector business practices. Thank you, Mr. Chairman.

[The prepared statement of Mr. Dinkins follows:]

**Congressional Testimony**  
**“Government Waste Corrections Act”**

June 29, 1999  
Paul Dinkins  
Executive Vice President  
The Profit Recovery Group International, Inc.

Thank you Mr. Chairman for the opportunity to testify before this committee. My name is Paul Dinkins, Executive Vice President of The Profit Recovery Group International, Inc. (PRG).

In my testimony I will provide:

- I. A walk-through of the “recovery audit” process
- II. Recommendations for improvements to the bill under discussion
- III. An update on our work within government

### **I. The Recovery Audit Process**

Recovery auditing is a professional service pioneered by my company roughly 28 years ago as a safeguard against the financial leakage that occurs in the purchase and payment of goods and services. Recovery auditing is a professional service and an accepted business practice to identify and recovery overpayments inadvertently made to suppliers of goods and services. This practice has recovered billions of dollars in the private sector that would otherwise have remained undetected. The service is risk free. Professional fees are paid from the proceeds of the recovered funds. The contingency fee basis for payment is the best possible approach, we think, because it focuses on performance and puts all of the risk on the contractor. Private sector fees average approximately 30% of amounts recovered. Government programs to date have a contingency fee of 20.2% based on our GSA Multiple Award Schedule contract for Recovery Auditing.

It is a fact that every purchase and bill paying organization, regardless of size or quality, experiences overpayments. Overpayments typically occur as a result of human and systemic errors. In our constantly changing environment as one problem is fixed another surfaces. A major role of the recovery audit process is to provide a Monday Morning quarterback’s view of why errors occurred and what can be done to mitigate them. This is an extremely valuable side benefit of the process.

Recovery auditing is most commonly applied in large purchase and payment environments. Error rates are typically small. However, a small error rate becomes very meaningful in large environments. For example, most large private sector purchase and payment organizations have an accuracy level of 99.9%. The error rate of .1% becomes meaningful as it represents \$1 million of loss per \$1 billion of purchases.

Every day more large organizations utilize recovery audit professional services. We have served over half of the Fortune 1000 companies in the US and major companies in 22 other countries.

Decades of experience demonstrate that the error rate in terms of identified and recovered overpayments has remained relatively static. It would be reasonable to assume that with systems advancements, error rates should be mitigated. However, the rapid proliferation of electronic



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commerce has had two distinct effects. First, it has dramatically increased the amount of electronic media that can be interrogated using proprietary software to identify all errors. Second, errors that occur in an electronic environment are often not limited to a single transaction, but rather repetitive across large volumes of transactions.

Audits are conducted each year on prior year purchase and payment transactions. The process involves a complete review of all related transaction media such as supplier contracts, correspondence, purchase orders, invoices, paid history files, vendor statements, etc. These transaction records are reassembled as part of the audit including both physical and electronic media. Much of today's purchase and payment transactions are electronic in nature. Therefore, sophisticated software applications are utilized to search historical records to identify potential overpayments along with other sources of documents that may be paper, microfilm, fiche, or images.

Summarizing the benefits to the government; everyone wins. Agencies will have money returned, general government through the Treasury will recovery funds, taxpayer sees his money well spent, and the Congress improves executive management. Hence, it seems impossible to question the value of expanding this process.

## II. Recommendations for Improvements to the "Government Waste Corrections Act"

Mr. Chairman while we have suggestions to improve the language in this legislation, let me say at the outset that we very strongly support this bill. We believe that the concept has been well tested over decades in the private sector, nine years at AAFES and in the current demonstration program.

There are several recommendations we have to improve the current version of the bill including:

1. §3561 (3). Change to include ...to identify overpayments *and under deductions* made by executive agencies...
2. §3562 (1). Recovery audit requirement – We recommend that the threshold for application of recovery audit services be increased from \$10,000,000 to \$500,000,000. The reason for this recommended change is that the potential for recovery for an executive agency of only \$10,000,000 would be an estimated range of \$10,000 to \$40,000. These small amounts will not justify the administrative burden and program costs for everyone involved.

Furthermore, we suggest changes to section (b) Procedures (3). The current language provides for "the head of an executive agency to conduct recovery audits directly, by procuring performance of recovery audits by contract or by any combination thereof." We respectfully submit that where the private sector has attempted to implement internally, it is done so only after years of experience with a professional service because there is no experience base or methods to deploy. Even private sector companies that have developed some internal capability have done so in conjunction with ongoing external professional services.

3. §3563 (a). Recovery audit model programs – If the use of "model programs" is meant to hasten implementation we are supportive. If however, it implies still another stage of

demonstration program, we think this will slow the process down. We there suggest elimination of "model."

4. §3563 (a) (1) change to read "be focused on agencies that represent the greatest possible benefit in terms of monies recovered; and (2). Change to read..."continue in, as in the private sector, as long as benefit is derived from the program in terms of monies recovered.
5. §3564. This section is written with recoveries of appropriated funds in mind. Revision is required to specify how monies from revolving funds will be treated, such as the Defense Working Capital Fund, or HCFA Trust Fund. It is our understanding that all monies, less contractor fees, should go back to these revolving or no year money funds.
6. §3565 (b) Awards – We recommend the language be modified in this section such that any cash award does not create a conflict with the performance of recovery audit services. It is our understanding that there are already programs in place to recognize and reward Federal Employees for outstanding performance. If the "awards" language in the Bill is to be retained, it should be specific as to "support and facilitation" of the recovery audit program, to ensure that Government and Contractor personnel are not working at cross-purposes.

### **III. Update on Recovery Auditing Services within Government:**

The Profit Recovery Group provides a unique perspective on the recovery audit industry because:

- We are the largest and only public company in the industry with a market capitalization over \$1.2 billion
- We bring world wide experience auditing several trillion dollars in transactions annually
- PRG has served over 3,000 clients including over half of the Fortune 1000
- Staff is comprised of over 2,000 employees in 23 countries
- PRG's global practice spans 28 years of experience.

As such, we understand industry best practices and norms and are well qualified to provide expert opinions on practices and policies related to the purchase and payment of goods and services. Based on our experience to date, we believe that government will benefit from recovery auditing even more than the private sector.

On average, our practice in the private sector recovers approximately .1% of annual purchase volumes or \$1 million per \$1 billion of annual purchases.

Government has already benefited from recovery auditing. In fact, the Army Airforce Exchange System (AAFES) has benefited from recovery audit services since 1991. AAFES makes purchases of roughly \$4.95 billion per year. The most recently completed audit of 1998 purchases and payments yielded \$24,455,909 in recovered monies or .49% of purchases (\$4.4 million per \$1 billion of purchases). To date, PRG has recovered over \$100 million for AAFES.

We are now finalizing a recovery audit demonstration program for the Department of Defense. Approximately \$29 million in overpayments have been identified to date with over \$4 million of this amount recovered or in the process of being offset. The balance of \$25 million is in various stages of recovery. This represents a rate of recovery of .48% or \$4.8 million dollars per \$1 billion of purchase. The program within DoD is now being expanded to the balance of the

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Defense Working Capital Fund. In our view, the expansion was limited to the DWCF because it is a revolving fund and all recovered monies go back to the fund. We recommend expansion of the program to the balance of the appropriated fund areas quickly to optimize benefits for DoD. Prior to the bill under review, there has been no incentive for an agency to conduct recovery audits in appropriated fund areas because recovered monies for the most part would go back to Treasury.

We do not have a broad enough sampling of results within Government to accurately project the benefit of the program. However, we can very safely estimate the range of benefit to be at minimum the .1% experienced in the private sector up to and beyond the .48% currently experienced with the DoD demonstration program. We understand that there will be different issues and opportunities for different types of purchases audited. It is also worth mentioning that we typically produce higher results in the second and third years with a new client based on improved information access, understanding of the client and greater participation and support by the client. Therefore, we estimate the rate of recovery across audit of government payments for goods and services to be in the range of .3% or \$3 million per \$1 billion of annual purchases. Having said that, we believe that the largest single opportunity for recovery of overpayments is within HCFA. Internal government reviews of HCFA have indicated significant overpayments.

Using the .3% estimated rate of recovery, annual benefit from program expansion to all of the Department of Defense alone is \$510 million. This is based on annual DOD purchases of goods and services of \$170 billion. The first year of program expansion would produce an added benefit because at minimum, the last three fiscal periods of purchases and payments can be audited at one time producing a one-time recovery of \$1.53 billion.

We are now just beginning a program with the U.S. Department of Veteran's affairs with purchases of approximately \$4 billion annually. The first program implementation will cover the most recent three years or roughly \$12 billion in purchases. PRG provides services to over 600 other healthcare providers.

I have recently provided testimony to The Subcommittee on National Security, Veterans Affairs, and International Relations on June 16<sup>th</sup> on reasons to reform the Prompt Payment Act. We believe these recommendations will greatly enhance the government's ability to take advantage of cash discounts, improve cash management, and reduce interest penalty paid. In fact, one recommendation alone will save the Department of Defense in excess of \$100 million annually in cash discounts. As our work within government progresses we will continue to highlight recommendations that will improve business practices and mitigate future overpayments.

## Summary

In summary, Mr. Chairman, we believe this legislation to be both well crafted and well intentioned. With the incorporation of the recommendations proposed in our testimony, this Bill will provide a powerful tool for all segments of the government to recover overpayments, correct problems, enhance payment processes, and adopt private sector business practices. This will result in an ongoing process providing the recovery of billions of dollars that would otherwise remain undetected.

Thank you Mr. Chairman.

**Biography  
For  
Paul Dinkins  
Executive Vice President  
The Profit Recovery Group International, Inc.**

Paul Dinkins joined the Profit Recovery Group International in 1992. In his role as Executive Vice President, his responsibilities include business development and account management for Government programs and large private sector clients. He has overall responsibility for all government activities. Mr. Dinkins played an instrumental role in preparing the company for growth, expanding the revenue base from \$18 million to \$300 million in 1999 across 23 countries, and taking the company public in March 1996. PRG's client services are focused on the identification and recovery of overpayments inadvertently made to suppliers of goods and services with fees based on a negotiated share of the monies recovered. This win-win business practice has grown to include over 3,000 clients' worldwide. PRG has served over half of the Fortune 500 companies with over 2,000 employees. Since taking the company public in 1996, market capitalization has surpassed \$1 billion. Mr. Dinkins is an experienced international business executive with years of global client acquisition and account management.

Mr. Dinkins has played a significant role in the development of programs for Federal and State Governments over the last five years. This has included participation in the development of legislation related to Recovery Auditing including the 1996 and 1998 Defense Authorizations Acts, as well as the initiation of programs within the Department of Defense, and Veterans Affairs. Mr. Dinkins has spent a great deal of time educating government agencies to the benefits of recovery auditing and has gained a GSA Multiple Award Schedule contract specific to Recovery Auditing that provides an efficient contracting vehicle for recovery auditing services. He is actively engaged in the current demonstration program nearing completion and participating in program expansion within the Department of Defense. The first year program expansion benefit for the Department of Defense is estimated to exceed \$2 billion in recovered monies. He is also actively engaged with most of the large federal agencies regarding application of recovery auditing programs.

Mr. Dinkins prior experience spans 18 years of Management Consulting services. From 1982 to 1992, Mr. Dinkins served in various positions, most recently as a Partner, with Senn-Delaney Management Consultants. In 1992 Mr. Dinkins and his partners sold the firm to Arthur Anderson LLP. His consulting background includes re-engineering and performance enhancement programs for financial areas, operations and distribution.

Mr. Dinkins is a 1974 graduate of the University of Pittsburgh. He and his family reside on their ranch in the foothills of the Rocky Mountains in Colorado.

Mr. HORN. Well, I thank you. I am very impressed by the detailed recommendations you have made and that is going to be very helpful to us when we offer a manager's amendment, namely mine, to the markup. And so thank you very much for delving into that. I appreciate it. And we always welcome any of you that have some comments on the specific language of the bill. That is most helpful to us.

We now go to Mr. Wilwerding. Thank you very much for coming. He is the chief executive officer and president of Omnium Worldwide Inc.

Mr. WILWERDING. Thank you, Mr. Chairman, and good afternoon. On behalf of all the people at Omnium Worldwide, founded 30 years ago, I want to offer into testimony our suggestions and our analysis of this legislation and the important impact it can have on the Federal Government.

Omnium Worldwide is both a domestic and international specialist in cost containment and receivable management issues. Omnium has offices in nine States as well as in Sao Paulo and Rio de Janeiro, Brazil, and Mexico City, Mexico. We operate on issues from overpaid insurance claims to precharge often delinquent accounts. Omnium recovers hundreds of millions of dollars each year for our clients.

I have been asked to speak today because of my 14 years of experience in this industry. I commend the committee's desire to address the problem of overpayments within Federal agencies. My objectives today are as follows. First of all, to testify on the need for overpayment identification and recovery within Federal agencies. Second, to outline the size and potential of the overpayment market, specifically in the private health care industry, and the purpose of extending this potential to Federal agencies. Third, to speak on everyday practices of overpayment recovery in the private sector. And, finally, to offer some suggested changes to the language of H.R. 1827 that may enhance the effectiveness of the legislation.

Our company's existence and that of the industry specifically formed around the identification and recovery of medical benefit overpayments is a testament to the problem in the marketplace and the need for this legislation. As defined, overpayments are not fraud, but common administrative and clerical errors, as I believe Ms. Snyder pointed out earlier today. One of our companies, Accent Insurance Recovery Solutions is the leading provider of overpayment identification and recovery for commercial insurers, managed care, and self-funded organizations.

Health care benefit overpayments occur when funds are paid out errantly. Numerous reasons exist for these overpayments, including duplicate payments, payments to ineligible beneficiaries, calculation errors, and payments to wrong providers. The vast majority of these dollars do not deal with medical necessity. These types of overpayments are a large percentage of the estimated \$12.6 billion overpaid by Medicare in 1998.

Private overpayment recovery firms employ state-of-the-art proprietary technology to identify, validate, and recover claim overpayments. Commercial payers outsource these functions because they are not the competency of the payor, pursuing these claims is not a cost-effective allocation of resource of the payor, and the capital

investment to develop the technology infrastructure to carry out these functions is not a primary investment. Given that private payers use these services on a contingency fee basis, there is no fund outlay to realize the benefits of the service. The entire burden of the function falls on the vendor or contractor.

In the majority of cases, Accent is asking the provider of service, physician, hospital or clinic for the refund. Both expertise and professionalism are mandatory as we work with the largest providers across the country daily, resolving both clear-cut and complicated overpayment situations. These cooperative relationships are of paramount importance to the provider, the payor, and our company. The result is a very high recovery rate and no provider complaints.

Estimates are that 4 percent of total claims paid by the private health insurance sector are overpaid. This results in nearly \$7.6 billion in overpayments for commercial payers. Contrast this with the reported 7 to 16.5 percent error rate for Medicare. The dollars available for identification and recovery are staggering. And, at this point, Mr. Chairman, I would like to offer in that I do state the 7.5 to 16.5 percent. There is record of 16.5 percent being the actual error rate when Medicare includes not just claims that are entirely overpaid, but also those that are partially overpaid, which does raise the estimate of dollars being lost to overpayment annually.

Private recovery firms average recovery rates between 50 and 70 percent of dollars validated as overpaid. We believe the success in the private sector can be mirrored in the public sector. Private recovery firms recover from the same providers that are being overpaid by Medicare. The claims payment errors are being made by fiscal intermediaries and carriers hired by HCFA to administer the claims. These contractors are the very same carriers who hire private recovery firms to recover their overpaid dollars on their commercial insurance portfolio.

Over the last 3 years, the estimate is that HCFA has overpaid some \$56 billion in both fraud and waste. In that same time period, recoveries from fines and restitutions have dropped 65 percent from 1997 to 1998, down to \$321 million. Recoveries for the first half of 1999 are estimated at \$176 million. By employing private recovery firms, the Medicare Trust could realize conservatively billions in savings in the next 3 years.

H.R. 1827 is an important step toward implementing the mandatory use of auditing firms. A few areas of emphasis would enhance the legislation and ensure success of this most important effort this committee is now undertaking. First, we suggest that both auditing and the recovery function be mandated. As the legislation currently reads, the recovery function is assumed, but not specifically stated. Auditing without recovery will not yield the results desired.

Second, timeframe should be added to specify the appropriate lapse between the audit findings and the beginning of the recovery activity. This critical element determines the recovery success.

Third, set-offs, while effective, are an extreme burden on providers and their accounting systems and I wish Mr. Walden was here with his experience in the hospital board. I am sure he would at-

test to the fact that the accounting of set-offs is very difficult for the provider to handle.

Fourth, the committee should be very cautious in allowing agencies to opt out of the program. Deferrals will greatly reduce the recoveries and available benefits from this prudent legislative act.

Fifth, some types of overpayment, audit, and recovery may incur expense that exceeds the 25 percent fee cap. And here I echo Mr. Peterson's testimony.

Finally, the committee should consider the financial net benefit and allow some fee arrangements to exceed the cap where appropriate.

H.R. 1827 is a very important step in the pursuit of merging the private sector efficiency and expertise with the government improvement opportunities. I appreciate the chance to address the committee and welcome any questions.

[The prepared statement of Mr. Wilwerding follows:]

**Testimony of Doug Wilwerding  
Chief Executive Officer  
Omnium Worldwide Incorporated  
Omaha, Nebraska**

**Before the Subcommittee on Government Management,  
Information, and Technology**

**Hearing on H.R. 1827,  
"Government Waste Corrections Act"**

**June 29, 1999**



Good afternoon. Mr. Chairman, I want to thank you and the members of the committee for inviting me to testify today.

My name is Doug Wilwerding. I am the Chief Executive Officer of Omnium Worldwide, headquartered in Omaha, Nebraska. Founded 30 years ago, Omnium is a domestic and international specialist in cost containment and accounts receivable. Omnium has offices in Arizona, Colorado, Illinois, Iowa, Minnesota, Nebraska, Wisconsin, Virginia, and Texas. Our international locations are Sao Paulo and Rio de Janeiro, Brazil and Mexico City, Mexico.

From overpaid insurance claims to pre charge off and delinquent accounts, Omnium recovers hundreds of millions of dollars each year for our valued business partners. I was asked to speak to the committee today because of my twelve years of experience in the consumer debt and overpayment industries.

I commend the committee's desire to address the problem of overpayments within federal agencies. HR 1827 will allow federal agencies to benefit from the services that recovery audit firms have been providing to the private sector for years. My objectives today will be:

- To testify to the need for overpayment identification and recovery within federal agencies.
- To outline the size and potential of the overpayment market in the private health care industry with the purpose of extending this potential to federal health agencies.
- To speak on the every day practice of overpayment recovery in the private sector.

- To tell you where, in my experience, some changes, additions, and improvements could be made to HR 1827. Small changes to the bill will allow the committee to maximize the impact of the bill, ultimately recovering more money for the federal government.

If there are any doubts about the existence of the need for this type of legislation, let my company, customers, and competitors be the living, breathing example of the \$100 million-plus health overpayment recovery industry in the private sector. One of the divisions of my company, Accent Insurance Recovery Solutions is the nation's largest health overpayment recovery firm. A healthcare overpayment is the result of too much money paid out by the health insurance claims administrator to a provider or an insured. Indeed, healthcare overpayments account for a large portion of the \$12.6 billion of improperly paid Medicare claims in 1998. Reasons for overpayment include duplicate payments, calculation errors, and payments to the wrong provider. Entities that outsource overpayment functions are indemnity insurance companies, managed care organizations and self-insured companies.

Private overpayment recovery firms identify and recover overpayments using state of the art proprietary technology. The private insurance sector uses services like Accent's because identifying and recovering overpayments is not their core competency. Their expertise is in paying claims in a timely manner and in providing customer service to their many insureds or members.

Outsourcing overpayment identification and recovery is an attractive option to private insurance companies because it requires no long term financial commitment or investment. They do not need to commit financial or technical resources developing identification and recovery software, hiring and training recovery specialists, and building entire operations around the identification and recovery function.

In addition, private recovery firms recover overpayments on a contingency fee basis. A fee is not taken unless the account is successfully recovered. Because of this, there are no start up costs associated with recovery auditing. And, outsourcing overpayment recovery takes the case management process away from the administrator and allows experts like Accent to manage the entire process from referral to closure.

In the majority of cases, the overpayment is being pursued from the provider of the service (physicians, hospitals, clinics, *etc.*) for the refund. These providers have busy billing and accounting departments and are not always aware of the overpayment. When contacted, they are provided with the information they are going to need to locate the overpayment in their system. Sometimes the refund is relatively easy to recover; sometimes discrepancies exist that require further clarification. Because Accent recovers overpayments for so many insurance companies all paying claims to the same providers across the country, our cooperative relationships with providers are very important in achieving a consistent, high rate of recovery for our clients.

There is a very general acceptance of the work performed by private recovery firms, which is evidenced with the amount of money recovered. Overpayment recovery is problem solving in which the end result is a win-win situation for both parties. The recovery process is a professional exchange of information with the goal of recovering the money for the payer while also alleviating the provider from resolving account discrepancies, which can be a target area for auditors.

The terms 'overpayment' and 'recovery' are everyday vernacular to the health care industry. Insurance companies are well aware of their overpayment volumes. An outstanding overpayment can distort an insured's claims history and serve as a loss to the insurance company or the group for which they are administering claims. Recovered overpayments, however, add substantial amounts of money back to their bottom line.

It is estimated that 4% of total claims paid by the private health insurance sector are overpaid. This results in nearly \$3 billion in overpayments in the private sector annually. The error rate in the public sector is higher. In the Medicare program, HHS and HCFA estimated a 7% error rate in 1998, however, when totally overpaid and partially overpaid claims are included, the error rate is 16.5%.

Private recovery firms have, on average, recovery success rates of half, in many cases 60-70 percent of the dollars referred. Private sector success can be mirrored in the public sector. Private recovery firms recover overpayments from the very same providers that are being overpaid by Medicare. In addition, these overpayments are made by fiscal intermediaries, carriers and administrators hired by the HCFA to administer claims. These administrators are in most cases private insurance carriers - the very carriers that make overpayments on non-government business. If HCFA outsourced the identification and recovery of overpayments, the 50-70 recovery percentage that is obtained for its private sector companies may be applied to Medicare overpayments, returning billions of dollars to valuable federal programs.

The federal government has the opportunity to capitalize on overpayment recovery itself or through federal programs. The Federal Employee Benefit Program administered by the Office of Personnel Management is the world's largest employer sponsored health insurance program with nine million lives. The Military Health System provides coverage for another eight million lives, and the Medicare program provides coverage for 39 million citizens. Medicare alone accounts for a significant portion of the federal budget.

In the last three years, Medicare has estimated that it made \$56 billion of improper payments due to fraud and overpayments. It is unclear what requirements HCFA has of its intermediaries and carriers to identify and recover these overpayments.

We do know that little is being recovered. Recoveries through fines and restitution dropped 65% in 1998 to \$321 million. Recoveries for the first half of fiscal year 1999 are \$176 million. These recoveries have little impact on the billions improperly paid.

HR1827 is an important step toward implementing the mandatory use of recovery auditing firms, however, with a few amendments, the impact the bill would have on the amount of money returned to the federal government would be great.

HR 1827 does not state strongly enough that recovery, along with identification, is mandatory (Section 3562.c.b.). Mandatory identification without mandatory recovery of the identified overpayment does not go far enough toward maximizing the return to the federal government. Time frames should be placed on when the recovery process must begin after the overpayment has been identified. It is very important to begin the recovery process as soon as possible after the overpayment has been identified, otherwise, the identified overpayment will only become aged, unrecoverable, and an administrative hassle to the overpaid party. Some of the \$56 billion improperly paid by Medicare in the last three years may indeed be unrecoverable at this time.

In addition, HR 1827 states that overpayments may be deducted from future payments, but in many cases this will not be efficient. Federal agencies need to have proactive recovery procedures in place.

We also feel that an agency should not be granted the authority to procure recovery audit contracts itself as mentioned in Section 3562.b.3. This could result in a conflict of interests. Audit control should be centralized to an independent party.

It will be very important to carefully monitor, and possibly, limit the reasons and frequency that an agency can 'opt out' of the recovery audit plan. This could have potentially detrimental effects on the recovery audit project. Without careful scrutiny, agencies could exercise this clause completely eliminating the benefits of the bill.

In addition, while executive agency consultation by the Director is important, the Director should also consult potential contractors. These private industry experts could lend valuable expertise to the Director and help identify agencies upon which the enactment of the bill would have the greatest impact.

A fee cap of 25% may be unreasonable for some types of overpayment recovery. Depending on the type and age of the overpayment, recovery may be significantly more difficult to achieve. A recovery auditing firm may need to employ more resources that elevate their costs to perform the recovery. In order to stay profitable, a fee of more than 25% may have to be charged.

The general concept of HR 1827 is valid and greatly needed within federal agencies. Overpayment identification and recovery is a common practice in the private sector and is responsible for returning millions of dollars to private health insurance companies. If HR 1827 were amended to specifically include health overpayments, it would have an even greater impact on the overpayment problem within the federal government by opening up the billions of dollars of improperly paid Medicare claims to recovery auditing firms.

Thank you very much for inviting me today to share my views with the Committee.

**Douglas R. Wilwerding, CCAE**  
 CEO & President, Omnium Worldwide, Inc.  
 Vice Chairman of the Board of Directors

**Professional History**

1998 to Present	<b>President and Chief Executive Officer</b> Omnium Worldwide, Inc.
1998 to Present	<b>Vice Chairman of the Board of Directors</b> Omnium Worldwide, Inc.
1996 to 1998	<b>President</b> Accent Insurance Recovery Solutions, a division of Omnium Worldwide
1990 to 1996	<b>Chief Operating Officer</b> Accent Insurance Recovery Solutions, a division of Omnium Worldwide
	<b>Senior Vice President</b> Omnium Worldwide, Inc.
1986 to 1990	<b>Corporate Marketing Director</b> Accent Service Company, Inc., a division of Omnium Worldwide

**Associations**

1997 to Present	<b>Health Insurance Association of America</b> Chairman, Affiliated Services and Products Committee
	<b>Omaha Chamber of Commerce</b> Board of Directors, Leadership Omaha Alumni Association
1991 to Present	President, Leadership Omaha Alumni Association
1997 to 1998	Chairman, Outstanding Young Leader Award Committee
1994 to 1996	Member, Outstanding Young Leader Award Committee
1991 to 1996	Graduate, Leadership Omaha
1994 to Present	<b>Omaha Creighton Preparatory School</b> Development Committee
1990 to Present	<b>Society of Certified Credit Executives</b> Certified Member
1991 to 1994	<b>Great Plains Girl Scout Council</b> Board of Directors
1994 to 1996	<b>Christian Urban Education Society</b> Team Leader
1989	<b>Douglas County Young Republicans</b> President
1987 to 1991	<b>Junior Achievement of Nebraska</b> Consultant for "Project Business"

**Past Testimony**

**U.S. House of Representatives, Committee on Ways and Means**  
 October 9, 1997

**Accomplishments**

1996	<b>Ten Outstanding Young Leader Award Recipient</b> Presented by Omaha Jaycees
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**Certifications**

1992	Certified Collection Agency Executive by the Society of Certified Credit Executives
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**Education**

1985	University of Denver - B.A., Marketing and Finance
1986	University of Denver - M.B.A., Marketing

Mr. HORN. Thank you very much for that helpful statement. Mr. Terrence Lyons is director of accounting, the Walgreen Co.

Mr. LYONS. Mr. Chairman, thank you for the opportunity to appear before this committee. My name is Terry Lyons and I am a director at the Walgreen Co. Walgreen's is a leading drug and general merchandise retailer with fiscal year sales for 1998 of \$15.3 billion. My responsibilities include the management of our outsourced recovery audit process. My testimony provides a private sector view of recovery audit benefits and how the Walgreen Co. uses the process.

Walgreen's recognized long ago the benefits of using a professional service provider to identify and recover overpayments. Purchasing and payment systems used by any volume intensive organization like Walgreen's are designed to be cost-effective and to provide for maximum through-put to ensure timely payment of supplier invoices. However, mistakes occur, whether through human error or systemic breakdowns.

Our experience has indicated that human error is the most common contributing factor in payment errors. Human error can never be entirely eliminated. Therefore, the need exists for a safety net to audit payment transactions for accuracy and validity, recover any overpayments, and to identify why overpayments occur.

The most attractive advantage for utilizing a recovery auditing service is that there is no risk or investment required. The development of internal controls and/or programs to conduct comprehensive recovery auditing is simply not 100 percent cost-effective. We use the largest service provider, the Profit Recovery Group International who has broad experience in many operating environments.

The value of recovery auditing to us is apparent in the dollars recovered from the two most recent audit years. The audit of our 1996 purchases was completed in October 1998 and we recovered \$16.9 million in overpayments on a purchase volume of \$8.5 billion. The audit of our 1997 purchases is just now being completed and we expect to recover approximately \$17.5 million in overpayments against a purchase base of \$9.7 billion. Although the numbers are large, nearly \$35 million just over the past 2 audit years, they actually indicate an error rate of only about 0.19 percent. Meaning that 99.8 percent of our payable transactions were processed and paid correctly.

The success of our recovery audit activity is based on a set of mutually identified duties and expectations from both parties. We, as the client, must fully support the process. We must provide our service provider with the access to all required media, both electronic and paper, needed to research, identify, and document any instances of overpayments and/or underdeductions. Points of contact are established within the purchasing, transportation, accounts payable, accounting, and finance areas to liaison with contractor personnel to provide whatever support is required.

Our recovery audit firm has responsibilities and duties to ensure the success of their effort. They gain a full understanding of our purchasing and payment systems for both electronic and paper transactions. They meet and develop good working relationships with all of the designated points of contact within our organization



and they protect our vendor relationships. In short, we expect our contractor to function in a fully outsourced manner that represents the interests of the Walgreen Co.

The question of why Walgreen's would employ an outside firm to do recovery auditing rather than doing it internally has certainly occurred to you. The answer is simple. As a company, we have chosen to invest our developmental dollars in what we do best: systems and technology that provides improved productivity within our stores and improved customer service. Also the investment in technology and resources needed to develop this kind of capability in-house could be cost-prohibitive. We find it attractive to outsource this function to a professional recovery audit firm. They have the technology, the resources, and the expertise to do what they do best.

In summary, Mr. Chairman, we have found the use of professional recovery audit services to be invaluable in both recovering passed-over payments and improving internal controls. Among the major benefits: We recover millions of dollars each year, we incur no financial burden, the process is not disruptive to our normal operations, and the nature of the service is ongoing with benefits, year after year. As a private sector user of audit recovery services, I believe recovery auditing services for the government is a terrific idea. It will result in the recovery of a great deal of money and further demonstrate how government can benefit from private sector business practices. Thank you, Mr. Chairman.

[The prepared statement of Mr. Lyons follows:]



**Testimony to the Subcommittee on Government  
Management, Information, and Technology  
Committee on Government Reform, June 29, 1999**

**By: Terrence Lyons  
Director of Accounting, Walgreen Company**

Mr. Chairman, thank you for the opportunity to appear before this committee. My name is Terry Lyons and I am the Director of Accounting for Walgreen Company. The Walgreen Company is a leading drug and general merchandise retail operation with fiscal year 1998 sales of \$15.3 billion. My responsibilities include management of our outsourced recovery audit process.

My testimony provides a private sector view of recovery audit benefits, and how the Walgreen Company uses the process.

**Why Use Recovery Auditing:**

Walgreen recognized long ago the benefits of using a professional service provider to identify and recover overpayments. The purchasing and payment systems used by any volume intensive organization like Walgreen are designed to be cost effective and provide for maximum through-put to ensure timely payment of supplier invoices. However, mistakes occur, whether through human error or systemic breakdowns. Our experience has indicated that human error is the most common contributing factor in payment errors. Human error can never be entirely eliminated. Therefore, the need exists for a "safety net" to audit payment transactions for accuracy and validity, recover any overpayments, and identify why overpayments occurred.

The most compelling reason for a recovery auditing service is that there is no risk or investment required. The development of internal controls and/or programs to conduct comprehensive recovery auditing is simply not 100% cost effective. We use the largest service provider, The Profit Recovery Group International, with broad experience in many operating environments. This brings a fresh perspective to bear on our systems and procedures.

**How Recovery Auditing Works At Walgreen:**

The value of recovery auditing to us is apparent in the dollars recovered from the two most recent years. The audit of our 1996 purchases was completed in October of 1998 and recovered \$16.9 million in overpayments on a purchase volume of \$8.5 billion. The audit of our 1997 purchases is just being completed and is expected to recover approximately \$17.5 million in overpayments against



a purchase base of \$9.7 billion. Although these numbers are large, nearly \$35 million over just the past two audit years, they actually indicate an error rate of only about 0.19%, meaning that 99.8% of our payables transactions were processed and paid correctly.

The success of our recovery audit activity is based on a set of mutually identified duties and expectations for both parties.

- **Expectations and Duties of Walgreen's**

We as the client must fully support the process. We provide our service provider with access to all required media, both electronic and paper, needed to research, identify and document any instances of overpayment or under-deduction. Points of contact are established within the purchasing, transportation, accounts payable, accounting and finance areas to liaison with contractor personnel and provide whatever support is required.

We expect our contractor to provide all the necessary support for the audit, including issuing claim letters, handling any vendor correspondence or phone calls, negotiating with vendors where appropriate, and providing a complete audit trail from initial claim identification until final collection.

Claims that have been identified and submitted for processing are, after notification to the vendor, deducted from the next vendor remittance.

- **Expectations and Duties of Recovery Audit Service Provider:**

Our recovery audit firm has responsibilities and duties to ensure the success of the effort. They gain a full understanding of the purchasing and payment systems, for both electronic and paper transactions; meet and develop good working relationships with all the designated points of contact within our organization; understand the inter-relationship between different parts of our organization, and protect our vendor relationships.

We expect our contractor to:

- Employ its methods, expertise and proprietary software to identify, research, document, prepare and finalize all instances of overpayment and/or under-deduction, and
- Provide well trained professional staff and state of the art technology
- Apply the knowledge accumulated in their proprietary databases to maximize the audit results, and
- Propose "best practice" solutions to any identified weaknesses in Walgreen's payment processes.



- Professionally manage the audit process including administration of any and all vendor correspondence related to claims they generate, and negotiate settlements with the vendor where appropriate
- Provide quarterly verbal and written management reports outlining results, findings and recommendations identified, as well as informal updates on a more frequent basis as needed.
- Provide special ad hoc reports or statistical analyses on an "as needed" basis.
- Finally, we expect our contractor to maintain an open line of communication with Walgreen's management, and to protect the confidentiality of all proprietary Walgreen's information.

In short, we expect our contractor to function in a fully out-sourced manner that represents the interests of Walgreen.

The question of "why" Walgreen's would employ an outside firm to do recovery auditing, rather than doing it internally may have occurred to you. The answer is simple; as a company we have chosen to invest our developmental dollars in systems and technology that provides improved productivity within our stores and better customer service. Also, the investment in technology and resources needed to develop this kind of capability and expertise in-house would be cost prohibitive. We find it attractive to outsource this function to a professional recovery audit firm. They have the technology, resources and expertise to perform. It is what they do for a living and what they do best.

### **SUMMARY**

In summary, Mr. Chairman, we have found the use of professional recovery audit services to be invaluable in both recovery of past overpayments, and improving internal controls. Among the major benefits:

- We recovery millions of dollars each year
- We incur no financial burden
- The process is not disruptive to our normal operations
- The nature of the service is ongoing with benefits year after year

As a taxpayer and private sector user of recovery audit services, I believe that recovery auditing services for government is a terrific idea. It will result in the recovery of a great deal of money and further demonstrate how government can benefit from private sector business practices.

I thank the Chair and the committee for the opportunity to appear before you today.

Biography  
For  
Terrence M. Lyons  
Director of Accounting

Walgreen Company  
Danville, IL

Mr. Lyons began his career with Walgreen Company in 1978 in the position of Accounting Manager. Since then he has held the position of General Manager and is currently Director of Accounting. Prior to joining Walgreens, he worked at Commercial Credit Corporation and Super X Drugs, a division of Kroger.

Mr. Lyons is responsible for the implementation of the recovery auditing professional services at Walgreen Company as well as the administration of the program for the past ten years. Under his guidance, recovery auditing has made a significant financial contribution at Walgreens.

He attended Xavier University and is a member of International Accounts Payable Professionals, Association of Records Managers and Administrators and Retail Energy Managers.

Terry resides in Danville, Illinois with his wife and has six children.

Mr. HORN. Well, we thank you for that very thorough statement. Our next witness is Mr. Stephen Booma, health care consultant who has had quite a rich experience with the Travelers Insurance Co. and Mutual of Omaha Insurance Co. We are glad to have you here.

Mr. BOOMA. Thank you, Mr. Chairman. And I would like to thank the subcommittee for allowing me to discuss this with you.

As you said, I do have quite a history with the health insurance industry. I am 27 years in this business. I have 24 years with the Travelers. At the Travelers, I was president of their regional home office in Chicago. I also ran other strategic business units. At Mutual of Omaha most recently, I headed up their managed care area, president of their HMO subsidiary, and I was also responsible for all of their claim payment. So, in short, I was the one who had to make the decision to use an outside vendor or to do it in-house. And I will explain my comments on that. Right now I am operating as an insurance consultant working in mergers and acquisitions, but also working with companies in the managed care arena to improve their performance.

Today, I would really like to address my comments as a private administrator of health plans. And I would say, from the outset, that we chose to go outside and use private recovery firms. I also believe strongly, at the outset, that the Federal Government, as the largest purchaser of health plans, should also use outside recovery firms.

The reasons why. They are really pretty simple and we are at the point today, this afternoon, where I think we have discussed them enough where almost everyone is in agreement. So it is wonderful. But I will just maybe emphasize a couple of points. First, and foremost, recovery firms have the expertise and have the highest level of professionalism in handling this type of work. That is their only business. That is not the core business of anyone other than the recovery firms. So it makes perfect sense to allow the experts to do it.

If you have someone like HCFA start to use outside recovery firms, you will actually see competition within other firms to do that work and the expertise will grow. If that expertise is tried to develop inside, I can almost guarantee you that I wouldn't see that type of growth in this level of business.

The amount of money in overpayments is staggering. And I think we all agree that they can occur simply from human error. To me, it doesn't make any sense to have the folks that are making the human errors try to go get the money they made the errors on. Human nature tells you that if you make an error, there is a strong inclination not to point that out. That would be one of the primary reasons that we chose to go to outside, because we wanted people that were not attached to the process to make those decisions.

In the health care business, doctors, hospitals, and health care providers of all kinds and insurance companies are very familiar with this process. And, in fact, it is not an adversarial process, at least on this particular process. Oftentimes, insurance companies, Managed Care Organizations are at opposite ends with providers, but providers really look for help in solving overpayment situa-

tions. They know, most of the time, that they have made overpayments. It is important to work with them to try to correct those overpayments and they are pleased when they can do that in a logical and orderly manner. And the recovery firms are best positioned to do that.

Our customers understand, especially the larger ones within the private insurance world, that errors occur. And they are most interested in making sure that those errors are corrected and that it is done in an orderly manner. If you don't employ recovery firms, then the process and the length of time is difficult and oftentimes very burdensome. Insurance companies who take on the full risk of contracts for individuals or small groups understand the use of this too and benefit directly from using outside recovery firms. That was another primary reason why we chose to do it.

So I would, in summary, strongly recommend that this bill specifically allow for insurance claims recovery for HCFA as well as other Federal plans. I would also emphasize that I think it should be mandatory. I don't think there should be ways to opt-out. Because if you allow them to opt-out, the people who are running the plans will probably want to continue to try to self-police themselves and that won't work. Thank you.

[The prepared statement of Mr. Booma follows:]

Testimony of Stephen Booma  
Health Care Consultant

Before the Subcommittee on  
Government Management, Information and Technology

Hearing on H.R. 1827,  
"Government Waste Corrections Act"

June 29, 1999



Good afternoon. Mr. Chairman, my name is Steve Booma and I would like to thank you for the opportunity to discuss this important topic with you today.

I have worked in the health insurance industry for the last twenty-seven years. Twenty-four years were spent with The Travelers Insurance Company and four years with Mutual of Omaha Insurance Company. At The Travelers I ran several large strategic business units, including President of the Midwest Home Office. With Mutual of Omaha, I was Executive Vice President of Health Care Management Operations, which encompassed all of their Managed Health Care business. In addition, I was President of the HMO subsidiary, Exclusive Healthcare, Inc.

My responsibilities included claims administration for all health insurance at Mutual and managing the adjudication process for over \$4 billion of health claims covering individuals, small groups and large employers.

Currently, I am a consultant with insurance companies and managed care operations assisting with mergers and acquisitions as well as developing programs to enhance their performance.

I would like to speak with you today from the perspective of an administrator of health insurance plans. As a private administrator of health insurance plans, we elected to use outside recovery firms for claim overpayments. I believe strongly that the largest purchaser of health plans in the nation, our Federal Government, should utilize the same programs as private administrators. Specifically, HR 1827 should require the use of recovery firms for health insurance overpayments of public health care plans.

Testimony of Stephen Booma  
June 29, 1999  
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We elected to use recovery firms for several reasons. First, outside recovery firms have the expertise and highest level of effectiveness for securing overpayments. Some administrators maintain "in-house units" to perform this work, but I have found that outsourcing this work produces the best results.

Secondly, recovering overpayments is not the primary business of health insurance plans, but is the *only* business of recovery firms.

Third, there is a considerable amount of money involved with overpayments. Most claims administrators are accurate in the vast majority of claim payments but a fraction of just one-percent is a great deal of money when handling billions of dollars. Overpayments result from errors with hospital and doctor bills as well as other health care providers. Overpayments also result from clerical errors made by claims payers, and contractual changes that may result in overpayments. Many administrators guarantee work to over 99% financial accuracy, but the complexity and sheer magnitude of millions of claim payments and billions of dollars creates these overpayments.

For those in the health care business—doctors, hospitals, healthcare providers of all kinds, and insurance companies—claim overpayments are just another part of our work that must be dealt with in a professional manner. There is not an adversarial relationship with the claims administrators, recovery firms and providers—at least on this subject. In fact, providers usually know when they have been overpaid and the vast majority of them appreciate help in clearing these overpayments from their books in a professional manner.

Testimony of Stephen Booma  
June 29, 1999  
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Large employers want their claim payments to be as accurate as possible to keep health insurance affordable for themselves and their employees. They understand claim overpayments occur, however, and support the use of recovery firms paid on a contingency basis. Both large insurance companies (which assume all the risk for health plans they sell to individuals) and small employers pay on a contingency basis as it is one of the most cost effective methods to manage overpayments.

I would strongly recommend that this bill specifically allow for insurance claims recovery to provide HCFA and other Federal plans the opportunity to utilize health insurance claim recovery firms. This will result in dramatic claim cost savings for the American public and assure the highest level of accuracy of claims payments for beneficiaries and providers.

Thank you.

Mr. HORN. Thank you. That is very helpful. Mr. Robert Koehler is attorney-at-law, Patton Boggs here in Washington and the American Logistics Association. Have we got a little room for you there at the table, finally? Thank you.

Mr. KOEHLER. I moved from the end of the dug-out to take the clean-up spot. My name is Robert Koehler. I am a senior partner in the Washington, DC, law firm of Patton Boggs. And I have specialized in government contract law for the past 30 years. I am here on behalf of the American Logistics Association, a trade association of some 600 manufacturers, brokers, and distributors who sell brand or trade-name items to the Federal Government. And this involves both the commissary systems, the Defense Supply System, as well as the non-appropriated fund activities such as AAFES and NEXCOM.

Because of the limit of 5 minutes, I will only highlight the more critical issues that we think we should address in this bill. Mr. Chairman, by way of background, I have been involved with the recovery audit associated with DSCP and PRGI for the past 2 years. In this regard, I represent 10 companies: Frito Lay, Fort James, Hunt Wesson, Johnson and Johnson, Kellogg, Mars, Nabisco, Pillsbury, Reckitt and Colman, Tropicana, and General Mills. In my past, I have worked extensively on the issues of price warranty as far as GSA is concerned; as far as this agency, DSCP, is concerned; and with the AAFES.

As we look at this legislation, I think it is fair to make comment on what was learned—at least what we, from our perspective, learned—from the demonstration program. From our perspective, as we look at the demonstration program, it was envisioned to take the basic concepts that are used in the commercial world and apply them at the DOD level. Very simple. Unfortunately, it isn't that simple.

And the difficulty, Mr. Chairman, that occurs is two factors. One, there are affinity contract terms and conditions that must be adhered to by the government in conducting either audits or seeking to recover claims. And, two, and most importantly, there are well-established Federal acquisition regulations that both the government and the contractor must comport with in these audit activities. And from our perspective, when DSCP and PRGI initiated their activities in the demonstration program, this was totally ignored.

For example, the first thing that happened in 1996 was the PRGI and DSCP issuing thousands and thousands of collection letters to companies demanding payment, giving them 30 days to pay and also advising them that if the situation arose, it was going to withhold the funds on any outstanding invoice. And, fortunately, this violated the Federal Acquisition Regulation. We brought this to their attention and everyone of those letters had to be withdrawn. Six months later, new letters were issued. And during this time period, when we began to look at the process that they were going about, it became clear that what they were attempting to do was to develop a system that they relied on in the commercial activity that can't be done in the government sector.

For example, they had two types of claims. What they call a unit price claim, which was a claim that asserted that the companies

were not paying the most favored customer price to the government. The second type of claim was what they called the prompt payment claim. That meant that if the company was providing a commercial entity a prompt payment discount let us say of 2 percent if you pay it in 10 days, not 30 and the government wasn't getting that, they demanded equal treatment.

In the commercial world, that might be appropriate. In government contracts, the essential thing is you have to adhere to the terms of the contract. And, unfortunately for the government and PRGI, the price warranty clause is a very specific document that details what is the basis upon which the contractor warrants his price, the average price, being most favorable to the government. And in our judgment, that was totally ignored. Now we are working now through the process of trying to rectify that.

The second part was the DSCP contracting activity was associated with all the commissaries overseas. DSCP and PRGI issued claim letters and failed to look at their own documentation that existed in the government at the local commissaries levels in Europe. The industry brought this to their attention and, quite frankly, Mr. Chairman, raised hell about it. After a considerable period of time, DSCP finally got the funding to go over to Europe to look at these documents and that was done just January of this year. We are now advised that a significant amount of those claims that they had made against the companies on the unit prices may be withdrawn.

Now the second part relates to the prompt payment discount. Again, we believe that the price warranty clause specifically requires you to consider what is an average price. What DSCP and PRGI have done is extracted this one element called billing advantage, assumed that that was not part of the average price, and that is where a majority of the claims are that have not been recovered. And the reason is because the contractors want the government to adhere to the terms of the contract and these claims, we don't think, represent that term.

Now with this as background, we now have to look at the new bill. And let me say, Mr. Chairman, on behalf of all the companies that ALA represents, we have absolutely no objection to outside audit function. None whatsoever. We recognize that it is done throughout the government.

But I think the key difference of what is being proposed here versus what exists now and what PRGI contract is even right now is what I think is an extremely dangerous move by allowing the agency to delegate extremely core responsibilities from the contracting officer to the audit company. And I think that if you will ask any government contractor, if you ask any government representative who has been a government contractor, this particular provision is of great, great concern to them.

It is very simple, the reason. The bill establishes giving authority to individuals to find the claims, process the claims, pursue the claims, and settle them. And if you looked at PRGI's testimony that they gave back on June 12, that is exactly what they were talking about. You are also giving them 20 percent of what they recover. That is not incentive fee, that is a headhunter's fee. And that, to me, is extremely dangerous.

One of the principles, I think, that is lost in a lot of this is that government contracting under the Federal Acquisition Regulation is extremely different. I might note that Mr. Peterson, who is from AAFES here this afternoon, testified about their great results. Make no mistake about it, AAFES regulations are entirely different than DOD's. AAFES is a non-appropriated fund activity. It is not governed by the Federal Acquisition Regulation. DSCP, the commissaries, all the activities that you are referring to are. And that is a significant difference. So I think we have to analyze the success one might have, based upon the atmosphere that the regulations allow them to exist.

Finally, ALA believes that providing the private contractor auditor with such a broad authority and then to receive 20 percent presents a clear and unmistakable conflict of interest, violating one of the government's bedrock contracting principles. And I read just a portion of the Federal Acquisition Regulation, "Transactions relating to the expenditure of public funds require the highest degree of public trust and impeccable standards of conduct. The general rule is to avoid, strictly, any conflict of interest or even the appearance of a conflict of interest in government contracting relationships."

And, again, the idea of giving the contractor a combination of the authority that the contracting officer has and the percentage presents, I think, a conflict that cannot be overcome. ALA does not have any difficulty with a continuation of the program. Where we have the difficulty is trying to allow the contractor to have that contracting responsibility. And that is where the major conflict arises.

I also think that one of the issues that has arisen in our dealings, in discussions with the contracting officer and other government representatives is we have talked about attempting to resolve some of these issues, settle them. One of the issues that always comes up is, well, I might agree with you, but I have PRGI on the other side of me who has a contract and is entitled to 20 percent recovery. I have a conflict with him because if I settle at one level, he might assert that he is entitled to a higher percentage. I think the bill ought to have a provision that makes it very clear that the government is not liable in any way, shape, or form to the contractor for any type of offset or settlement or decision that the contracting officer makes in reaching that settlement vis-a-vis that 20 percent.

Bottom line, we support the bill only if—only if—you exclude from this bill the contracting officer delegation to the outside auditor. If it is just really a continuation, we have no difficulty with the bill. Thank you, Mr. Chairman.

[The prepared statement of Mr. Koehler follows:]

TESTIMONY  
OF  
ROBERT H. KOEHLER  
ON BEHALF OF THE  
AMERICAN LOGISTICS ASSOCIATION  
BEFORE THE  
SUBCOMMITTEE ON GOVERNMENT MANAGEMENT,  
INFORMATION, AND TECHNOLOGY OF THE  
HOUSE COMMITTEE ON GOVERNMENT REFORM  
ON  
H.R. 1827, THE "GOVERNMENT WASTE CORRECTIONS ACT OF 1999"

Tuesday, June 29, 1999

My name is Robert H. Koehler. I am a senior partner in the Washington, D.C. law firm of Patton Boggs LLP and, for the past thirty years, specializing in Government contract law. I am here on behalf of the American Logistics Association ("ALA"), a trade association of 600 manufacturers, brokers and distributors who sell brand or trade name products to appropriated-fund agencies such as the Defense Commissary Agency ("DeCA") and Defense Supply Center Philadelphia ("DSCP"), and to non-appropriated fund activities such as the Army and Air Force Exchange Service ("AAFES") and the Navy Exchange Service Command ("NEXCOM") for re-sale at commissaries and exchange stores located in the continental U.S. ("CONUS"), overseas, and outside the continental U.S. (i.e., Alaska, Hawaii, Puerto Rico) ("OCONUS").

On behalf of ALA, I would like to thank the Committee for providing ALA the opportunity to present its views concerning H.R. 1827 and how it might be improved. In this regard, our comments will focus on Section 3562, *Recovery audit requirement*.

**I. The Underlying Premise**

The underlying premise of Section 3562, indeed, for the bill itself, is that: (i) the Government annually makes significant overpayments to its contractors; (ii) the reasons for the overpayments are basically ministerial or clerical in nature ("duplicate payments; pricing errors, missed cash discounts, rebates, or other allowances"); (iii) documentation necessary to establish and quantify the overpayments is reasonably available and readily ascertainable from both the Government and its contractors; (iv) an incentive-based, no-cost, "recovery audit" and claim adjudication by a private contractor is the most cost-efficient and efficient manner to recover the amounts; and (v) delegation of the Contracting Officer's contractual authority<sup>1</sup> to pursue and settle

<sup>1</sup> The term "Contracting Officer" includes the Administrative Contracting Officer ("ACO") and the Termination Contracting Officer ("TCO"), which may be the same person and who is a Government employee that is granted the authority to enter into, administer, or terminate contracts and make related determinations and findings. Federal Acquisition Regulation ("FAR") 1.602-1, 1.602-2, 1.603-1, and 1.603-3. The Contracting Officer is the responsible person charged with the duty to collect debts owed by contractors. FAR 32.601 and 32.610.

Government claims to a private contractor is an appropriate, reasonable and legally permissible delegation of such contractual authority.

ALA supports any legislation that will improve the Government acquisition process – selling to the Government is not an easy matter – but the recent experience of ALA’s members with the current DOD Demonstration Program makes us far from encouraged by H.R. 1827.

- **DOD Demonstration Program**

The Defense Authorization Act for Fiscal Year 1996 mandated that the Department of Defense (“DOD”) conduct a demonstration program to evaluate the feasibility of using private contractors to *audit* DOD’s records and procedures to identify overpayments made by the Government to its contractors. Pursuant to this Act, the outside auditor was to look for payment of unallowable costs, missed deductions, duplicate payments, unauthorized charges, and other payment discrepancies; and the audit was to cover fiscal years 1993, 1994 and 1995, using “data processing techniques” generally used in audits in the private-sector. DOD selected DSCP and its *Brand Name Contracts* for the demonstration audit.

- *DSCP’s Brand Name Contracts*

By way of background, DeCA was created in 1991 through the consolidation of commissary systems operated by the military services, and it currently operates 298 commissaries in CONUS and overseas that sell groceries, health and beauty products, and household supplies to military members and their families, retirees, and other authorized personnel. DOD IG Report No. 99-078(PDF), *Outsourcing Of Defense Commissary Agency Operations* (February 5, 1999). For our purposes here, it is important to note that during the Demonstration Audit Period (FY 93, 94 and 95), DSCP had responsibility for overseas commissary sales, while DeCA was responsible for commissary sales in CONUS.

The *Brand Name Contract* is a standing offer between the Government and the manufacturer, producer or distributor (“contractor”) for the provisioning of brand name products for resale in commissaries or other similar facilities.<sup>2</sup> Signed by the contractor and the Contracting Officer, it establishes the terms and conditions for all delivery orders issued by the individual commissaries or other authorized activities. The terms and conditions are referred to as the *Brand Name General Requirements*, and the products the contractor is authorized to sell are listed on the contractor’s *Brand Name Supply Bulletin*.<sup>3</sup> In addition, the *Brand Name Contract* recognizes (and encourages) the practice of contractors providing the Government with voluntary price reductions (“VPRs”), special offers, promotions, coupon programs, and other marketing and merchandising activities that result in reduced prices for the commissaries.

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<sup>2</sup> See FAR 6.302-5(c)(3).

<sup>3</sup> The contractor’s *Brand Name Supply Bulletin* lists all of the items authorized for resale. It describes the product, brand name, Universal Price Code (UPC) number, size and type of container, method of packaging, minimum quantity per order, and price for each geographic area as defined by DeCA.



While these VPRs and special offers may be initiated by the contractor by formal notification to DSCP ("Up-Front VPRs"), the more prevalent method is for the contractor or its authorized representative (i.e., broker) to deal directly with the individual commissaries on separate delivery orders ("Individual Contract Pricing"), or by the issuance of on-site Vendor Credit Memo ("VCMs"),<sup>4</sup> by on-site redemption of in-store coupons, and similar activities. It is important to note here that all of the documentation related to Individual Contract Pricing activity is retained by the individual commissary, not at DSCP Headquarters. Accordingly, a substantial majority of the documentation applicable to the audit of DSCP's contract was held at the individual overseas commissaries or in-country distribution centers.

The identification and recovery of routine billing errors (i.e., duplicate payments, pricing errors, etc.) is ministerial or clerical in nature, and uncomplicated in its process. However, an assertion by the Government that the prices it paid were not as advantageous as a contractor's most favored commercial customer is governed solely by the terms of the contract's "Price Warranty" provision. This distinction is critical because in the latter case, the Government can recover only on the grounds that – in accordance with the terms of the contract – the prices it paid were not as advantageous as a contractor's most favorable customer.

In this regard, Clause 52.216-9P08, *General Conditions (JAN 1992)(Applicable To Supply Bulletin offerors only)*, at pp. 23-25 (Section L) of the *DPSC Brand Name General Requirements*, DPSC Form 3846, dated January 1992 ("the Clause"), provides, in pertinent part:

(f) Prices.

(1) Prices are submitted for "F.O.B. Destination" deliveries to every place within CONUS to include Alaska, Hawaii and Puerto Rico. Prices submitted for overseas delivery points shall be . . . on an "F.O.B. Destination" basis. Prices submitted for delivery to a Defense Depot or port of embarkation for shipment overseas shall be equal to or lower than the CONUS price for the same item in the same geographic area (e.g., prices for delivery to Defense Depot Mechanicsburg shall be the same as or lower than commissary prices in the surrounding northeastern United States).

\* \* \*

(3) Warranty.

(i) The offeror warrants that **all prices offered the Government are as advantageous as the prices offered the most favorable customer. Such warranty includes base price, freight and transportation charges, billing advantage, quantity discounts, allowances, rebates and special promotions** (however,

<sup>4</sup> DSCP's General Instructions for its Supply Bulletin provide that "in the absence of a published change listing "SPECIAL" offers, if such offers are made by a Contractor or his authorized representative, purchasing agencies [i.e., the commissary] are authorized to accept the low offer, prepare the delivery order quoting the lower price and properly annotate the order as to the condition of the offer." Paragraph 8.f, *DSCP General Instructions For Brand Name and Limited Coverage Supply Bulletins*, October 1992.

the warranty excludes reasonable allowances to distributors, wholesalers or jobbers for bona fide services performed by them but not by government customers).

\* \* \*

(iii) To assure compliance with the above warranty, the offeror agrees that the contracting officer shall have the right to examine books, documents, records, and any other evidence necessary to determine the basis for the prices offered. The examination will compare the average price paid by the Government versus commercial customers for the same item during the offeror's latest fiscal year.<sup>5</sup> Should such an examination reveal any instances of overpricing, the offeror further agrees to reimburse the Government for that amount.

(Emphasis added.) Based on the above provision, it is clear that in determining whether a company has complied with its price warranty, it is the DSCP Contracting Officer's obligation – whether by means of an outside audit-contractor such as PRGI or by the Defense Contract Audit Agency (“DCAA”) – to determine the Government's average price and then the commercial customer's average price for the same unit during the contractor's latest fiscal year, before it can assert a warranty claim. As an aside, it should be noted that, although DeCA uses this same “price warranty” provision, agencies such as GSA, AAFES, NEXCOM, etc., each have their own, distinct, price warranty provisions.<sup>6</sup>

- “Recovery Audit” Contractor

Following the September 1995 passage of the FY 1996 Defense Authorization Act, DSCP solicited proposals and finally made an award of the demonstration program contract to Profit Recovery Group International, Inc. (“PRGI”) a year later, on September 30, 1996. Under the terms of the contract, PRGI's only compensation was an “incentive fee” of 20% of amounts recovered by the Government.

However, PRGI clearly had in mind that the claim procedure it devised would promptly generate cash flow because it proposed, and obviously convinced DSCP, that PRGI's commercial *modus operandi* would work with the Government as well: Develop the claim documentation, notify the contractor of the claim, then promptly unilaterally deduct the claimed amount from the contractor's next invoice, thereby holding (and having the benefit of) the amount in dispute while the contractor researches its records to challenge the validity of the withholding.

<sup>5</sup> Although not defined, the term “latest fiscal year” is interpreted here to mean the contractor's fiscal year immediately preceding its current fiscal year.

<sup>6</sup> For example, in AAFES contracts, the *PRICES* Clause provides that the “contractor warrants that during this contract, the net price to AAFES (considering unit price, discounts, allowances, co-op advertising, rebates and other terms and conditions) for each item purchased will be as favorable as, or better than, the price the item is being sold by contractor, to other customers under the same or similar conditions, and in the same general geographical area pursuant to agreements made during the same period . . . . In the event the contractor subsequently extends offers (e.g., VPRs, rebates, coupons) or other special terms to other customers, the contractor is obligated to promptly extend them, under the same condition, in writing, to the contracting officer.”

In this regard, PRGI's contract with DSCP states:

Costs to be paid under this contract will be in the form of a fixed incentive bonus payment on amounts recovered by the Government. In accordance with PRGI's cost proposal, such a fixed incentive bonus payment will be 20% of recovered monies. PRGI's bonus fees will be billed monthly and are to be calculated on claims collected less any applicable paybacks and adjustments.

Paybacks are understood to be recoveries by the Government that are reimbursed in full to the vendor based upon additional information provided by said vendor which prove the applicable claim or deduction to be invalid.

Adjustments are understood to be recoveries by the Government that are reimbursed in part to the vendor based upon additional information provided by said vendor which prove part of the claim or deduction to be invalid.

Paragraph B-2, PRGI-DSCP Contract (emphasis added). Clearly, PRGI and DSCP planned to put the onus on the contractor to disprove the claim while the Government held the contractor's money – and PRGI got paid.

- *PRGI Demand Letters*

In the spring and summer of 1997, PRGI representatives signed "Bill of Collection" letters in the name of the DSCP Contracting Officer's technical representative to contractors, stating that "audit of your account reveals that you are indebted to the United States Government in X amount," citing the reason for the indebtedness, and advising that "if payment is not received within 30 days, interest will be charged on the unpaid portion from the date of this letter . . . currently 6.375%." These letters further stated that "in addition to charging interest, administrative offset action will be initiated against any unpaid invoices sufficient to recover the debt," with the threat that this offset action, "authorized under the provisions of FAR 32-511 may be taken at any time, whether or not 30 days have elapsed since the date of this letter." While this procedure may have been used by PRGI in the commercial setting, unfortunately this demand, and the threat to unilaterally set off the asserted amount, clearly violated FAR Subpart 32.6, *Contract Debt*.

As a matter of fact, since 1989 the FAR has mandated that: (i) for a unilateral debt determination, the Contracting Officer shall issue a final decision, as required by the *Disputes* Clause; (ii) no demand for payment shall be made prior to the issuance of the final decision; and (iii) interest does not begin to accrue on the debt until after the issuance of the final decision and after a demand for payment is made. FAR 32.608 (c).

Moreover, the PRGI-generated claim letters provided no documentation to support the asserted claims. They merely provided a calculation of the amount due without providing a single document to support the basis for the alleged claim. For example, in those letters where the claim was based on the difference in "unit price"<sup>7</sup> between items sold to overseas commissaries and the

<sup>7</sup> For the most part, the PRGI claims are purportedly under the "price warranty" provision, and they fall in two categories: (1) "unit price" claims, where it asserts that the unit price paid by the overseas commissary is not equal to or

contractor's commercial customer, the letters cited to a "Leemis Report," but did not provide the Report, or any other documentation, to substantiate the claim. Again, PRGI's approach was to assert a claim, provide no proof of claim, withhold the money (of course, get its 20%), and force the contractor to prove it did provide "most favored customer" prices.

In September 1997, several companies questioned DSCP concerning these issues, challenged its right to unilaterally withhold funds from companies in the absence of a Contracting Officer's Final Decision, and demanded that the companies be provided the documentation relied upon by PRGI to assert the claims. One month later, on October 8, 1997, the DSCP Contracting Officer rescinded all of the letters that had been issued by PRGI.

Then, beginning approximately in June 1998, DSCP began re-issuing its letters, advising companies that they may be indebted to the Government, and this time provided a limited amount of information to support the alleged indebtedness. Virtually all of the letters were "price warranty" claims, as distinguished from ministerial or clerical errors.

These letters presented new problems. They revealed that, although the "price warranty" provision in the *Brand Name Contract* is the only contractual basis for the Government's claims, PRGI totally ignored the warranty's operative provisions that required the Government to determine the "average price paid by the Government versus commercial customers for the same item during the offeror's latest fiscal year." Second, for the "unit price" claims, it became evident that PRGI totally ignored all of the pricing information the Government had at its overseas commissaries and in-country distribution centers concerning all of the price reductions, discounts, promotions, or rebates the contractors had provided at the commissary level. Finally, for claims seeking to recover the "discounts for prompt payment" given to commercial customers but not the Government, it was clear that PRGI simply ignored the clear and unambiguous language of the warranty provision by singling out one of the elements ("billing advantage") to be considered in determining "average price," and PRGI made it a stand-alone basis for the Government (PRGI) to assert a claim.

- "Unit Price" Claims

After a series of meetings between representatives of DSCP and company members of ALA, it is our understanding that DSCP secured funding that permitted representatives of DSCP and PRGI to travel to the overseas commissaries and in-country central distribution centers in January 1999 to review that contract documentation. At a meeting in February 1999 with company members of ALA, we were advised that all of the DSCP "unit price" claims were being withdrawn pending PRGI's review and analysis of the documentation obtained overseas. At that time, the DSCP Contracting Officer indicated that it now appeared that a substantial number of the "unit price" claims would be eliminated. In March 1999, the Contracting Officer notified the contractors that the "apparent letters of indebtedness to the Government" were being held "in abeyance pending a review based on additional information we recently received."

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better than the company's commercial customer in the U.S., and (2) "discount for prompt payment" claims, where it asserts that the contractor did not provide the Government with discount terms as favorable as that given the commercial customers.

- *“Discount For Prompt Payment” Claims*

In April 1999, the DSCP Contracting Officer renewed the “discount for prompt payment” claims, stating, in part that:

In addition to the base price of an item, paragraph (3) of the contract clause titled General Conditions (52.216-9P08) specifically cites “billing advantage” among the terms the contractor warrants to be as advantageous as those offered to the contractor’s most favored customer. The term billing advantage includes cash discount terms for prompt payment. This clause affords us the right to recover overpayments resulting from the more advantageous discount terms you offered your commercial customers than you offered to DSCP.

Once again, however, we believe DSCP has improperly isolated “billing advantage” as a separate and distinct basis for asserting a claim. The “price warranty” provision, however, requires DSCP to determine an “average price” using all of the factors (e.g., base price, freight and transportation charges, billing advantage, quantity discounts, allowances, rebates and special promotions).

ALA believes there are serious legal impediments to these claims, which include:

- There is disagreement as to whether a “discount for prompt payment” is a “billing advantage” within the meaning of the price warranty provision. In 1992, a DSCP contracting official advised ALA, in writing, that a discount for prompt payment was not a “billing advantage.”
- Even assuming this type of discount is a “billing advantage” under the “price warranty” provision, it is improper for DSCP to consider “billing advantage” as a separate and distinct factor warranted by the contractor, rather than considering it as but one of the factors identified in determining “average price.”
- Since the “price warranty” provision limits DSCP’s examination, and its right of recovery, to the company’s prices for its “latest fiscal year,” it renders the Government’s rights applicable to FY 93, 94 and 95 unenforceable, lapsed, or otherwise beyond the term of the contractor’s warranty.
- DSCP would not be entitled to recover the difference between the discounts offered commercial customers (i.e., 2%-10 days, net 11) and those to DSCP (i.e., net 30) because it was impossible for the Government to earn the commercial discount, even if offered.

Although we are continuing to discuss these issues with the DSCP Contracting Officer<sup>8</sup> in an effort to reach an amicable resolution, it appears that we are at an impasse on these core issues.

- *Conclusions Concerning the DSCP Demonstration Program*

Proponents of the DSCP Demonstration Program continue to advertise a recovery of \$19 million in "overpayments" based upon an August 1998 assessment by PRGI. Of this total, PRGI identified ministerial billing errors (i.e., duplicate payments, unposted credit memorandums, accounting errors, and the like) of approximately \$2.8 million, with a recovery of approximately \$1.8 million. However, under the category of claims under the "price warranty" provision of the *Brand Name Contract*, the "unit price" type claims are approximately \$3.7 million, the "discount" related claims \$12.3 million, with recovery of less than \$100,000. GAO Report No. GAO/NSIAD-99-12, *Recovery Auditing Offers Potential To Identify Overpayments* (December 1998).

These results are not surprising. Ministerial and clerical billing errors are routinely and readily resolved by the contracting parties based on hard facts (i.e., invoices, payment vouchers, credit memo, etc.). However, when PRGI asserts "price warranty" claims, they must be in accordance with the contractual provision upon which the claim is grounded. ALA believes that it is in this latter area that PRGI has forced the pursuit of questionable claims.

From ALA's viewpoint, the DSCP Demonstration Program has produced unacceptable results for these reasons:

- PRGI and DSCP either failed to consider the mandates of FAR Subpart 32.6, *Debt Collection*, in pursuing these types of claims, or simply ignored them in generating claims.
- PRGI proposed, and DSCP accepted, a course of conduct that was intended to withhold the contractor's money while the contractor challenged the claim. While this plan obviously generates cash flow for PRGI on 20% of the withholding, the withholding itself violates FAR Subpart 32.6, *Debt Collection*.
- At the time of contract award, apparently neither PRGI nor DSCP recognized the fact that "unit price" claims under the "warranty price" provision would necessarily turn on Government documentation located at the overseas commissaries and in-country central distribution centers. When industry representatives stressed the importance of this documentation, apparently the overseas commissaries objected to doing PRGI's legwork of searching for, and reviewing, their respective files for the VCM, coupon redemptions, and other data that would identify price adjustments by contractors. Faced with this dilemma, PRGI and DSCP simply elected to proceed with the "unit price" claims without reviewing those Government documents. (As noted earlier, it was not

<sup>8</sup> The current DSCP Contracting Officer, Dennis Polimeni, assumed responsibility for the PRGI claims in February 1999. Since then, he has been very proactive in his handling of these claims, and ALA wishes to commend him for his efforts and prompt responses to individual contractor questions.

until January 1999, some 27 months after DSCP's award to PRGI, that PRGI and DSCP personnel reviewed those documents.)

- It is ALA's understanding that DSCP was unable to find its own documentation for at least one of the years in question (FY 93). So PRGI simply assumed nothing had changed from year to year and sought recovery for FY 93, even though it had no documentation to support the claims. This fact alone points out the extreme difficulty, if not practicable impossibility, in finding documentation to refute claims that are based on transactions, among hundreds of thousands of transactions, that occurred four, five and six years ago. This, ALA believes, is why the "warranty provision" extends only to the contractor's "latest fiscal year."
- While the Fiscal Year 1996 legislation required the private contractor (PRGI) to audit DOD's records for FY 93, 94 and 95, that requirement did not, and could not, change or modify existing *Brand Name Contracts* and its "price warranty" provision which, in turn, is limited to the contractor's "latest fiscal year." Accordingly, the Government has the right to pursue ministerial clerical payment errors at any time prior to the close of the contract. Claims based on a warranty, however, are governed by the terms of the warranty. PRGI and DSCP continue to ignore this basic distinction.
- It was in the financial interest of both PRGI and DSCP to present the "discount for prompt payment" claims as if "billing advantage" was an independent warranty item, totally independent of the "average price" determination, because the documentation identifying that factor can be generated with little effort. ALA believes this is one example of the problems caused by incentive-based audit contracts.

ALA does not oppose the Government's use of private contractors to audit DOD records or, for that matter, contractor records. In fact, other agencies have adopted the outside audit approach with apparent success. The difference is that, with regard to the other agencies, the auditor-contractor mission is to conduct compliance audits and determine allocability and allowability of costs, not generate claims – and then receive a "piece of the action."

## II. The Proposed Legislation

As noted at the outset, our comments on H.R. 1827 will focus on Section 3562, *Recovery audit requirements*, and how it might be improved.

To the extent this legislation is intended to impose an obligation on Government agencies to conduct audits of its own records – either by Government auditing teams or by private contractors – to identify and recover contract overpayments resulting from ministerial or clerical errors (i.e., duplicate payments, overpayments, accounting errors, unapplied payments, unapplied credits, erroneous price entries, etc.), ALA fully endorses this effort. However, at least based upon the

statistics provided in the December 1998 GAO Report, the recovery associated with ministerial or clerical errors will be modest, at best. See, GAO Report, *Recovery Auditing Offers Potential To Identify Overpayments*, Table 1 at page 4.

ALA believes that the real intent of the legislation is to pursue claims<sup>9</sup> arising under “price warranty” clauses.<sup>10</sup> While ALA also endorses an effort by the Government to enforce its contractual rights under such a clause, we believe there are significant administrative, contractual and legal differences between pursuing ministerial errors and contract claims – and the current legislation fails to make this critical distinction.

- “Recovery Audit”

The bill defines “recovery audit” as:

[A]n auditing process to identify overpayments made by executive agencies to vendors and other commercial entities in connection with a payment activity, including overpayments that result from duplicate payments, pricing errors, failure to provide applicable discounts, rebates or other applicable allowances, or changes[,] or payments that are not authorized by law, regulation, or other applicable requirements.

Subparagraph (3), Section 3561, H.R. 1827 (emphasis added). This definition, ALA believes, properly frames an audit function – with the operative words being “to identify” – because it places the auditor only in the role of a “fact finder,” not negotiator, arbitrator, or decision-maker. In this regard, it is consistent with current acquisition regulations concerning contract administration and audit services.

For example, FAR Part 42, *Contract Administration and Audit Services*, makes clear that the auditors’ responsibility is to analyze the contractor’s financial and accounting information, then provide information and advice to the Contracting Officer. The auditor is **not**, however, the authorized representative of the Contracting Officer, and has no authority to administer any aspect of a Government contract, or to negotiate and/or settle matters with a contractor, or to otherwise make binding contractual decisions. It is the Contracting Officer who, by statute and regulation, has the exclusive right to administer, and make binding decisions concerning a Government contract. And it is the Contracting Officer who has the responsibility to “request and consider the advice of

<sup>9</sup> Well over 90% of the alleged overpayments identified in the December 1998 GAO Report fall into a claims category; that is, where PRGI and DSCP are seeking recovery for contractor’s alleged failure to comply with the requirements under the “price warranty” provision of the DSCP *Brand Name Contract*. See, for example, the following categories: “discounts not offered,” “discounts earned but not taken,” and “overcharge by comparison.” These types of alleged claims are being vigorously contested by the contractors, and the Government’s recovery to date is negligible.

<sup>10</sup> The vast majority of Government contracts do not have “price warranty” clauses. Typically, the contracting agency will insert such a clause only where commercial items are being purchased under a basic agreement (“BA”), basic ordering agreement (“BOA”), or blanket purchase agreement (“BPA”). These are written instruments of understanding where the parties agree to the terms (items, price, delivery requirements, etc.) and clauses that will apply to future orders by the Government during the term of the agreement, and contemplates the future orders will incorporate, by reference, the applicable terms and conditions. See, for example, FAR Subpart 16.7, *Agreements*.



specialists in audit, law, engineering, transportation, and other fields, as appropriate.” FAR 1-602-2 (emphasis added). See, also, FAR 42.302, *Contract administration function*.

The operative provisions of H.R. 1827, however, go far beyond providing audit advice.

- **Delegation Of “Executive Agency Authority” To Private Contractors**

The bill would permit the private contractor-auditor to take the following actions, without the review or approval of the Contracting Officer: (i) determine whether the contractor has fulfilled its contractual obligations under the “price warranty” clause of the contract; (ii) prepare and issue letters to contractors asserting indebtedness to the United States and demand payment; (iii) determine the contractual and legal adequacy of the contractor’s response; and (iv) negotiate and settle overpayment claims with the contractor on behalf of the Government. These are the realities of the following provision:

(B) the executive agency may authorize the contractor (subject to subparagraph (C)) to notify entities [i.e., contractors] of potential overpayments, to respond to questions [i.e., from contractors] concerning potential overpayments, and to take other administrative actions [i.e., assert, negotiate and settle claims] with respect to overpayment claims; and

(C) subject to section 3711 of this title, the executive head [i.e., delegated to the contracting officer] shall have final authority to resolve disputes, to compromise or terminate overpayment claims, to collect by setoff, and to initiate litigation or referrals for litigation.

Paragraph (c)(1), Section 3562, H.R. 1827 (emphasis added). There should be no mistake about this: this is an **unprecedented** grant of contractual authority to a private contractor!

It is well established that for Government acquisitions, the Contracting Officer has the sole responsibility for entering into, administering, and/or terminating contracts, and making related findings and decisions. FAR 2.101. It also is well recognized that the Contracting Officer may delegate responsibilities and duties to an ACO, a TCO, Contracting Officer Representatives (C.O.R.), Contracting Officer Technical Representatives (C.O.T.R.), and rely upon other authorized agents (i.e., inspectors, engineers, project officers, contract specialists, etc.). We are unaware, however, of any instance when these **core responsibilities** of a Contracting Officer have been delegated to any person outside the Government, much less a private contractor.

Moreover, providing the private contractor-auditor with such broad authority to pursue claims – for which it receives 20% – presents a clear and unmistakable conflict of interest. In this regard, the FAR admonishes that:

Government business shall be conducted in a manner above reproach and, except as authorized by statute or regulation, with complete impartiality and with preferential treatment for none. Transactions relating to the expenditure of public funds require the highest degree of public trust and an impeccable standard of conduct.

**The general rule is to avoid strictly any conflict of interest or even the appearance of a conflict of interest in Government-contractor relationships.**

FAR 3.101-1 (emphasis added). ALA has no quarrel with the concept of compensating an outside auditor on an "incentive fee" basis, so long as the auditor is acting solely as an advisor to the Contracting Officer and has no role in determining whether to pursue the matter. But that is not what is being proposed in H.R. 1827.

ALA believes such a delegation of responsibilities is an extremely dangerous precedent – and it is being proposed, not because Contracting Officers and their authorized representatives cannot do their jobs, but because it facilitates private contractors such as PRGI to generate and control the cash flow from the "claims" they initiate and process! In this regard, the private contractor's 20% fee is a bounty, not an incentive.

- *Contracting Officer's Authority Is Compromised*

Under the current Demonstration Program, ALA believes that the authority of the Contracting Officer to resolve disputes concerning the applicability of the "price warranty" clause to the claims generated by the private contractor-auditor, PRGI, has been severely compromised. For example, DSCP views its contract with PRGI as requiring the Government to vigorously pursue all of the claims generated by PRGI because, absent such pursuit, PRGI might itself file a claim against DSCP for the 20% fee. When dealing with the supplier, ALA believes that DSCP's first consideration is: Will this resolution be acceptable to PRGI.

Whether DSCP is correct in its assessment of potential liability to PRGI for not pursuing claims is not the issue here. It is the perception that adversely impacts and undermines the Contracting Officer's responsibilities to ensure that each supplier "receives impartial, fair, and equitable treatment," as required by FAR 1.602-2(b). Moreover, ALA believes that it unduly restricts the Contracting Officer's ability to settle or compromise other unrelated issues or claims when the overpayment claims drive a "bottom line" settlement. In affect, the private contractor-auditor is moved from the role of advisor to a partnership with the decision-maker.

ALA suggests that this legislation make clear that the private contractor-auditor is acting only as an advisor to the Contracting Officer, that the Contracting Officer has sole discretion concerning the pursuit, negotiation and settlement of alleged overpayment claims, and that the Government has no responsibility for, or liability to, the private contractor-auditor for the loss of fees or incurred costs associated with any matter negotiated, settled, compromised or abandoned, for whatever reason.

### **III. Conclusion**

ALA believes that H.R. 1827 provides an unprecedented, and extremely dangerous, delegation of the core responsibilities of the Government's Contracting Officer to a private contractor. This, standing alone, is sufficient for ALA to oppose the bill. But when this delegation of core responsibilities is then coupled with giving an incentive fee or bounty for amounts

recovered, we believe the bill fundamentally alters the relationship between the Government and its contractors.

While the lure for the Government to imitate the claimed successes of “overpayment” recoveries in the private sector is, at first blush, appealing, those tactics cannot be used by the Government. In the private sector, the tactic is simple: identify a potential overpayment, notify the manufacturer, deduct the alleged overpayment from the manufacturer’s next invoice, and force the manufacturer to prove there was no overpayment while, of course, the purchaser has the beneficial use of the manufacturer’s money.

If Congress adopts this approach, it also will have to rewrite a fundamental federal acquisition principle: Government contractors are to “receive impartial, fair, and equitable treatment” from the Contracting Officer. FAR 1.602-2(b).

In the final analysis, H.R. 1827 benefits only the private contractor-auditor – it is the mechanism by which the outside auditor virtually controls its own financial success, with little or no risk. If the supplier disputes the contractor-auditor’s asserted claim, the contractor-auditor walks away from the matter, and leaves to the Government the cost and expense of resolving the dispute (i.e., litigation). This bill does not correct Government waste; it only establishes a new money pipeline for the “recovery” auditors. But at a very great price to the integrity of the federal acquisition system. For these reasons, ALA on behalf of its 600 member companies opposed the enactment of H.R. 1827.

Thank you for providing ALA the opportunity to present its views to the Committee on H.R. 1827.



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## Robert H. Koehler

Mr. Koehler is a former member of the firm's Executive Committee and the senior member of the firm's Government Contracts practice group where he concentrates his practice in Government contract litigation and counseling. Mr. Koehler will be the Managing Partner of the Patton Boggs Emerging Information Technologies Office opening in September 1999. Mr. Koehler has been lead trial counsel in over sixty Government contract cases throughout his career and has lectured on Government/ commercial procurement practices. He also has extensive appellate experience in appeals in the United States Courts of Appeals, especially in the Court of Appeals for the Federal Circuit on Government contract and intellectual property issues.

Mr. Koehler was the primary author of a three-volume acquisition procedures manual for one of the firm's major Defense contractor clients, and he authored "Certifying Claims Under The Contracts Disputes Act of 1978- The Ghost of Rickover Past" which appeared in the American Bar Association's Public Contract Law Journal. Mr. Koehler represents clients on a wide range of Government contract matters, including "price warranty" issues under contracts with agencies such as the Defense Commissary Agency, Defense Supply Center Philadelphia, General Services Administration, Department of Veterans Affairs, the Army and Air Force Exchange Service, and Navy Exchange Service Command.

Mr. Koehler was on active military duty from May 1968 to May 1973, serving as an officer in the Army Judge Advocate General Corps, concentrating in Government contract law. He received various decorations and commendations, including the Bronze Star, the Meritorious Service Medal, the Army Commendation Medal with Oak Leaf Cluster, and the Vietnam Service and Campaign Medals.

Mr. Koehler joined Patton Boggs as an associate in May 1973, becoming a partner in January 1976. Between 1981 and 1983 he was a member of the firm's Management Committee and was the Leader of the Government Contracts practice group between 1983 and 1996. Mr. Koehler also served as Chairman of the firm's Technology Committee for five years.



## **Robert H. Koehler**

Mr. Koehler currently serves on the Board of Directors of the USO of Metropolitan Washington, and was Chairman of the Board for two years. He also served for six years on the Board of Trustees of the McLean School of Maryland, a school for children with moderate learning disabilities and was Board Chairman for four years.

Mr. HORN. Thank you very much. We appreciate that comprehensive testimony.

Mr. Dinkins, in your testimony, you say that the government will benefit from recovery auditing even more than the private sector. However, you also state that you do not have a broad enough sampling of results within the government to accurately project the benefit of the program. What factors support your conclusion that the government would realize a greater benefit from recovery auditing than the private sector?

Mr. DINKINS. Well, I would say to begin with, the long experience that we have with AAFES at just under one-half of one-tenth of 1 percent and the current experience in the demonstration program, those numbers are roughly synonymous. So I wouldn't venture to state at this point—and I would say that the opportunity within HCFA is significantly higher than that. It would be billions of dollars a year and also a higher recovery percent. But somewhere between the private sector average rate of one-tenth of a percent and one-half of one-tenth of 1 percent and probably closer to that one-half of one-tenth of 1 percent number is the real opportunity within government.

Mr. HORN. In your testimony, you recommend raising the threshold for payment activity, subject to recovery audits, from \$10 million to \$500 million. You stated that the amounts recovered from an audit of the \$10 million payment program would not justify the costs and administrative burdens. What are the costs associated with performing recovery audits?

Mr. DINKINS. That statement is probably more self-serving for us the contractor in the sense that we have a huge investment at the beginning of any effort to access all of the relevant media, process it through a data center, prepare and deploy staff, technology, hardware, et cetera. And in a smaller environment, those investments would not bear fruit. And I would point you to a corollary in the private sector. Typically, we looked at environments that are in excess of \$500 million. That is not to say that there wouldn't be multiple segments within any particular agency that would add up to \$500 million. That would obviously be well worthwhile looking at, in terms of the benefits to both parties.

Mr. HORN. Well, you noted that since September 1996, when the Defense Supply Center of Philadelphia contracted with the Profit Recovery Group to perform these recovery audits, more than \$20 million in overpayments had been identified. Only \$2 million has been recovered. Now, according to Mr. Dinkins statement, I guess the balance is in various stages of recovery and I would be curious—and Mr. Wilwerding might want to get in on this—what is the status of recovery of the identified by uncollected overpayments?

Mr. DINKINS. Our experience in the private sector ranges in the high 80 percent range in terms of what is collected, as compared with what is identified. And, typically, the difference is that there is some piece of information that was not resident within the client's files that the supplier may have access to that helps to create a better understanding of the situation. I think that the reason for—first of all, let me correct a couple of figures. Where we are today is about \$4 million: \$2.5 million of which is identified, an-

other \$1.5 million which has been approved by the contracting officer and ready for deduction through DFAS's systems.

I think you heard prior testimony from Mr. Allen at DSCP saying that there was another \$10 million that was ready to go on top of that. I don't recall the exact numbers. There is about \$12 million today that is identified and writing final determination from the contracting officer.

Now, obviously, we don't affect collections with the suppliers. That is the Department of Defense's role and responsibility as part of the program. We identify the overpayments and then they pursue their normal course of action in terms of how to first notify the supplier that there is a potential overpayment, ask for their comment before anything further happens, and then, at an appropriate time, make an offset on a future payment.

Mr. HORN. Mr. Wilwerding, do you have anything to add to that?

Mr. WILWERDING. Yes, Mr. Chairman. I believe also an important part of that recovery percentage—and I agree with Mr. Dinkins that the private sector recovery percentages do range up toward 80 percent in some cases. A great deal of that is a result of the working relationship between the recovery vendor and the payees in these points and, on the health care, being the providers. In that there is a system in place to forward information, substantiate claims, and facilitate payment back and forth. That would take some time to develop on behalf of the government agencies, but it is very realistic to believe that that would be in place and would create a very synergistic environment to work together in that recovery effort.

Mr. HORN. Well, we asked the last panel about the following and how are disputed over payments handled by your companies, when that is a dispute? Is there an organized process or an appeals group? Or how does it work? Is it the contract officer? Yes, Mr. Dinkins.

Mr. DINKINS. That is actually not our role. That is handled through normal scenarios within the government and it is primarily a contracting officer makes the final disposition of any claim.

Mr. HORN. So it works very much like in our debt collection legislation. If it is turned over to a private collector, why they simply go get the amount and if there is a problem with the IRS, fine, talk to the people at IRS. OK, I understand that. Does anybody have any other thoughts on the appeal process in any way? Yes, Mr. Koehler.

Mr. KOEHLER. Mr. Chairman, under the Federal Acquisition Regulation that governs all contracts, there is no debt under the regulation until the contracting officer issues a contracting officer's final decision. At that point, when the contracting officer issues a decision, that then constitutes a debt and the government then has the option to withhold payment or offset, but not until that point in time. It is also the point in time when interest begins to run.

I think earlier one of the panelists was talking about that months and months would go by with interest or years would go by with interest. Well, that is not true. If the government identifies a claim and the contracting officer issues that decision, that interest begins to run on those amounts at the Treasury rate. So I think

that we have to keep that in mind as we move forward on this project.

Mr. HORN. Mr. Dinkins, the Government Waste Corrections Act of 1999 recognizes that the identification of overpayments to providers of goods and services through recovery auditing has been used successfully in the private sector. Accordingly, the proposed legislation generally requires each executive branch agency to conduct recovery audits for its payment activities that expend at least \$10 million annually. Although the Federal Government buys many of the same items as does the private sector, the Federal Government is also the sole buyer of other items, such as major weapons systems.

With that as a preface, does the—you pronounce the initials here PRGI—does that Profit Recovery Group perform or have the capability to perform recovery audits for private sector companies such as United Airlines that buy from the aerospace industry?

Mr. DINKINS. Yes. As a matter of fact, we do provide services to major airlines today.

Mr. HORN. Major weapons systems manufacturers such as Boeing or Lockheed-Martin do not offer cash discounts and other overpayment type claims typically found in retail businesses. What are some of the examples of the type of overpayment claims you anticipate finding in major weapons systems acquisitions?

Mr. DINKINS. Most of the identified overpayments in that arena would be contract compliance related issues. You still have incidences of duplicate payments and other types of errors. Contract compliance will be the key area of that investigation.

Mr. HORN. We have heard from the chief financial officer of Medicare. I am just curious, how applicable is recovery auditing to health care, be it Federal level or the State level, or just plain old hospital level?

Mr. WILWERDING. Mr. Chairman, we would feel that it is extremely applicable. Going back to my testimony, Medicare program is utilizing the private sector carriers to administer these health benefits. Those carriers are currently using private sector recovery firms to audit, identify, validate, and recover overpaid claims. They are using very similar, if not the same, claim systems, the same training techniques on their claim analysts, and the same internal audit techniques they use on their private sector insurance claims.

Therefore, it would be apparent that the ability to audit and identify these claims and recover those claims on behalf of Medicare would be similar to that of the private sector.

Mr. LYONS. I think I can speak on that issue also, Mr. Horn.

Mr. HORN. Sure.

Mr. LYONS. I was the chief operations administrator for our company's health insurance programs in the late 1980's and early 1990's. Walgreen's is self-insured and self-administered. And, we employed outside audit recovery firms to review health insurance claim payments with about a 4 percent recovery rate, if I recall.

Mr. DINKINS. I would add to that, Mr. Horn, that that represents about 10 times the level of recovery demonstrated in government and other programs today. So health care typically offers a larger area of opportunity.



Mr. HORN. I don't doubt that. There are big dollars at stake there. Mr. Wilwerding, the majority of claims deemed erroneous stemmed from issues of lack of medical necessity, incorrectly coded claims, and services paid for that were actually uncovered or unallowable. Given that you do not get involved in making medical judgments, could you describe the methodology you use and the type of errors you identify?

Mr. WILWERDING. Certainly, Mr. Chairman. Our process is to identify errors that are primarily based on a set of data facts that determine the eligibility and the appropriateness of the claim. That may be associated with the beneficiary's eligibility for the program, the contract allowances, what the insurance policy or benefit policy covers and what it does not cover. They could identify things such as duplicate payments or payments that are not customarily made or over a certain program maximum amount. The validity of those claims tends to run very high. Of the claims we identify as potential overpayments, we acknowledge that some 80 percent of those claims will be accurately overpaid.

We will only pursue—and I think it is an important issue to bring out here under contingency fees and I would assume Mr. Dinkins would support this—those of us that are operating on getting paid on successful recoveries will only pursue those claims that are valid overpayments. We have no incentive to pursue claims that we know are not valid and will not likely be reimbursed by the payee. It is, in the health claim area especially, since we deal with fairly low-balance claims and a high volume of those claims, extra effort is given to make sure that the claims we are pursuing are accepted by the provider and we have the data in-house to present to the provider the valid request for the reimbursement.

Mr. HORN. Mr. Wilwerding, in your testimony, you state that it would not be efficient for the Federal departments and agencies to collect overpayments by offsetting future payments. Why would this process not be efficient?

Mr. WILWERDING. Perhaps that testimony needs to be revised. It is not necessarily inefficient, but I do believe that it is burdensome upon the provider community and we could, at some point, and I could submit a statement into the testimony that would give an example of why this would be burdensome if you would prefer that.

Mr. HORN. Mr. Lyons, does the Walgreen Co. do any of its recovery auditing internally?

Mr. LYONS. We do have a small initiative, Mr. Horn. Frankly, we are trying to put our dollars into developing systems that will eliminate the post-audit recovery issues. So we are looking at new billing systems and new accounts payable systems that will tend to probably not eliminate completely, but at least minimize post-audit recovery activities.

Mr. HORN. H.R. 1827, which is before us, would require a recovery audit contractor to provide departments and agencies with periodic reports on conditions giving rise to overpayments and recommendations on how to mitigate such conditions. What recommendations has the Profit Recovery Group International provided to the Walgreen Co. on ways to improve its payment processes and reduce the incidences of overpayments?

Mr. LYONS. Well, I am not sure that I can be very specific in that area, although various audit recovery firms in the past have made specific recommendations. Typically, these are recommendations having to do with system changes and/or manual procedure changes. Some of which we have made. It is easy to make a manual procedure change. It is very difficult to make a systems change when it is tied into a fully integrated process.

Mr. HORN. We noted earlier that the Defense Department contracting officer in most Federal departments deal with the vendor-supplier disputes over the validity of an overpayment identified by a recovery auditor. How does Walgreen handle this?

Mr. LYONS. Well, I think the first point that I want to make is that the Walgreen Co. controls the audit activities. So, when a dispute arises, the facts typically speak for themselves. Is there a purchase contract? And is there the supporting documentation to validate the claim? Usually, if there is, we proceed. If there is not, we don't. And I should say in that respect, that I see very few post-audit recovery claims that do not have a tremendous amount of documentation, supporting documentation.

Mr. HORN. Mr. Koehler, as I understand it, the Profit Recovery Group International identified overpayments, sent letter of indebtedness to vendors, and many vendors protested through their trade association, the American Logistics Association, for which you are counsel. Have vendors complained to the American Logistics Association about recovery auditing performed for private sector companies? And, if so, what are we talking about in terms of complaints?

Mr. KOEHLER. Well, Mr. Chairman, the answer is no, because the American Logistics Association is associated just for sales to the Federal Government so that the association itself would not have access to that. I know on a personal level the companies that we do represent that there are two different types of, if you will, issues that arise on the commercial side. One is the ministerial or billing errors. And Mr. Lyons is correct. That type of documentation is relatively easy to see and there is very little difficulty with getting those resolved.

The other area, though, is in relation to the government contracting, is in the application, not of those type of ministerial or billing errors, but rather in the interpretation of the price warranty clause and the attempt to enforce it. I think George Allen, for DECA, stated that with regard to the price warranty issue, that those were breach issues. Well, if that is the case, then that clearly is an area that should never be delegated to an outside contractor for resolution. Because only that area is the responsibility of the contracting officer.

Mr. HORN. Now I gave the last panel the chance to have anything to say that they haven't said in the dialog either between the Chair and the panel or within the panel. So anybody want to get something off their chest now into the record? Any takers on that?

Well, we thank you very much for coming. We appreciate the knowledge you bring to this and the experience. And that will be very helpful in marking up the bill.

I would now like to thank the following people for setting up this particular hearing: The Government Management, Information, and Technology Subcommittee staff is headed by its staff director,

Russell George, and chief counsel—I don't see him right now. The person to my left, to your right, who has put most of the effort into this particular hearing, is Randy Kaplan; who is also counsel to the subcommittee and a professional staff member. Matthew Ebert, policy advisor, is back here on the bench. Jane Cobb of the full committee, is liaison on this bill, with Mr. Burton's interest. And we have Bonnie Heald, director of communications, probably with somebody in the media here. And Grant Newman, our clerk, against the wall over there. We have John Phillips, intern. And then Paul Wicker, intern; Justin Schlueter, intern; Lauren Lefton, intern.

And, for the Democratic side, Faith Weiss, the minority counsel; Earley Green, minority staff assistant. And Yon Lupu, the court reporter.

So thank you all. And, with that, this hearing is adjourned.

[Whereupon, at 5:01 p.m., the subcommittee was adjourned.]

[Additional information submitted for the hearing record follows:]



DEPARTMENT OF HEALTH &amp; HUMAN SERVICES

Health Care Financing Administration

The Administrator  
Washington, D.C. 20201

DEC 15 1998

The Honorable Edward M. Kennedy  
United States Senate  
Washington, D.C. 20510-6300

Dear Senator Kennedy:

Thank you for your letter suggesting the use of private insurance recovery specialists to recover Medicare overpayments. I regret the delay in this response.

The Health Care Financing Administration continues to seek new ways to reduce fraud, waste, and abuse and to recover overpayments whenever possible. We are aware that the private sector has benefited from using recovery specialists, and we have had numerous inquiries about adopting this business concept for the Medicare program. It is our understanding however, that this type of service is generally provided on a contingency fee basis. Since we do not have the statutory authority to pay contractors in that manner, we are unable to consider using private recovery specialists at this time.

As you know, we are working in a range of areas to reduce instances of overpayment, enabled in part by the invaluable anti-fraud provisions of the Health Insurance Portability and Accountability Act of 1996. We greatly appreciate your continued interest in Medicare and in our fight against fraud, waste, and abuse. I look forward to working with you in the future on these critical issues.

Sincerely,

Nancy-Ann Min Deparle  
Administrator



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Sincerely,

A handwritten signature in cursive script that reads "Nancy-Ann Min Deparle".

Nancy-Ann Min Deparle  
Administrator



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Nancy-Ann Min Deparle  
Administrator

TOTAL P.03

OCT. 6. 1998 12:48PM COMMITTEE ON LABOR

NO. 235 P. 2/2

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**United States Senate**  
 COMMITTEE ON LABOR AND  
 HUMAN RESOURCES  
 WASHINGTON, DC 20510-6300

October 5, 1998

Nancy Ann Min DeParle  
 Administrator  
 Health Care Financing Administration  
 Department of Health and Human Services  
 Attention: HCFA-7020-P  
 Post Office Box 26676  
 Baltimore, MD 21207-0519

Dear Nancy Ann:

With the enactment of the Health Insurance Portability and Accountability Act of 1996, Congress provided important additional resources to fight health care fraud and recover inappropriate payments. The intent of Congress with this legislation was to improve the integrity of the Medicare program and to encourage HCFA to act expeditiously to contract for innovative solutions to fight fraud and to expand programs to recover overpayments due to billing errors.

I am writing to encourage you to consider the use of one possible tool to recover a significant portion of Medicare overpayments: private insurance recovery specialists. It is my understanding that many of the private insurance companies which act as Medicare administrators use additional private sector expertise to recover overpayments they encounter in their private insurance business. Other federal programs such as health plans participating in the Office of Personnel Management's employee health benefit plans also use this source of expertise.

I recognize that HCFA has worked hard in recent months to deal with the complex issues associated with Medicare fraud and abuse. The private sector model for recovery of overpayments is an option that should be considered. Please do not hesitate to contact David Nexon or Sheera Rosenfeld in my Health office if you have any questions.

Sincerely,

Edward M. Kennedy

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NO. 235 P. 2/2

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United States Senate

COMMITTEE ON LABOR AND HUMAN RESOURCES  
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 WASHINGTON, DC 20510-6300

*Account*

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**RESPONSES TO KEY PORTIONS OF THE TESTIMONY OF  
ROBERT KOEHLER ON H.R. 1827 - JUNE 29, 1999**

Following are excerpted from pages 8 and 9 of the written testimony:

Point 1: "PRGI and DSCP either failed to consider the mandates of FAR Subpart 32.6, Debt Collection, in pursuing these types of claims, or simply ignored them in generating claims."

**Response:**

*During the very early phases of the demonstration project, the interpretation of the language in Section 354 of the 1996 Defense Authorizations Act was that PRGI, operating under the outsourcing initiatives, was empowered to act as the Contracting Officer's authorized representative. As a result of complaints by the ALA on behalf of some of its constituents and in an effort to be as fair as possible, all correspondence was subsequently issued over the Contracting Officer's signature, in full compliance with FAR 32.6.*

Point 2: "PRGI proposed, and DSCP accepted, a course of conduct that was intended to withhold the contractors money while the contractor challenged the claim. While this plan obviously generates cash flow for PRGI on 20% of the withholding, the withholding itself violates FAR Subpart 32.6, Debt Collection.

**Response:**

*At no time since the inception of this program have involuntary offsets been taken against any vendor. Further, every vendor received at least two notification letters, each allowing 30 days for response and dialogue; a total of sixty days, even under the original interpretation where the letters were issued over the contractor's signature. Vendors were given every opportunity to refute, in whole or part, any claims issued.*

**According to the provisions of the FAR at Subpart 32.606:**

(d) Except in cases in which an agreement has been entered into for deferment of collections (32.613) or bankruptcy proceedings against the contractor have been initiated, the contractor shall be required to liquidate the debt by--

- (1) Cash payment in a lump sum, on demand; or
- (2) Credit against existing unpaid bills due the contractor.

(e) The responsible officials shall use all proper means available to them for collecting debts as rapidly as possible. Practices for ascertaining and collecting debts shall be comprehensive, dynamic, and as uniform as practicable. Full consideration shall be given to personal contact and follow-up.

**Further, FAR Subpart 32.608 reads as follows:**

32.608 Negotiation of contract debts.

(a) The responsible official shall ensure that any negotiations concerning debt determinations are completed expeditiously. If consistent with the contract, the official shall make a unilateral determination promptly if the contractor is delinquent in any of the following actions:

- (1) Furnishing pertinent information.
- (2) Negotiating expeditiously.

- (3) Entering into an agreement on a fair and reasonable price revision.
- (4) Signing an interim memorandum evidencing a negotiated pricing agreement involving refund.
- (5) Executing an appropriate contract modification reflecting the result of negotiations.
- (b) The amount of indebtedness determined unilaterally shall be an amount that--
  - (1) Is proper based on the merits of the case;
  - (2) Does not exceed an amount that would have been considered acceptable in a negotiated agreement; and
  - (3) Is consistent with the contract terms.
- (c) For unilateral debt determinations, the contracting officer shall issue a decision as required by the clause at 52.233-1, Disputes. Such decision shall include a demand for payment (see 33.211(a)(4)(vi)). No demand for payment under 32.610 shall be issued prior to a contracting officer's final decision. A copy of the final decision shall be sent to the appropriate finance office.

***In every case, even though the identified debts met the criteria referenced above, involuntary offset/collection was NOT instituted, in an effort to give the vendor community every opportunity to present facts or documentation mitigating in their favor. This action was taken despite the requirements of the FAR to expeditiously collect any valid identified debt owing the Government.***

Point 3: "At the time of contract award, apparently neither PRGI nor DSCP recognized the fact that 'unit price' claims under the 'warranty price' provision would necessarily turn on Government documentation located at the overseas commissaries and in-country central distribution centers. When industry representatives stressed the importance of this documentation, apparently the overseas commissaries objected to doing PRGI's legwork of searching for, and reviewing, their respective files for the VCM, coupon redemptions, and other data that would identify price adjustments by contractors. Faced with this dilemma, PRGI and DSCP simply elected to proceed with the 'unit price' claims without reviewing those government documents. (As noted earlier, it was not until January 1999, some 27 months after DSCP's award to PRGI, that PRGI and DSCP personnel reviewed those documents.)"

***Response: The audit work conducted by PRGI included a review of ALL government documentation maintained by the disbursing activity, DFAS Columbus, and by the Contracting authority, DSCP. Neither of these facilities had been apprised of, nor received documentation (as required by contract\*) relating to after-market price reductions (VPR's). From all records available, PRGI was able to ascertain the actual price paid by the government at the time of purchase. And from this, determine that in all cases resulting in claims, this price was higher than the price offered in the private sector for the same items during the same time frame.***

***The issue of Vendor Credit Memos in fact did not arise until the ALA had exhausted its previous attempts to 'kill' the audit. At that time the issue was presented that "...the government may have paid a higher price up front, but we [the ALA vendor] write checks and credit memos at all the individual commissary stores OConUS, so you eventually get a better price than our commercial customers."***

***When PRGI and DSCP were apprised of this allegation, PRGI immediately offered to visit the commissary stores and obtain the VCM documentation. NEITHER DeCA, NOR THE INDIVIDUAL STORES WERE EVER ASKED TO DO ANY OF THE CONTRACTOR'S "LEGWORK" FOR THEM. Further, each individual vendor was advised that if they had documentation refuting the claim in whole or part, they simply had to provide documentation***

*supporting their position. The vendor community's response was, at first, that they did not have any of this documentation...the ONLY place the documentation could be obtained was in the overseas commissaries. In point of fact, when the government asked for VCM documentation from the vendor, the response (with the contractor present in the room) was "...it's your documentation, you go get it from DeCA". {We can only surmise that the industry representatives believed that neither the government, nor the contractor would incur the expense of travelling overseas to obtain the documentation.}. Later, the industry amended its position, stating that it did have the records, but was not inclined to do the research needed to provide the documents as they were old and stored off-site.*

Point 4: " It is the ALA's understanding that DSCP was unable to find its own documentation for at least one of the years in question (FY 93). So PRGI simply assumed nothing had changed from year to year and sought recovery for FY 93, even though it had no documentation to support the claims. This fact alone points out the extreme difficulty, if not practical impossibility, in finding documentation to refute claims that are based on transactions, among hundreds of thousands of transactions, that occurred four, five, and six years ago. This, the ALA believes, is why the "warranty provision" extends only to the offer's "latest fiscal year".

*Response: This statement is flatly inaccurate. Although some hard copy documentation for FY 93 was not available, all the requisite electronic files were. Further, PRGI "assumed" nothing; if there was insufficient documentation available to justify a claim, the claim was not written. It is not in the best interests of any party to generate claims that are not documentable, supportable and collectable, since these would never be recovered for any client, public or private. Where claims were written for FY 93 transactions, the requisite documentation was reviewed by the contracting officer before approving the claim, and supplied to the vendor as part of the claim documentation. Further, all claims were written, and detailed to the Contract and CLIN level, including the number of units, purchase cost and extended cost for each line item, information only available from the government disbursing records.*

*Regarding the age of the claims, the fiscal years to be audited were stipulated by the enabling legislation. The older the data, the more difficult it is to obtain and work with for all parties, however, both the FAR and the DoDFMR stipulate that contract audits can go back six years, and this was well within the permitted time frame. Further, the IRS regulations on these types of financial records require they be maintained for seven years.*

*Finally, the assertion that the warranty clause extends only to the latest fiscal year is clearly without basis in either logic or law. The intent is to ensure that there is a commonality between the audit period and the records being reviewed. To do otherwise would require comparing the prices paid in FY 1993 to the prices offered by the vendor in FY 1999.*

Point 5: "While the Fiscal Year 1996 legislation required the private contractor (PRGI) to audit the DoD's records for FY 93, 94 and 95, that requirement did not, and could not, change or modify the existing brand name contracts and its 'price warranty' provision which in turn, is limited to the contractors "latest fiscal year". Accordingly, the government has the right to pursue ministerial clerical payment errors at any time prior to the close of the contract. Claims based on a warranty, however, are governed by the terms of that warranty. PRGI and DSCP continue to ignore this basic distinction."

*Reply: The ALA's assertion vis-à-vis the warranty clause in DSCP 3846 is untenable, and the government has already rendered an opinion to this effect.*

Point 6: "It was in the financial interest of both PRGI and DSCP to present the "discount for prompt payment" claims as if "billing advantage" was an independent warranty item, totally independent of the "average price" determination, because the documentation identifying that factor can be generated with little effort. The ALA believes this is one example of the problems caused by incentive-based audit contracts.

*Reply: Cash discounts for prompt payment are, in fact, a separate warranty item. The very nature of such discounts makes them discretionary on the part of the purchaser. When an invoice is presented for payment with stated terms of "2% 10 days, net 30 days", the purchaser has an option, pay in ten days and take the discount or pay in 30 days and pay the full invoice amount without discount. When a vendor elects not to offer the government the same discount terms as it makes available to the private sector, they are removing the government's ability to exercise such an option, and avail itself of these time value of money discounts.*

*Cash discount for prompt payment is solely a time-value-of-money issue, and has no bearing on the unit cost of merchandise. The sole purpose of a cash discount for prompt payment is enhance the vendors cash flow by incentivising the purchaser to pay the invoice earlier than the "net" due date.*

#### SUMMARY OBSERVATIONS:

Recovery auditing in the private sector deals with substantively the same issues, and in many cases the same vendors, as the current demonstration project within DoD. In the private sector venue, 80% to 90% of the claims written are collected, and where disputes arise, they are amicably resolved for the most part. The Federal Government, regardless of which agency or entity is involved, should be able to procure commercially available items in exactly the same manner, and with exactly the same advantages as the private sector.

The vendor community has, as well articulated by the ALA, however, sought to preserve a highly convoluted and, for them, lucrative procurement arrangement with the government. The fact that the ALA exists solely as an instrument to deal with military/governmental purchasing on behalf of commercial brand name suppliers, evidences the importance of the military market to its constituent members. There is no such private sector counterpart, nor does the ALA involve itself in private sector matters.