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,U.S. DEPARTMENT OF HEALTH, EDUCATION, AND WELFARE

THE SECRETARY'S NATIONAL CONFERENCE ON FRAUD, ABUSE, AND ERROR:

Protecting The Taxpayer's Dollar

December 13 and 14, 1978
Washington Hilton Hotel
Washington, D.C.

Conference Proceedings

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FOREWORD

I am pleased to present this report of the proceedings of the first Secretary's National Conference on Fraud, Abuse, and Error which we convened in December 1978.

The Conference assembled more than twelve-hundred representatives of local, State, and Federal program offices, investigative and law enforcement organizations, private institutions, executive and legislative bodies, and client advocacy organizations.

As the workshop and discussion group summaries in this report show, the Conference provided a forum for a wide range of viewpoints and the exchange of vital information on ways to improve efficiency and integrity in HEW programs, while continuing and enhancing the compassionate ends these programs are designed to serve.

There is no better symbol of the importance of the Conference than our keynote speakers: the President of the United States, the Attorney General, the Comptroller General, the Majority Leader of the U.S. House of Representatives, Governor George Busbee of Georgia, and Mayor Richard Hatcher of Gary, Indiana.

The Conference gave life and force to a strong conviction of mine: that we must demonstrate that social programs can be managed efficiently—that we must strive to give every citizen the benefits to which he or she is entitled—no more, but no less. I believe that the Conference and the proceedings in this report will help assure that taxpayers' dollars are not misused, that the quest for program efficiency is combined with compassion for the most vulnerable and disadvantaged among us, and that public confidence in government integrity will steadily grow in the years to come.

JOSEPH A. CALIFANO, JR.
Secretary of Health, Education, and Welfare

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NOTE: Workshop and Discussion Group Panelists and Speakers were invited to submit texts of their remarks to be included in the published proceedings of the Conference. All those which were received in time are included.

OPENING SESSION—WEDNESDAY, DECEMBER 13

Opening Remarks

Honorable Joseph A. Califano, Jr., *Secretary of Health, Education, and Welfare*

I'm happy to welcome you. This National Conference on Fraud, Abuse, and Error is, in my judgment, an historic event: the first time a Federal agency has sponsored a meeting on such a scale, with an audience so diverse, to discuss new ways of protecting the taxpayer's dollar.

It is especially significant, I think, that the agency is HEW—a Department whose budget is the third largest in the world, ranking behind only the budgets of The United States and the Soviet Union: a Department too often associated with free spending, but limited efficiency.

We meet at a moment when the taxpayers of this nation are demanding that the Government become a better steward of public programs and public funds. The American people deserve to hear about the efforts of Government to improve public management—efforts of states, counties, cities and efforts underway at HEW for the past 23 months.

Some of those efforts are by now so far along that we can count the savings to the taxpayers of America. I will be announcing some of those savings in my remarks tomorrow.

I believe that the story of those efforts is one of the most exciting stories in government. Indeed, the fact of this Conference itself is a profoundly positive story:

- It highlights the efforts of government at every level—and service providers who deal with government—to render themselves accountable.
- It underscores our efforts, in Washington and across the nation, to attract the best people to program management, and to put them to work cutting back waste, uncovering abuses and monitoring how funds are spent —using modern tools like computers.
- Finally, this Conference gives us an opportunity to point out to the Congress, the State legislatures and the American people ways of curbing "legislated waste." For it is a plain fact that much waste in public programs could be cut down or cut out by intelligent legislation: legislation to curb hospital-cost inflation, for example:

All of us are aware of one overwhelming reason for rooting out waste: the plain economic reason of scarce resources and the eroding effects of inflation.

But there are at least three other reasons that such efforts are important:

First: The programs we are concerned with are good programs; they serve millions of Americans well.

Federally insured student loans, for example, have helped more than ten million students and their families to meet the costs of education after high school. Ninety percent of students getting this kind of help pay back their loans, fully and dependably. By tightening the management of these programs, we make more funds available for more students.

The medicaid program of health care for poor families has played a role in reducing this nation's infant mortality rate from 24.7 per thousand live births in 1965 to 14.0 per thousand in 1977. To let a few unscrupulous practitioners escape undetected is to squander resources that could be helping poor children.

Our system of welfare, for all its faults, helps 7.4 million children and 4.2 million blind, aged and disabled people who cannot work to meet their needs for basic subsistence. We cannot let a relatively few cheats and chiselers rob the truly needy of the help they need.

So we intend to discipline these and other programs—while we fight those who would dismantle them. Why? Because we see efficient management as an act of compassion—an act that unlocks scarce resources to be used for human ends.

Second: We need to restore the trust and confidence of our fellow citizens in the competence of government.

A recent Gallup Poll revealed that nearly half of the American public believe that 48 cents of every Federal tax dollar is wasted. This reflects a serious exaggeration on the part of the public about the extent of waste and mismanagement— an exaggeration that all of us must work to correct. But at the same time, if such an attitude exists, right or wrong, it may not be long before the public seeks to cut back social programs in an undiscriminating way.

We must not, in our concern about management, lose our sense of perspective. But as long as there is public concern, we have an obligation

to earn public confidence by putting our house in order. Unless we do, our programs will suffer unfairly—and many people will suffer unfairly.

Finally: There is the simple fact that we who spend public funds serve as trustees.

The responsibilities that trust implies are nothing less than the wellspring of our democratic institutions. If we ignore that trust, not only faith in government—but the actual institutions of government will falter and fail.

So I think that it is important that we answer this call for accountability; that we seek to serve not only the poor and vulnerable, not only the handicapped and disadvantaged people who are our clients, but also the taxpayers and voters who place their trust in us.

I have high hopes for this Conference. If it succeeds, I believe we can look forward to several hopeful developments:

● All of us here will go home, whether to Washington, D.C. or more distant places, not only with renewed commitment, but with new knowledge and new techniques to use in the programs we manage.

● We may see the Congress, the state legislatures, and other jurisdictions, establishing new instrumentalities to combat fraud and abuse—or passing new cost-saving measures.

● The public will have a sense, not only of the problems we face, but a sense of our progress in solving them. For real progress is underway—progress that deserves attention. I intend to expand on this progress in my formal remarks tomorrow.

● Finally, this Conference gives us an opportunity to renew and strengthen the sense of partnership between the Federal Government, State and local governments, and service providers involved in federal programs. Strengthening that partnership will go a long way, in my judgment, toward making us once again a nation in which people think of their democracy as "We, the people" instead of "They, the government."

So let us get to work.

We have an impressive, richly diverse group assembled—and a crowded agenda. Our plenary speakers include a Governor, a Mayor, a Cabinet Officer, a Congressman, the chief federal auditors, and the President of the United States.

In these two days, this Conference will feature 25 separate workshops, seminars and discussion groups in addition to the open sessions. Their topics will range from new computer techniques to criminal prosecution; from financial management to the right of privacy. Well over a hundred experts from all over the nation will serve as panelists or discussion leaders.

Ladies, and gentlemen, I welcome you. I'm eager to learn from you. And I'm grateful to you for joining in this demonstration that government can work—if those who serve in government will work.

And so—to quote some ringing words of John F. Kennedy—let us begin.

INTRODUCTION OF GOVERNOR BUSBEE

By the Honorable Joseph A. Califano, Jr., *Secretary of Health, Education, and Welfare*

Ladies, and gentlemen, our first speaker, according to his biography, is the second of five children in a pioneer Georgia family. His father, we are told, was a farmer, a housebuilder—and a mule trader.

With a background like that, it was inevitable that he would go into politics.

So successfully has he gone into politics—in the finest sense of that word—that just last month, Governor George Busbee was reelected Governor of Georgia with 80 percent of the vote.

To earn such ringing approval a public figure must display not only political skill, but administrative achievement. And Governor Busbee has done that:

● As an "education Governor" he has pioneered a statewide kindergarten program for Georgia's schools; expanded job-training efforts and built a new system of teacher-aides to help teachers in the primary grades.

● He has established a State consumer protection agency and has led Georgia in protecting its coastline and other natural resources.

● And most to the point for this Conference, Governor Busbee has led a significant reform of Georgia's Medicaid system—determined that the system should serve all of those who were eligible, but only those who were eligible.

Governor Busbee's administrative achievements in the field of human services—and his stature as one of the outstanding governors in the Nation today—give him notable authority as our opening speaker today.

Ladies and gentlemen, Governor George Busbee of Georgia.

REMARKS

Honorable George D. Busbee, *Governor of Georgia*

Thank you, Mr. Secretary, both for your fine introduction and for the opportunity to speak to this distinguished group.

I can assure you that the problems of fraud, abuse and error in government programs are not foreign to me. In fact, one of the first acts I took after being elected Governor of Georgia, and prior to taking the oath of office, was to request from then-Governor Carter the funds necessary for an analysis of Medicaid provider payments in order to detect any potential program abuses.

Based on such in-depth study and with the help of our legislature, we in Georgia haven't been timid about attacking the problems we found.

A new procedure was developed and implemented to prohibit Medicaid payments for over-the-counter or non-prescription drugs in outpatient hospitals, because we found cases in which the State had been charged $50 for a bottle of 100 aspirin tablets or $80 for 19 cents worth of drugs. I appointed a drug formulary commission which developed maximum allowable costs for certain high-volume prescription drugs, and the resulting savings promise to be substantial.

We conducted comprehensive audits of dental statements against actual work performed, and were one of the first states in the Southeast to gain certification of a Medicaid Management Information System (MMIS).

We now have standardized policies and procedures manuals statewide, and have doubled the number of lawyers working in fraud and abuse prosecution. In order to constrain overutilization, I instituted a co-payment on drugs and applied for and received approval of a waiver from the Secretary of HEW to implement a system of co-payments on hospital and physician services in Medicaid.

During this time, I also chaired an intensive effort—a Task Force on Medicaid Reform—for the National Governors' Association. This group, composed of Governors and experts from 12 states, received advice and suggestions from all 50 states through 10 regional hearings and produced a comprehensive policy statement and detailed report which was adopted unanimously by the Governors. Because of the excellent cooperation of the Congress and the Administration, many of the reforms we suggested have already been implemented or responded to.

For example, federal health care financing and related quality control programs have been con-

solidated in the Health Care Financing Administration, thus reducing much of the confusion and duplication of effort heretofore experienced by the State and HEW in this area. HEW has also created the Institute for Medicaid Management to address the need we identified in providing better training and technical assistance to State Medicaid program managers.

A comprehensive recoding of Medicaid regulations is underway to address our desire to see simpler and more usable Medicaid rules and regulations. And as a final point among many, several bills have been introduced in Congress to significantly strengthen the capabilities of both State and Federal government to detect, prosecute and punish fraudulent activities under the Medicare and Medicaid programs. But, obviously, the problems of fraud, abuse and error haven't all been solved. All I've touched on thus far is simply Medicaid, and we still have a long way to go there, too.

Although Georgia has been able to alleviate many of the symptoms I haven't found a cure for the basic problem. However, many of the people I've heard discussing fraud, abuse and error haven't even found the problem.

Of course, it's easy enough to single out the welfare recipients, social workers, doctors, dentists, educators and students and blame them for the runaway costs which characterize these programs. It's easy, but not true. The vast majority who are involved in these programs are good, honest, caring people.

The basic problem is between and among the levels of governments trying to administer these programs. Let me give you some examples.

Remember the waiver on a co-payment for certain hospital and physicians services I told you I got approved? After gaining the Secretary's blessing, I was sued in Federal Court along with him. We received several conflicting opinions from within HEW on what we could or could not do, and finally the waiver was disapproved by a State Institutional Review Board, which was created and operated under guidelines promulgated by HEW.

Ironically, the Medicare program recognizes the value of requiring individuals to share in the cost of their medical care. They charge a $144 deductible per year on inpatient hospital services, and for outpatient hospital and physician services, they charge a $60 per year deductible and require a 20 percent coinsurance. Because of cost sharing, Medicare does not have overutilization and abuse like the Medicaid program.

But in Medicaid, regulations don't permit co-payments for required services.

However, in this age of limits, we must have some constraints in Medicaid. If co-payments can work for the elderly, there is no reason to suspect they won't work for the economically-deprived. I —and I believe the nation's taxpayers—believe the government must find ways to stretch its dollars, to temper its largesse with good sense, and to end the abuse of fiscal integrity by arbitrary regulation.

There are other examples of the same thing in regulations that have nothing but the best intent and often have the opposite effect.

In the nursing home program Congress requires states to pay "reasonable costs" for nursing home care. "Reasonable," however, seems to translate into a requirement to pay whatever the operators think they need, which amounts to an open ceiling on inflation. I have a request in HEW right now to institute a negotiated fee system for physicians, in order to address this type of problem, but it looks as if it will be denied.

Unless we take steps such as this, we will continue to experience gross overutilization of our system, and over-utilization—according to our estimates—greatly exceeds fraud and error.

As another deterrent to this problem, we developed and received approval on a demonstration project called "Cost Effective Alternatives to Nursing Home Institutionalization." This project has developed a system of community-based foster and daycare programs for the elderly poor and afflicted as an alternative to the more costly and often debilitating nursing home.

We must develop alternatives to institutionalized health care in hospitals, nursing homes and institutions.

It is programs such as this, if adopted as a national policy, which can help not only reduce overutilization, but also help bring skyrocketing costs down, while providing more humane care.

Regarding costs, I referred earlier to a comprehensive dental audit we conducted which gained a number of indictments, received the full cooperation of our Dental Association and truly made excellent headway. The deterrent factor from publicity associated with a trial is incalculable. But the cost for the staff time of federal, state and local investigators is also incalculable. There simply has to be a more cost-efficient way.

If we at the state level are going to be partners with HEW in attacking fraud, abuse and errors, we must have some latitude under your regulations.

I find it inconceivable that regulations in the Guaranteed Student Loan Program, for example, have not been issued for a period of more than six years, although Congress has changed the

laws governing the program at least three times during that period.

On the other hand, I find it inconceivable, when states are expected to change matching ratios, or implement on a moment's notice changes in ways of doing business—which might substantially increase state costs—simply at the whim of a guideline writer. All too often such guide lines carry penalties—such as loss of eligibility—if you fail to comply. Such guidelines, in too many instances, go way beyond legislative intent and are issued without adequate prior consultation with those who are expected to operate within them.

Under such conditions, large error rates are understandable. But even an error hasn't been adequately defined. In food stamps, federal law requires that we have a caseworker review eligibility and grant amounts every six months. Now suppose just after our caseworker visits, a grandmother moves in with a family to avoid going to a nursing home. Six months later, our caseworker notes a change in the number of persons in the household. During this time payments have continued, but we must register this case as an error, which becomes part of our error rate.

Finally, I would be remiss if I did not mention duplication of effort as a problem which contributes to fraud, abuse and error.

The worst of all complexities is in federally-supported student loan programs. The federal government now provides some form of financial support to seven different loan programs.

This mixture of overlapping and uncoordinated programs, each with its own rules and regulations, is mind-boggling to me, and I'm sure that it is to students, parents, educational institutions and state program administrators. Even though Secretary Califano has moved to pull the HEW Student Aid Programs into one Bureau, these programs and the various other loan programs are in no way interrelated nor coordinated with each other. Many students can obtain loan funds under more than one of the programs, which presents great repayment and servicing hazards to all parties concerned. The terms, conditions, definitions, loan limits, interest rates, repayment requirements, cancellation options, lenders of record, eligibilities of students, and administrators responsible for these programs, vary in practically all respects. Multiple borrowing is possible. Consolidation of loans under the different programs is not possible. And change does not appear imminent.

The probability of mismanagement and resulting waste in such a bewildering complex of loan programs, run by different departments of the

federal government, concerns me greatly as a taxpayer. I want to emphasize that I am not talking about the possibility of a loss resulting from a student in not paying a loan, for I believe experience has shown that in a properly run program, all but a relatively small percentage of students do, within time, repay their student loan obligations. Instead, a way must be found to reduce the number of federally-supported student loan programs and to simply and effectively coordinate their administration.

Lest my message to you be misunderstood, let me say that my purpose here today is not to lay blame, it is to assess the need for change. It is not to identify symptoms, it is to identify causes. The examples I mentioned were not offered as excuses, but as fact.

They are facts which point to the system we employ to initiate and administer the programs for the poor, the afflicted, and the disadvantaged. And I say to you candidly, that unless we address the system and the ways the three levels of government relate to one another, there will be no significant reductions in fraud, abuse and error.

For too long in these programs, the three levels of government have pointed the finger of blame and accusation at one another over our collective inability to effectively deal with problems facing the people we serve. And, unfortunately, we at all levels of government have done such a good job of blaming our faults on each other, that we have convinced everyone that government in general is inept and unworthy of public trust and confidence.

So I say to you that we must change the system—we must find ways to work together. And I believe that there are certain keys to this change, if it is to come about properly.

The first key is flexibility. As long as those who are in Washington continue to not only say when and why something ought to be done, but also say where resources ought to go and how problems ought to be addressed—in a completely standardized way—then we are going to continue to find misdirected allocations of funds, outright fraud and rampant abuses.

The second key to constructive change rests in the area of incentives for efficiency, rather than in penalties. Presently an administrator is not rewarded for efficiency or for reductions in errors or abuses. He or she is penalized for non-compliance with goals that are set arbitrarily or according to the mean. Put simply, what we need is more government incentives and fewer government insanities.

Thirdly, I believe another key is already being

turned with the President's initiatives on guideline simplification. Better, simpler, and clearer guidance is a must. But I would caution that simply understanding more clearly who is the final decision-maker is no solution if that decision-maker is at the wrong level of government.

Finally, the last key to constructive change is better prior consultation, and this can only be addressed by the federal government under the current rules. Legislation, regulation, guidelines—all are only going to be as effective as the consultation on the front end is with those who are expected to administer and live within them.

I believe the time has come when we need to add to our vocabulary the term "sunrise legislation" as a corollary to "sunset legislation."

What we need more of is federal legislation which is well-thought-out, designed, and drafted in a joint effort with the states and local governments before its enactment into law. Following legislative action, sufficient "sunrise" time should be allowed for the adoption and review of all necessary rules, regulations and procedures before the date on which such legislation shall become effective. And finally, the administering agency ought to be required to promulgate the regulations within the required time period. In other words, we must allow time for the "sunrise" so that the dawning of any major legislation enacted can come about in an orderly and efficient manner.

If we would take a little more time in the front end, we might all better avoid the criticism of fraud, abuse and error in the final end.

Thank you.

INTRODUCTION OF MAYOR HATCHER

By the Honorable Joseph A. Califano, Jr., *Secretary of Health, Education, and Welfare*

Our next speaker long ago grew accustomed to being first.

He was the first freshman councilman in the history of his city to be elected city Council President.

He was the first black mayor of Gary, and one of the first black mayors among America's largest cities.

But in one important area, he ranks only twelfth: Mayor Richard Hatcher of Gary was number 12 among his parents' 13 children.

Perhaps having come along so late helps explain why Dick Hatcher has always run so fast and worked so hard.

He worked his way through Indiana University waiting tables—then worked his way through law school by serving an eight-hour shift each day in a hospital.

By the time he was 29, Dick Hatcher was Deputy Prosecuting Attorney in the Lake County Criminal Court. Before he was 35, he was the Mayor of Gary.

America's cities today are the critical front lines in our effort to provide adequate human services and a better quality of life to people who need help and opportunity.

Dick Hatcher comes to us fresh from the front lines.

We all know it is not easy to get Richard Hatcher to come to Washington. Today we have succeeded in getting him to come.

Ladies and gentlemen, Mayor Richard Hatcher.

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REMARKS

Honorable Richard G. Hatcher, *Mayor of Gary, Indiana*

WILL, SKILL AND MORAL FIBER— SIMPLIFY AND END ABUSES

Secretary Califano, Attorney General Bell, Comptroller-General Staats, Governor Busbee, fellow participants in this conference.

I am pleased and honored to have been chosen to address you today, at this important conference on a most important subject. On second thought, maybe I am no more honored or pleased than is a man invited most cordially to attend his own hanging. However that may be, it is certainly true that whatever comes out of this conference, we will surely echo Ben Franklin's famous and probably apocryphal dictum—that is, we must all hang together, or we shall surely hang separately. And hang we will, it would appear, unless we can find a way to convince the voters of the nation that funds expended for various federal programs which benefit the poor, the inner cities, the disadvantaged are spent because they must be. And that they are spent wisely and well. When Secretary Califano called this conference, he wrote to participants:

"In an era when budgets are expanding, when the public is resistant to new taxes, and when there is skepticism about the ability of government to function effectively, public officials face a critical challenge—to demonstrate that social programs can be managed responsibly and effectively.

If we seek additional funding to meet pressing human needs, we must also prove that existing resources are not misused."

The Secretary puts the issue well—expanding budgets, skepticism on the part of the electorate as to efficiency and responsibility.

The problem, of course, is very real. Error, fraud and other abuses apparently account for some 7 billion dollars in the HEW budget—and that's enough to rebuild downtown Gary and have enough left over for rebuilding Newark, and several other cities. The figures cited in testimony before the Congress are intriguing. Speaking to the House during debate on the HEW and Labor Department budgets, on June 8 of this year, Illinois Representative O'Brien had the following to say; I quote:

"The HEW Inspector General reports, apparently concurred in by the Secretary, showed some $7 billion of losses in the Department of Health, Education, and Welfare alone. The largest part of these losses, $4 to 5 billion, was associated with health care outlays; but the remainder is attributable to error, fraud, abuse, and waste in the welfare, income security, education, and social services programs, a sum approximating $2 to $3 billion.

About 50 percent of the losses is attributable to errors, errors made in the Department or by the state or local personnel, and through human error in the eligibility determination process, or through improper payments resulting from mistakes in the paying of bills or claims, all mainly due to just plain carelessness."

That is a startling set of figures indeed, and one which cries out loud for corrections. Certainly all of us must agree that such waste—whether it be intentionally fraudulent or merely the result of ineptitude—must be addressed and eliminated.

But of course it is all too easy to agree that there is a problem, and to agree that we must do something about it. What is to be done is a more difficult question, and how the problem arises may be even more difficult. It is interesting to note, in the figures cited by Congressman O'Brien, that the problem is only partially, and indeed almost peripherally, a problem of local enforcement. That is, if one removes the health care outlay problems, which are not at all controlled by municipal officials, and takes half of the remaining 2 to 3 billion dollars cited by Mr. O'Brien as attributable to local flaws—and, since Mr. O'Brien is a Republican, it is probable that his figure is not low—about 1 billion to one and one half billions of dollars in error is attributable to local disbursement of funds. Now, I submit that, while it is not a good thing to have such error, given the magnitude of the budget, we are probably talking about a degree of error on the local level which is within normal statistical proportions.

Nevertheless, one would wish to avoid even such error. Especially in the area of welfare, it is important to do so for political if for no other reasons. Those who are the enemies of poor people—there are such, no matter what they call themselves—spare no pains to try to make of welfare fraud a major issue of national concern. It is interesting to note, by the way, that the same people who have fits about welfare fraud have very few fits about equally illegal and much

more egregious fraud in the Defense Department or in the professional, corporate and business side of American life.

That includes, one is interested to note, medical fraud, which always requires the aid of a rather well-paid section of our society, the physicians. That problem is instructive. How is a local official to deal with medical fraud? Doctors, after all, are the only ones who can decide what procedures need to be undertaken, and since we have no national health insurance programs, doctors are the only ones who can decide how much to charge for such procedures. That the medical profession is not fraud-free was once again proven by a devastating investigation in Chicago by some reporters and some investigators for the Illinois Better Government Association. They found that a group of physicians and other health care professionals were suggesting abortions for women who were not pregnant—and, in a couple of cases were finding evidence of pregnancy from samples of male urine. It is very difficult for local officials to guard against that kind of fraud, which, in other more complex medical procedures, no doubt accounts for part of the 4 to 5 billion dollars lost in health care outlays which Representative O'Brien cites.

As for the Defense Department, it is well-known that Senator Proxmire has found a good deal to complain about there. Columnist Jack Anderson, in a column entitled "Let the Taxpayers Pay," and dated December 7, 1978 in Chicago, provides some information which indicates that, just in the area of property disposal, hundreds of millions of dollars worth of equipment is lost, stolen or misused each year. Strange to say, I have not heard an outcry equal in volume to that which one hears when someone is labelled by the press a "Welfare Queen." Maybe we need to add to our "Welfare Queens" our "Military Hardware Kings," to right the balance a little.

My point here is that it does not make sense, except in the context of a particular kind of politics, to address the question of fraud, error and abuses in the human services area only. We can all agree that we should avoid fraud, abuses and error—just as Christians can all agree that they should avoid sin. But it is a little difficult to find much will to do so in the areas most closely related to the needs of the most helpless in our society when those who are not helpless at all—the rich, the powerful—seem to line already well-lined pockets by such unlawful and immoral means. It is harder for the poor to be pure when the rich are corrupted.

On the other hand, I would be the last to say

that because someone else's skirts are dirty, mine ought not to be clean either. I would like to discuss, then, a few problems having to do with possible reasons for fraud and error on the local level, which may be of use.

One of the most important reasons why fraud and error are as prevalent as they appear to be in the human services areas, and in welfare programs in particular is simply that there are so many programs, and they are so complicated. SSI, AFDC—the alphabet soup list of agencies administering to the poor is endless, and one must add to it the local distributors of welfare, local welfare departments and, for certain kinds of aid in my own state, an agency called the Township Trustee. The complexity of these programs is such that a little-noted recent development in legal services programs and in other law reform groups has been something called welfare advocacy, where lawyers train lay people to steer welfare recipients through the maze of agencies and alphabets from which they might receive badly needed assistance—and such advocacy is badly needed by people who by definition are least able to cope with complex systems.

That problem is hardly new. In a paper prepared for a conference to evaluate anti-poverty programs held at the University of Wisconsin in 1974, Laurence E. Lynn, Jr. professor of Public Policy at the J. F. Kennedy School of Government at Harvard comments, I quote:

"Though one may be sympathetic to incrementalism as a short-run expedient, it is hard to resist the conclusion that the eventual overhaul and simplification of the income-maintenance system is desirable in both programmatic and human terms. The existing, highly complex income-maintenance system is unfair, inefficient, and counterproductive. People do not understand it, nor do they have confidence in it.

A number of recent developments improve the chances for eventual enactment of welfare reform, especially some form of income supplementation plan or negative income tax."

It is now four years later, and there is no such simplification in the welfare process as that suggested by Professor Lynn on the horizon. Obviously, if at least some if not all of the various programs involved in human services could be combined under one roof—and even more, if they could be dispensed without penalizing the poor—fraud and error would be reduced greatly. Income maintenance experiments have shown to date that there is very little loss of work incen-

tive if people are given hard cash money. I quote Professor Lynn again:

"The results of the New Jersey graduated work incentive experiment . . . clearly indicate that a negative tax type plan with a basic benefit as high as the official poverty line will not trigger large scale reductions in work effort among male heads of families . . . . Thus, there is now a respectable body of evidence laying to rest a fear that often seemed to dominate earlier welfare reform debates: that primary wage earners would significantly reduce work effort if they were generally eligible for cash assistance."

A similar experiment conducted in my own city, in Gary, indicates similar results. But nothing has yet happened to create such income maintenance programs, or any others, which would reduce the complexity of welfare and other human services programs to a level where adequate supervision and policing could significantly reduce fraud, error and abuses.

But the problem of reforming welfare is very difficult, and is deeply enmeshed in the coils of American racism. In commenting rather sharply about Professor Lynn's paper at the same conference, Lester Thurow, Professor of Economics at M.I.T. says:

"The war on poverty started as a war on white poverty in the late 1950's but it had become, and was perceived as, a war on black poverty and low relative incomes by the middle of the 1960's. This perception has both its strength and its weakness. The need to do something about blacks led to the passage of many of the programs, but many of the programs failed to reach their funding goals because they were seen as programs that aided blacks and not whites. One cannot understand the problems with AFDC mothers unless one understands that the public generally thinks of this program as one that aids "black" mothers.

Politicians of all convictions have been convinced that you can be beaten if you publicly advocate general welfare reform. To be for reform is to put yourself into a position where you can be portrayed as being in favor of welfare. This leads to defeat. At the moment this political perception of reality is the major obstacle to any negative income tax general welfare reform package."

I think Professor Thurow's perception as valid today as when he offered it. For many white politicians, at least, welfare reform is a dirty

word. There is no doubt in my mind that much of the "taxpayer revolt" characterized by Proposition 13's passage in California is fueled by a conviction that those blacks are getting all sorts of government money they shouldn't be getting. Given the response to the taxpayer's revolt by politicians in the last few months, it seems unlikely that any serious welfare reform will come about. Given the fact that, as Professor Thurow says, welfare is perceived as black welfare, it is unlikely that the same political forces who have thrust the Bakke decision upon us, who have passed a variety of Proposition 13's in various localities, and who are more than willing to spend for weapons but less than willing to spend for welfare, will help bring about welfare reform.

In light of these political facts—facts based on race as well as on class—I confess that I see little hope for substantial reduction in welfare and other human services fraud, error and abuses.

I would like to have such hope. I am more than willing to join those who wish to exhort us all to be honest, to condemn carelessness and crime, cupidity and stupidity—but I don't think such exhortations and condemnations will do much more good than exhortations against and condemnations of sin. Short of systematic reform which makes the welfare process a simpler, more manageable one, little can really be done.

There is one other approach, of course, and it is an approach which is finding much favor lately and which, I am sorry to say, is even being echoed in President Carter's recent budget statements. If we cut down on aid given to the poor, then we'll have less fraud, at least in total dollar volume, though not as a percentage of allocated funds. That's one way to do it. Such an approach, it seems to me, suggests that welfare is somehow something that the affluent and good give to the poor and bad, rather than a process which attempts to make up to the poor and unfortunate for the social disabilities which an unkind nature or a racist and class-biased politics has imposed upon them. Such reform, such reduction of abuse, fraud and error is inhuman and not worthy of Americans. Besides that, it is dangerous, as the burning streets of Detroit, Watts and Chicago's West Side amply demonstrated a few years ago.

I have tried to deal with an important aspect of this problem as best I can, but I do not think that I have resolved what is a proper and appropriate aspect of the work of this Conference. Secretary Califano has in mind, I think, the very appropriate feeling that efficiency and honesty ought not to be left as the property of the anti-welfare, anti-liberal forces in our country, that

those of us who consider aid to those in need of aid a first national priority ought to take our responsibilities to provide such aid efficiently and honestly, seriously, and thus to take away from the far right a ploy it has used very effectively against the rest of us.

I agree with the Secretary, if that is his intent. It will appear self-serving if I say that in my own administration I have used the toughest political clubs available to me to assure that honesty and efficiency are the rule, and fraud and error the exception, but I will say it nonetheless. Moreover, I suspect the same is true of most of those officials, at the municipal level at least, who share my outlook about welfare in general. In fact, I have suggested elsewhere that we have little choice about that, since especially black leaders in our country continue to be watched most carefully by law enforcement officials and get in trouble if they even look like they're doing wrong, much less if they actually do wrong.

I join the Secretary, then, in saying that all of us must bend every effort of our will, every ounce of our political skills, every atom of our moral fiber to assurances that human services programs are as efficient, as honest, as legal as is humanly possible. I also will gladly endorse any practical notions which come from this conference which will help me in Gary and which will help other officials in my state and in the nation to make such efforts of will, skill and moral fiber a reality.

But I cannot end this address to so distinguished an audience without also saying that it will take some significant reversal of priorities before these efforts will pay off very much. We will have to assure, first of all, that not only human services programs, but Defense Department and all other programs exercise the same efforts of will, skill and moral fiber towards honesty as we are prepared to exercise. Secondly, we will have to find ways of changing the notion abroad in our land that welfare is somehow a rip-off of the rest of the nation by black people, so that we can begin to go about the business of serious reform and simplification of existing welfare programs. Will, skill and moral fiber notwithstanding, only simplified programs will be policeable in such a way that we can assure honesty, efficiency and rectitude. Finally, I think public officials will only respond to the needs this conference has expressed if all of us go the extra needed mile to change the attitude of the nation towards welfare. It behooves us, while demanding efficiency and honesty, to also make clear, over and again, that people are entitled to welfare as part of the American system, that they receive

welfare not because they are bad, but because nature or the social system have done them some harm for which they bear only little responsibility.

If we can revive the notion that the war on poverty, ill-health and ignorance is as important —no, is infinitely more important—than any other war we have ever fought in our history, if we can create an atmosphere of crusade for and not against the poor and the disadvantaged, then I believe will, skill and moral fiber will begin to take hold, and fraud, error and abuse will abate.

I wish I had simpler answers to offer here, but I do not. I hope this conference succeeds in creating a new attitude, a new approach, and a new era in the welfare system as a whole, and that fraud, error and abuse will soon be things

of the past. They will be things of the past for certain, of course, if we end the extensive need for welfare, and bend our wills, skills and moral fiber towards the massive reduction of poverty, as well.

Thank you.

NOTES: The Citation from Congressman O'Brien can be found in *Congressional Record*, June 8, 1978, p. H 5159.

The Citations from Professors Lynn and Thurow can be found in Robert H. Haveman, Ed., *A Decade of Federal Antipoverty Programs*. New York: Academic Press of Harcourt, Brace Jovanovich, 1977, pp. 115 & 119.

INTRODUCTION OF THE COMPTROLLER GENERAL

By the Honorable Joseph A. Califano, Jr., *Secretary of Health, Education, and Welfare*

As Jove sat in judgment on the activities around Olympus, so does our next speaker sit in judgment on all the activities around Washington.

That is a heady—and heavy—responsibility, but Elmer Staats, as Comptroller General of the United States, handles it superbly, The General Accounting Office which he has headed since 1966, is a model of thorough, impartial, non-partisan inquiry into the integrity and effectiveness of Government programs. It is the world's most powerful audit organization.

Some government officials view an unsolicited letter from GAO with the same enthusiasm most of us feel for little green envelopes with the initials "IRS" in the corner.

In fact, GAO is the single most potent source of knowledge on how effectively Federal programs are being carried out. GAO produces about 1,000 significant reports a year; the Comptroller General personally approves those that are submitted to the Congress.

But Elmer Staats is more—far more—than a public servant who oversees and important agency, he is a scholar and philosopher of government—and a living symbol of unselfish public service.

His 40 years of Government service also include distinguished tenure in the Bureau of Budget, which he joined in 1939. He became Deputy Director by appointment of President Truman in 1950 and served under four successive Presidents. I think it is fair to say that he has had a longer and more sustained impact on Federal budget policy than any other official in history.

He is also one of the most diligent and even-tempered officials with whom I have been privileged to work. Near his desk he has a sign that each of us might do well to copy. It reads: "If a man likes to work, he can have a hell of a good time in this office."

Ladies and gentlemen, Elmer Staats.

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REMARKS

Honorable Elmer B. Staats, *Comptroller General of the United States*

PREVENTING FRAUD AND ERROR AND INCREASING PUBLIC CONFIDENCE IN FEDERAL PROGRAMS— TOP PRIORITIES

I welcome the opportunity to be present this morning to underscore the concern of the General Accounting Office—and the legislative branch of the Federal Government—in the critical subject which will be addressed by this group over the next two days. While the term "Fraud, Abuse, and Error" may strike some as being somewhat negative in tone, certainly the subtitle, "Protecting the Taxpayer's Dollar," is appropriate and one to which all can subscribe without reservation. My congratulations therefore go to Secretary Califano and his associates in the Department of Health, Education, and Welfare for this constructive initiative. We will all derive much from this conference which should strengthen public confidence that the Government is actively pursuing ways to deal with these problems.

Much has been said and written in recent months—possibly too much—about the loss of confidence in Government. These statements come not only from political leaders, the investigative press, and from interest groups, but from a broad segment of American society. "Proposition 13" and similar actions taken by voters in many States attest to this fact. Public opinion polls support this conclusion. Summarizing these polls, a writer in the current issue of *Fortune* magazine concludes that "Not since the days of the Great Depression have Americans been so complaining or skeptical about the quality and character of their country's public performance." He states that Americans have lost "confidence that Government can accomplish those things the people want done **." He concludes that "the tax protest is based on a genuine belief that Government can and should do all that it is doing—but much more efficiently." The call, he says, is "not for *less* Government but for *better* Government." That is

what this Conference is about.

It is often stated that no one knows the extent of fraud, abuse and error in carrying out Federal programs—and that, of course, is true. But whatever the amount, it nevertheless is a matter of wide public concern just as fraud and abuse in the private sector is a concern.

I know that you will join me in the conjecture that those who abuse their public trust are a tiny fraction of the three million Federal employees who work conscientiously and honestly day in and day out; observing the highest standards of ethics in all that they do. Their reputation is damaged—and the public confidence in Government is damaged—when a tiny minority commit fraud, where serious waste and mismanagement occur, or the Government is not able to protect itself against those who would defraud it.

Important as the detection of fraud, abuse and errors is, *detection* should not be our primary concern as Government managers. Our prime concern should be directed toward constructing systems of management control that will *prevent* fraud and abuses, make it more difficult, and decrease the likelihood of error and waste. When it comes to fraud, abuse and error, the old axiom that "an ounce of prevention is worth a pound of cure" fits well.

For a moment let us examine some of the benefits of preventing rather than detecting and punishing fraud, abuses and errors. The first thing is the obvious advantage of reducing expenditures. Fraud, abuses and errors all result in the outflow of Federal dollars that Government managers are supposed to use sparingly. To the extent we prevent fraud, abuses and errors by good management systems, we stem this source of unauthorized expenditures and thus carry out our stewardship responsibilities more effectively.

However, the loss of dollars—important as that may be—is not the only cost of fraud, abuses and error. Equally important is the toll in human suffering that occurs when the perpetrators of fraud and abuse, or even sometimes errors, are discovered. While it is true that some perpetrators of fraud and abuses are hardened criminals, a great many of them are made criminals by opportunities presented to them which they are not strong enough to resist. These opportunities usually occur because the management controls that should eliminate such opportunities have not been established; or, if established, have fallen into disuse. When such persons are caught, they suffer humiliation, loss of jobs and income, and frequently alienation from friends and family. Their lives are ruined. Often, they go to prison and that has not only a high cost in human

suffering but a high cost in dollars as well. Our jails are full enough.

If we can prevent some people from committing fraud or abuses by removing temptation, we have not only served the Government but we may have saved some fellow employee from himself or herself. Even errors can cause extreme embarrassment and if serious enough, may threaten a person's employment.

GAO Study of Fraud Potential

With this in mind, the General Accounting Office undertook in mid-1976 an effort to ascertain whether Federal agencies had instituted effective policies and procedures for combating fraud that might exist in their programs, whether committed by Federal employees, by recipients of Federal assistance, or by others. In doing this, we had to formulate criteria regarding the composition of an effective antifraud effort. It seemed to us that the essential elements of such an effort would include

- a set of procedures to assess the vulnerability of the programs in question. We wanted to learn if agencies had thought through the type of fraudulent schemes to which their programs were susceptible.
- the comprehensive collection and analysis of information on known incidents of fraud. The question here was whether the agencies were alert to identifying patterns or trends in the types of frauds being perpetrated.
- an aggressive effort to follow-up on instances of fraud that may have surfaced, not only to react but also actively seek out fradulent schemes. We wanted to know whether the agencies were "policing" as well as "investigating".
- strong leadership on the part of the Department of Justice in bringing its expertise to bear on the overall problem. Our intent here was to find out if Justice was doing what it could in assisting the agencies to combat fraud.

Our next step—arduous and time-consuming—was to identify and gather evidence needed to confirm or deny the existence of the postulated problems. We reviewed activities at the Departments of Agriculture; Labor; Transportation; and Housing and Urban Development, and the Veterans Administration, General Services Administration, and Small Business Administration. We examined these agencies' policies, procedures, and records and held discussions with their offi-

cials at headquarters and field offices of five States. We also performed work at the Department of Justice's Civil and Criminal Divisions and at various U.S. Attorneys offices. We believed this kind of coverage was necessary if we were to draw broad conclusions.

Although bright spots existed here and there with respect to an individual agency's antifraud activities, the existence of problems in the Government's ability to fight fraud was established. Some of our findings bear repeating to illustrate the magnitude of the problem.

The Government's financial assistance programs are vulnerable targets of fraud and related white-collar crimes. Identifying the extent, nature, and frequency of these illegal acts, together with strong internal controls and effective audit coverage, are essential first steps to combating and preventing them. Yet the agencies we reviewed were not doing *nearly enough* to identify fraud.

Federal programs involving grants, contracts, and loan guarantees are exploited through such means as

- false claims for benefits or services,
- false statements to induce contracts or secure goods or services,
- bribery or corruption of public employees and officials,
- false payment claims for goods and services not delivered, and,
- collusion involving contractors.

How Much Fraud is There?

As I said, no one knows the magnitude of fraud against the Government. Hidden within apparently legitimate undertakings, it usually is unreported and/or undetected. Opportunities for fraud, however, are tremendous when you consider the magnitude of some Government disbursements. For example,

- The Veterans Administration has annual outlays of approximately $18 *billion* in support of veterans benefits,
- The Department of Health, Education and Welfare has annual outlays of approximately
  - $109 *billion* in Federal and trust funds in support of the Social Security system,
  - $10.5 *billion* in welfare payments
  - $10 *billion* in grants to States for Medicaid, and
  - $3 *billion* for student assistance.
- Federal procurements in FY-1977 were almost $80 *billion*, including GSA procure-

ments for supplies and services, and DOD procurements of major weapons systems.

We found that agencies have not established management information systems to deal with the fraud problem. They do not know the amount of identified fraud in their programs. They cannot estimate the potential amount of unknown fraud. We noted, however, that individual case data was kept which could be used as a basis to formulate such a system. Without such data, agencies have no basis for establishing the level of resources needed to combat fraud, map antifraud strategies, and evaluate the scope and effectiveness of antifraud activities.

Until recently, agencies have not made fraud detection a high priority because their overriding concern has been program execution and emphasis on such program objectives as providing loan assistance. The low priority given to fraud detection leads to passiveness regarding potentially fraudulent situations.

Also none of the agencies reviewed has, until recently, designated a focal point responsible for seeking out and identifying fraud. Consequently, they generally take a reactive, rather than active, approach to fraud detection. However, a reactive approach is inadequate for detecting fraud, since there is often no specific incident to react to.

Agencies have no assurance that those personnel administering programs are referring all suspected frauds for investigation because:

- There are no controls to see that suspicious matters are reported.
- Large workloads hinder identifying suspected fraud by program personnel.
- Employees lose interest in reporting suspected frauds when follow-up actions, such as investigations and prosecutions, are not promptly taken.
- Many Federal programs are administered by State, local, or private sector institutions, and Federal agencies often unjustifiably rely on those non-Federal entities to identify and report frauds.

Agency investigators often do not have the background, experience, and training needed to effectively detect and identify fraud. About 70 percent of the staff involved in agencies we reviewed had no prior experience in fraud investigations, and about 80 percent had no formal training in investigating fraud. Where investigators have such training, it was generally limited to procurement fraud. Most investigators have also lacked the education in finance and accounting-related subjects often needed to iden-

tify fraud. Since fraud against the Government often involves examining financial documents, absence of a financial background could be detrimental to effective fraud investigations.

The Department of Justice needs to provide stronger leadership; it has been slow to assist, coordinate, and monitor the antifraud efforts of Federal agencies.

In 1975, Justice, recognizing the need to deal with white-collar crime, established a white-collar crime committee. One activity of this committee was to provide guidance to agencies on combating fraud. It has met extensively with agency officials and has assisted agencies in carrying out several successful projects demonstrating the existence of fraud in their programs. However, the effectiveness of this "outreach" function relies on the receptivity of the agencies to Justice's encouragement and the availability of resources Justice can devote to it. From a recent conversation with the Deputy Attorney General, I am much encouraged that the Department recognizes the need for a more active role by the Department.

Agency Recognition of Agency Action

But overall, a more positive, systematic approach to identifying fraud is needed. Our report on this subject was issued in September of this year. It contains specific recommendations to assist Federal agencies in their efforts to address comprehensively the fraud and abuse problem. I am hopeful that agencies will respond by following up on reports of the General Accounting Office and internal auditors.

I am happy to report to this conference that aggressive action has been taken:

- Before passage of legislation establishing Inspector Generals, several agencies such as Agriculture, HUD, VA, and Labor, administratively set-up an Inspector General type operation.
- The White Collar Crime Seminar sponsored by Inspector Generals from the Departments of HEW, HUD, and Agriculture.
- Among the agencies we reviewed, HUD's operational surveys are the most ambitious systematic mechanism aimed at actively seeking out and identifying fraud. The operational survey combines HUD investigators and auditors in a team which concentrates its efforts on a single HUD office. The surveys are aimed at uncovering deficiencies in program management and

identifying specific irregularities, which indicate possible fraud, for investigation.

Establishment of a GAO Task Force

As a follow-up on our report, I have established a Special Task Force for the Prevention of Fraud and have allocated substantial staff resources to assist the Task Force. The major responsibility of this group will be to:

- evaluate the adequacy of the management control systems in Federal agencies that are necessary for the prevention of fraud, and
- assess the adequacy of the follow-up and corrective actions taken on reports of auditors and investigators.

When systems have been properly developed and are functioning as planned, the possibility for fraud, theft, or error is greatly diminished. Where the systems do not exist, or are not being used properly, the opportunities to defraud the Government and the possibilities of error increase dramatically.

I intend to have the Task Force concentrate on agency controls over cash and receivables, inventories and supplies, and anything else of value that might be stolen or misappropriated if controls are weak. Since computer systems offer many possibilities for fraud, we will identify weaknesses in computer controls over payrolls, payments to vendors, and cash disbursements for other purposes. We will also be looking at the controls in effect to ensure that the Government gets what it pays for, and that work set out in contracts is actually performed.

The Task Force will analyze the reports of internal auditors in each agency it reviews, giving particular attention to indications of fraud or error the auditors have uncovered. Where these reports or our reviews show that controls are weak, we will search for potentially fraudulent situations, using our own computerized data retrieval and analysis packages where practicable. At the conclusion of our work at each agency, we will prepare a report to the Congress and the agency involved, with particular emphasis on any weaknesses in management controls that would permit fraud, theft, or error to occur.

Based on our findings to date, we are assigning the highest priority to fraud and abuse reviews. In fact, we will pull people off other high priority work, and as our work progresses, we may find it necessary to allocate even more staff. With the Task Force acting as the central or focal point,

all our work on fraud and abuse will be brought under the umbrella of the Task Force. This procedure permits us to develop an operational capability very quickly. Task Force members are already working to coordinate fraud and abuse type reviews planned or on-going within all our divisions. By mid-January, we expect to have our first list of specific reviews.

Since prevention will merit top priority in the fight against fraud at GAO, our work will concentrate on fixing or strengthening control weaknesses found in agency systems that permit fraud to occur. One of the best ways to prevent fraud and abuse is a series of checks and balances called internal controls. For example, when these controls operate effectively, one employee's work is usually checked by another in such a way that no one employee can abscond with agency assets without detection. The system also tends to identify error. Although no system is entirely foolproof, an effective series of checks and balances greatly decreases the likelihood that fraud and abuse will occur.

As we uncover potential fraud and abuse, we will be looking for patterns that can be explored in other agencies. And, as individual cases of potential fraud and abuse are disclosed, we plan to work closely with staff of the newly established Inspector Generals, and the Department of Justice to assist in conducting investigations necessary for prosecution. We are working out detailed procedures that will provide GAO periodic status reports on all cases referred to the Inspector General or Justice. Generally, we view our role as one of prevention rather than criminal investigation and prosecution.

Importance of Agency Accounting Controls

As most of you know, the General Accounting Office is responsible for approving agency accounting systems. We approve the design of such systems, in many cases before they are installed. In performing our work, we give a great deal of consideration to what controls are provided for and how they will be implemented. We are frequently appalled when we return to audit such systems after they have been installed because we find that many of the controls we considered important have been dropped.

Let me give you two simple illustrations. A "hash total", for example, is a very important control over card input to computers. This is simply a total of some number from all the cards and is used to be sure that all the cards go into processing. If a card is lost, the total will be wrong and the operator of the system will know a card is missing. Similarly if some one introduces an extra card, the total will also be wrong and the operator again alerted. In our audits we find time and time again that this simple control is not operating although the system design called for it. When we inquire as to why the procedure was dropped, we receive answers like "It took too long to check out all the cases where the totals did not agree" or "our workload increased so much we had to drop something".

A second control that we find is frequently overlooked is the "limit check." This control is usually used in payroll systems. Limit checks should reject any payment for more than the biweekly pay of a GS-18 and require special processing for any checks over that amount. This prevents the kind of error often associated with computers, that is, the issuance of a payroll check for some exhorbitant amount like $99,999.99. It also prevents anyone from running a fraudulent check through the payroll system for any amount over the biweekly pay. The limit check alone is not enough to prevent fraud, abuses or error but coupled with other similar procedures it can be effective. It is also a simple procedure because it can be built into the computer program. Yet time after time in our audits we see that limit check has been dropped because it requires some additional effort when rejects occur.

Today the problem of financial controls is changing—radically changing—and as the direct result of the use of computers. I do not intend to demean computers. They enable us to perform many Government functions much more economically than we could perform them manually. Moreover, many functions we perform today in Government would be virtually impossible without the computer. However, computers have complicated the internal control problems and we need to change our methods to adapt to the computer.

In some of the more advanced systems we see today, the documents involved are often thousands of miles apart; a purchase order in New York, a receiving document in California and an invoice in Washington, D.C. In some cases, particularly for small purchases, the transaction may occur in its entirety without any meaningful examination of physical data by any Government employee. The order is generated by the computer when stocks get too low; the goods are received and the computer notified. The invoice is received and the computer notified, and the match of the documents is made by computer and a disbursement authorized by the computer. Finally, the check is signed by a signature insert in the computer and no one has really examined the whole transaction. For such a system, the old ways no longer work.

We need a whole new set of controls based on the way the computer system operates. Moreover, when we rely so extensively on computers, it is essential that these new control systems be in good working order, for we have nothing to rely on to protect the Government against fraud, abuses and error except the control systems.

We had roughly 500 years after the Italians invented double entry bookkeeping to develop internal control systems for manual accounting systems and even then they were not perfect. We have only had about 20 years since computers became used extensively to adapt the internal control approach to computers. Frankly, much remains to be done to get the internal controls in such systems to a level that we can feel comfortable about them. Moreover, a system of surveillance is needed to see that the controls we have do not fall into disuse.

If these control systems are to function effectively, top management must take a direct interest in seeing that they work. Accountants and auditors are, of course, key people in this process but if these systems are to be kept in repair and a viable protection against fraud, abuse and error, management also needs to be concerned. The needed controls often require that functions be performed outside the accountant's area of responsibility and therefore may extend beyond his purview. Due to other priorities, the auditor's work may not be done with sufficient regularity to see that controls are kept up-to-date. Management must see that all the responsible officials cooperate in setting up the necessary controls and that the personnel resources necessary to keeping them effective are devoted to the task.

Lest I be accused of not considering cost, I want to add here that all controls have to be weighed in the cost-effectiveness scale. We call this risk analysis at GAO and by it we mean assessing the potential damage the lack of a control might permit and comparing the cost of the control with that potential damage. It is possible to be overcontrolled; however, from what our audits have disclosed, I doubt that most Government agencies have too much to worry about in that regard—at least for the immediate future.

Growing Congressional Interest

The Congress has recognized the need for better control in the private sector in the Foreign Corrupt Practices Act. The section of the act prohibiting corrupt payments is well known. The act also contains a less well known section requiring affected corporations to devise and maintain an adequate system of internal accounting controls sufficient to ensure that transactions are executed in accordance with management's authorizations, that transactions are properly recorded, that access to corporate assets is controlled, and that assets and records will be compared and reconciled at reasonable intervals. Such a system is a goal all Federal agencies might well strive for.

From my nearly 40 years, experience in both the executive and legislative branch of the Federal Government, I have seen the value of audits and investigations and the changes they can bring about. Therefore, I do not downplay their significance in any way but for our purpose today, audit and investigations will be a big help, but alone, they will not be enough. Federal auditors and investigators have many priorities, they do not ordinarily perform detailed audits of procedures to see that they are working on a routine, periodic basis. Unless they, or someone else, does make such reviews, it will be hard to keep effective internal control systems going.

Unfortunately, auditing and investigative staffs have had low priority. Accounting and auditing have generally received little attention until and unless something goes wrong. This situation is changing however, with the newly enacted legislation which created Inspectors General in 14 major Departments and Agencies, reporting directly to the agency head or his deputy and given a specific statutory mandate by law. Of particular interest to us in the GAO is the provision authorizing us to set audit standards to be followed by the Inspectors General in carrying out the functions assigned to them by the Act. As many of you know, we have had standards for Governmental audits since 1972. These standards are entitled, Standards for Audit of Governmental Organizations, Programs, Activities and Functions, but are usually called the yellow book because their formal name is so long. We will be reviewing these standards during the next year to see if they should be supplemented to give more emphasis to the need to prevent and detect against fraud, abuses and error. We welcome the suggestions which I hope and believe this conference will bring about.

Ethical Standards are Basic

Before concluding, I would like to say just a word to stress the importance of high ethical standards for Federal employees. Again, we should remind ourselves that fraud, abuse, and

error have two origins. One is with Federal employees themselves and the other with those outside of Government who take advantage of weaknesses in the Government's financial controls to obtain personal profit for themselves. However, there are a great many cases where both elements are involved. A strong ethical awareness among Federal employees will do much to remove the temptation for these employees to violate the trust which has been vested in them and to make them more aware and sensitive to the violation of such standards by others.

President Carter has had much to say on the subject of ethics and his leadership has undoubtedly had much to do with interest on this subject in the Congress itself. And I might add that the General Accounting Office has given very high priority to the review of financial disclosure systems, ethical standards, and, in the end, the monitorship of these standards by the executive agencies. We recommended and the Congress established an Office of Ethics to administer the

Executive Branch program in the Ethics in Government Act of 1978. I believe this Act will do much to enhance employee conduct and add to the integrity of the Federal Government's operations. It is an important step in preventing temptation, conflict of interest, fraud and other abuses.

Last week, I attended a program celebrating the 100th anniversary of the establishment of the Office of Auditor General of Canada and heard a leading British Member of Parliament give a brilliant address on the importance of audit and accountability in government. He observed that democracy, like love, will withstand all attacks except indifference and neglect. He concluded that the role of the auditor serves to remind us that "if we do not learn the lessons of history we will be condemned to relive it." In this Conference, we need to remind ourselves of the public trust we hold and to act—and to act visibly— to do whatever we can to demonstrate to the entire Nation that we can act responsively and responsibly in protecting the taxpayer's dollar.

INTRODUCTION OF THE ATTORNEY GENERAL

By the Honorable Joseph A. Califano, Jr., *Secretary of Health, Education, and Welfare*

Our next speaker endeared himself to me when—at one of the first meetings of President Carter's cabinet—he told the following story from his long and distinguished legal career:

A defendant was hailed into court in Georgia, charged with being drunk and with setting his bed on fire.

"How do you plead?" the judge asked.

"Guilty to the first charge, your honor," the defendant replied, "but innocent of the second."

When the judge looked puzzled, the man explained, "It's true that I was drunk, your honor. But the bed was already on fire when I got into it."

That story expresses the feeling of all of us who find ourselves facing difficult public problems: we know the feeling of having climbed into a burning bed.

And nowhere are things hotter than where Griffin Bell sits. Nowhere are keen judgment, unswerving integrity and deep wisdom more essential.

And no one in Government displays those qualities more prominently than the Attorney General.

I have worked closely with Judge Bell on several controversial issues involving our two Departments. He and his staff have provided us legal judgment on some highly complicated questions such as abortion, the rights of handicapped citizens, alchohol and drug abuse problems.

In the process, I have learned that Griffin Bell sees things as they are—and calls them as they are, with impregnable courage and integrity.

I admire him as a lawyer.

I respect him as a colleague—and I value him as a friend.

Ladies and gentlemen, the Attorney General of the United States, Judge Griffin Bell.

REMARKS

Honorable Griffin Bell, *Attorney General of the United States.*

Shortly after I became Attorney General, Secretary Califano told me that he had instituted two antifraud programs and explained some of the things that are being done in HEW. To the best of my knowledge, he was the first person in the new Administration to decide to do something about program fraud—that is, fraud in the Government. Since then, the Labor Department has been doing some of the same things with their programs. You all read about the GSA investigation, you read about the SBA investigation, and there are others.

But I want to give Joe Califano credit for starting all this. He is the person who offered the leadership to do something about fraud in Government. He had the feeling and the knowledge that in the last fifteen or twenty years in this country we have had a loosening of discipline. That is nowhere more true than in Government programs where you give money away. Many people set out now to steal from the Government. Twenty years ago, if you stole from the Government, it would be considered a high crime. Today, many people seem to condone it. I don't condone it. I'm doing everything I can to stop

such stealing from the Government. I don't think that the taxpayers will suffer that sort of conduct much longer.

And we are doing a great deal. My initial problem was to decide how to accommodate a really vigorous program against white collar crime, including Government fraud, into a system where the government had been doing things in a different way for a long time. So what we did at the Justice Department was to set priorities—this was early in 1977.

The priorities for Justice and for the FBI are white collar crime, organized crime, public corruption, and drug trafficking. Of course, the FBI has one category of business that's even higher than those four, and that's foreign counterintelligence.

White collar crime includes program fraud, which is the subject of this Conference. Public corruption includes investigations of public officials—local, State, and Federal—who are involved in some form of stealing—bribery, payoffs, that sort of thing. The last figure I saw indicated that there are about 700 public corruption investigations going on in this country. Now that

doesn't mean that suddenly everyone has become more corrupt. It means we are investigating more than we ever have before.

After setting those priorities, we decided that we would have to take one more step, and this eventually will have to be taken throughout the Government. We decided that we ought to study the allocation of resources. We live in a system which we call Federalism, encompassing local, State and Federal governments. We decided to look at who ought to be investigating certain types of crimes and who ought to be prosecuting. I instructed the U. S. Attorneys to begin to meet with all the local prosecutors in their districts. started meeting with the State Attorneys General; Mr. Civiletti, my Deputy, meets with them now on a quarterly basis. We are shifting over to the States some of the things that we used to do. Some things we can do better than the States, but we have studied the allocation of resources carefully. This eventually will have to be done in all government programs.

We've made great progress. We are vigorously investigating and prosecuting white collar fraud cases. We know they are more complex, and the investigations are tedious. We have only 800 accountants in the FBI out of 8,000 agents. We need more accountants. We need people who understand computers and data retrieval systems, people who can compete with the law breakers. That's what it really gets down to. Are we good enough to compete with those who understand how to commit sophisticated fraud? I think we are good. I think we're going to win. The main reason we're going to win is because we're set up for the battle, we're set up to win.

For one thing, we are getting great assistance from the agencies. The agency investigators know a great deal more about what's going on in the agency than we know at the FBI or in the U. S. Attorneys' offices or in the litigating divisions at the Department. We are there to help, we are there to prosecute, but we have to have some assistance from the agencies. We are getting a lot of help from the agencies and we are giving assistance, too. In 1978, so far, we have trained 600 agency investigators at seminars. We're setting some new standards of reference— when do you refer a case from the agency to us for investigation based on criminal activity.

I see good spirit on the part of all agency heads, the general counsels, the chief investigators. We're going into the next Congress with an omnibus white collar crime bill, which is needed. We'll have to continue to work on an interagency apparatus, particularly since we're getting all the new inspectors general.

We stand ready at the Justice Department to help in any way. If you have an investigation where you need us and we're not already in the case, call us. That's all you have to do. We're the lawyers for the Government, and we're the lawyers for the American people. That's what I perceive our role to be. As lawyers, just as if we were in the private sector, when our clients need us, we are available.

Someone wrote in a play about 400 years ago that the world seemed to be out of square. Well, our system of Government sometimes seems to be out of square, but I think we're putting it back in square. It's a good time to be Attorney General, and it's a good time to have a person like Joe Califano as Secretary of HEW—he's really good at his job. It's a pleasure to work with him. I think all of us working together will put our system back in square. It's not much out, but we're working to put it back in.

Thank you very much.

INTRODUCTION OF THE PRESIDENT

By the Honorable Joseph A. Califano, Jr., *Secretary of Health, Education, and Welfare*

Ladies and gentlemen: It is the happy fate of the best American Presidents to become identified with a great idea.

For Abraham Lincoln, that idea was union for this nation and freedom for all people.

For Franklin Roosevelt, that idea was economic justice and security for every American family.

For Lyndon Johnson, it was the idea of equal opportunity for the dispossessed, whether they were black or poor or old.

Our next speaker embraces all those ideas of his predecessors. But already, in less than two years in the White House, he has become identified with a great idea of his own: the idea that the people's government should serve the people; and that it should work with maximum integrity and excellence.

When he campaigned for office and when he came to office, that idea was in eclipse: the American people had lost faith in their leadership and their institutions.

Jimmy Carter promised to restore the trust of the American People. I believe he has already accomplished that. Through his leadership, this nation's government has been restored to its rightful owners—the American people.

Ladies and gentlemen: the President of the United States.

REMARKS

The President of the United States

I am delighted to join you today for this crucial conference. I want to commend Joe Califano for once again taking the lead in the efforts of my Administration to root out fraud and waste and abuse of taxpayers' money from this government.

This Administration has declared war on waste and fraud in government programs. With your help we will win that war.

We are concerned with more than saving dollars, crucial as that is today. We must restore and rebuild the trust that must exist in a democracy between a free people and their government.

My Administration took office after a painful and difficult period in American history, as you well know. The experience of Vietnam, of Watergate, revelations of wrongdoing by intelligence agencies, the resignations of a Vice President and President, the indictment and conviction of top government officials—these hit the American people like hammer blows, over and over again. Each shattered, a little more, the trust and confidence of the American people in their government and their elected officials.

Cynicism and distrust eat away at the vitality of a democratic nation. Lincoln once said, "With public confidence everything is possible; without it nothing is possible."

Over the past two years, slowly and steadily, we've begun to restore the trust and confidence of the American people.

But it is not enough for people to have confidence in the good intentions and personal integrity of those who hold public office. The American people must also know that government is capable of doing its job. Fraud and abuse and waste undermine that precious confidence.

Those who rob from government rob from every steel worker, teacher, store clerk and truck driver in America. Under this Administration, those who rob from the American people will be prosecuted to the full extent of the law.

I do not believe that Americans want to go back on the promise of a better life and a fairer society. The heart of America is too big for that. The American people will not accept callousness toward those among us who are aged or sick or jobless or lacking in education or opportunity. But neither will the American people accept a massive bureaucracy that is too clumsy or too poorly managed to do the job.

Most of the funds we spend in Federal programs benefit the people for whom they are in-

tended. As a known or suspected part of the total Federal budget, losses through fraud, abuse and error may be small. But compared to the tax bill of the average American, those losses are huge—and demoralizing.

The real damage of fraud and abuse cannot be measured just in dollars and cents. For the value of the people's trust and faith in their institutions of self-government is beyond price.

If we are to be successful in our efforts to make government work better, one myth must be dispelled at the outset—the myth that the values of compassion and efficiency are somehow in opposition to each other.

That is as asburd as imagining that a physician's medical skill is the enemy of his or her dedication to curing disease. Nothing could be more totally, more dangerously wrong.

When a program is poorly managed—when it is riddled with waste and fraud—the victims are not abstractions, but flesh-and-blood human beings. They are the unemployed teenager who gets shut out of a job—the senior citizen deprived of a needed medical service—the school child who goes without a nutritious meal—the taxpayer whose hard-earned dollar goes down the drain.

When I lived in Plains after retiring from Naval Service, I was able to start a small business processing peanuts because I obtained an SBA loan when I could not raise private funds. There are thousands of Americans, many of them members of minority groups, who dream of starting a business of their own, and seeing it grow and thrive and having that pride of personal independence. It is a cruel hoax to these Americans to see those dreams destroyed by those who abuse and defraud the SBA.

Those of us who believe that our society has an obligation toward its weakest members have the greatest stake in improving the management and efficiency of the programs that are designed to meet that obligation. This is especially true when the battle against inflation makes it impossible to bring vast new resources to bear on our social problems. At such a time—indeed, at any time—efficient management is in itself an act of compassion, for it unlocks new resources to be used for human ends.

There is a second myth—the myth that it is somehow more compassionate, more committed to appropriate another billion dollars of the taxpayers' money than to streamline an existing program so that it delivers an extra billion dollars' worth of service.

In fact, the latter is preferable in every way. It saves money, of course. But it does more than that.

Efficient management increases political support for a program among those whose taxes pay for it. It gives the lie to those who prefer to believe that programs that meet human needs cannot work. It inspires and boosts the morale of government employees who are deeply frustrated when their hard work is frittered away through waste or fraud.

I did not select that one-billion-dollar figure at random. This is the amount that Joe Califano has vowed to save in fiscal 1979 by cutting deeply into waste and fraud in the Department of Health, Education and Welfare.

Joe's efforts, and those of thousands of others working with him at HEW, are already showing good results.

Project Match is sifting out those on the Federal payroll who are illegally receiving welfare benefits.. The project is very new, but it has already repaid its million-dollar cost twice over.

Project Integrity is nailing the thieves and con-artists among health care providers.

Thanks to tough management of the student financial aid program, the number of student defaulters is falling instead of rising for the first time in the program's ten-year history—and the backlog, which hit 400,000 last March, is projected to be at zero by the end of 1980.

The credit for these successes belongs to an active partnership between the Federal government and the states and localities.

Similar efforts are underway in other parts of the Federal government. The Labor Department is attacking abuse in the CETA program. The Agriculture Department is fighting illegal trafficking in Food Stamps. At the Small Business Administration and the General Services Administration, we are cracking down on fraud and theft. At the Department of Justice, the prosecution of fraud within the government is now a high priority.

The headlines generated by these activities do not always make pleasant reading. But those headlines are a sign not that things are getting worse, but that they are improving.

When I campaigned for the Presidency, I promised the American people a compassionate and competent government. I have not swerved from that goal. Our expanding attack on waste and fraud is just one facet of a long-term effort that began the day that I took office.

That effort has made progress on many fronts:

I have used the appointment power to place the best people I could find at the head of the departments and regulatory agencies—reform-minded men and women who are free of the conventional orthodoxies about regulation and administration.

I have embarked on reorganization of the Federal government to eliminate the waste caused by duplication and bureaucratic overlap.

I submitted, and the Congress passed, the first sweeping reform of the Civil Service system in its century-long history. Civil Service Reform gives the departments and agencies a chance to strengthen their total management systems. It gives us the ability to deal firmly with those few who are dishonest or incompetent, and it increases the rewards for efficiency and effectiveness and accountability. It is a major step toward building a Federal workforce dedicated to competence and integrity at every level.

A year ago, we instituted a program of special recognition for Federal personnel at all levels who suggested improvements in doing government work that produced savings of $5,000 or more. The results were astounding. In one year, 1,380 people in 29 departments and agencies contributed improvements that brought savings of over $210 million—more than the total average income taxes of 95,000 Americans.

These results show that good management and effective use of incentives are as effective in reducing waste and fraud as enforcement and punishment.

The Civil Service Reform Act provides greatly increased cash awards, both from agencies and from the President, for employees who make significant suggestions, improve government operations, reduce paperwork, or perform special acts or services in the public interest.

We have waded into the thicket of pointless red tape and regulations that waste the time of citizens and state and local officials. For example, we inherited more than 1,700 separate planning requirements in various grant and aid programs. We are chopping away at these overlapping requirements and have eliminated or consolidated more than 300 of them in the past year. We're still at it, and HEW is setting the pace.

Last year, I asked the heads of the departments and agencies to improve their audit coordination and increase their reliance on state and local audits wherever possible.

A government-wide effort led by OMB and the General Accounting Office has now come up with a breakthrough in auditing Federally-assisted programs—a single guide to replace the almost one hundred now in use.

We need to bring the same kind of simplicity to our public assistance programs.

Today the welfare system of one state eats up 3 billion pieces of paper each year and a thousand different forms. A woman seeking economic aid in another state had to spend 300 hours in one year filling out paperwork documenting her need.

For this reason I am today asking Jim McIntyre and Joe Califano to head a major effort to simplify and streamline the hundreds of complex eligibility requirements which contribute $3 billion each year to the cost of public assistance and other human services programs—an administrative cost over and above what actually goes to the recipients. We will move to simplify these procedures where it really counts—at the State and local level.

Where we have the tools to root out fraud and abuse, we have put them to work. Where they did not exist, we are creating them.

Perhaps the most important new tools in the fight against fraud are the Inspectors General created in six departments and six agencies of the Federal government by an act of Congress I signed eight weeks ago. The Inspectors General will be a powerful new tool for the discovery and elimination of fraud. They have broad powers and a significant degree of independence.

I will choose these Inspectors General carefully. I want them to match the high standard set by Tom Morris, the first Inspector General I appointed at HEW, who has helped save the American taxpayer half a billion dollars since the beginning of 1977.

I have already directed Jim McIntyre to oversee the systems the Inspectors General will run. I want to be sure that in each department covered by the law, the auditing and investigative functions are meshed in a smooth and effective way.

Today I am taking a further step. I am directing that significant features of the Inspectors General program be extended throughout the Federal government. Each agency and department will prepare a plan for eliminating waste and fraud in its own activities, and will designate a single official to oversee the preparation and implementation of that plan. I have assigned the Office of Management and Budget responsibility for overseeing this effort.

I am looking to the Attorney General to assure that investigations by Inspectors General and their counterparts are effectively coordinated with other investigative and prosecutorial activities, so that criminal matters receive immediate and efficient attention.

The fight against waste and fraud will require the best efforts of us all. New programs and better enforcement will help. But our most important weapon in this struggle is the vigilance and dedication we bring to it. I call on all who work in government—Federal, State and local—to join me in this battle.

The stakes are high. If we succeed—as I believe we will—we will have kept faith with the

millions of men, women and children whose human needs our society has pledged to meet. And we will have kept faith with ourselves. For the ultimate beneficiary will be democratic self-government in this America that all of us love.

I. HEALTH WORKSHOP

Moderator

Leonard D. Schaeffer
Administrator
Health Care Financing Administration, HEW

Panelists

Charles J. Hynes
Deputy Attorney General
Office of the Special Prosecutor
State of New York

William C. White, C.L.U.
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REMARKS—"FRAUD INVESTIGATION AND PROSECUTION"

By Charles J. Hynes, Deputy Attorney General, Office of the Special Prosecutor, State of New York

The well-being of any system is dependent upon the full participation of all of its constituents. Over the last few decades, Government has increasingly acknowledged its responsibility to provide a program of health care and to equalize the economic extremes that are at the source of social injustice.

Hard figures on the cost of quality health care don't exist, yet we are continually being made aware of the mounting inflation of these costs. The Department of Labor reported in August 1978, that rising medical costs were a major factor this year in driving up the cost of living for retired couples by seven per cent.

For too long, fraud and mismanagement have been hidden within the costs of health care. They are not as easy to identify as a finger on a scale, because buying health care is obviously not the same as buying apples.

For nearly four years, my office has dealt with the problems of Medicaid fraud and mismanagement in New York State and while we have been reasonably successful in identifying and solving many of the problems, it is clear that lasting improvement will require a major overhaul of the program of delivering and paying for health care in this country.

Until we design and implement long term reforms in our health delivery system the crisis will continue.

In the past year, the President and the Congress have given us for the first time since the advent of Medicaid and Medicare the opportunity for reform.

Many of you know that on October 25, 1977, President Carter signed a bill which gives to each state the resources to contain health care fraud. The basic purpose of the law commonly referred to as HR 3 is to improve the capacity of State and Federal governments to detect, prosecute,

punish and discourage fraud and abuse by providers participating in the Medicare and Medicaid programs. Congress has wisely concluded that without meaningful state programs of criminal prosecution, health fraud cannot and will not be controlled.

The legislation contains funding incentives for states to establish Medicaid Fraud Units with statewide investigative and prosecutorial powers over the entire Medicaid system. Such units, if they meet the Federal standards, receive Federal reimbursement of 90% of their costs over the next three years.

It should be the goals of this investigation to substantially eliminate health care fraud, to work with the Health and Social Services agencies on the problems of mismanagement and then finally, to discover what has never previously been known —the real costs of health care. But let no one become overly optimistic. We in New York who have spent four year searching for this solution— have still much to go.

Let me review briefly the New York experience: What led to the nursing home scandals of the early '70's—What has happened since 1975.

The ancient Greeks judged whether a nation was civilized by the way it treated its elderly and by that test an aroused media in 1974 and early 1975 shamed all of us.

From August of 1974 through the early days of 1975, our eyes and our ears were pounded daily with horror stories of squalid conditions in nursing homes across the state. Stories of sub-standard food, stale and sour, stories of our elderly forced to lay in their own excrement while their bedsores festered unattended. While these stories shocked and disgusted us—what truly outraged us were stories of a wholesale rape of the State and Federal Treasuries by thieves who ran too many of these homes and to whose care we had committed our helpless elderly. We heard stories of trips abroad, mink coats, summer homes and swimming pools—all financed by Medicaid dollars.

And we were further outraged to discover that this scandal was nothing new—that thirteen years before in New York City the same thing had occurred and worse—many of the same people we read about in 1974 were involved in 1961. We learned that in 1961 no one was prosecuted and that restitution was limited to 10–20 cents on the dollar and that incredibly these thieves were permitted to remain in business.

On the 10th day of his new Administration in 1975, Governor Hugh L. Carey created a Moreland Commission under the direction of a distinguished lawyer, the former President of Brandeis University Morris B. Abram, and he directed that my office be established.

Because of the enormous media exposure concerning allegations of poor care in our nursing homes, particularly in the urban centers of New York State, we concluded that there would be an intense effort by the owners to clean up the homes and provide decent care. And so, while we immediately instituted a joint program with the Department of Health of unannounced on-site inspections of nursing homes throughout the state, our primary focus was concerned with allegations of fraudulent transactions. We set up a rather simple investigative triangle consisting of a lawyer, an accountant and an investigator which was to become known as the "Team Approach". The auditor was the first line of offense. It was his job to peruse the subpoenaed books and records of nursing home operators and to carve out items which appeared suspicious. The investigator would then take these leads and approach vendors who did business with nursing home operators. These two specialists were, throughout the investigation, supervised by a lawyer who closely screened the evidence acquired with a clear understanding that ultimately, the investigation could lead to the court room and beyond—to the appellate courts for review.

Let me give you one example how the team approach works. During the review of one particular home, the auditors found invoices for 400 paintings valued at $60,000,—lithographs with an average worth of $150—the auditor was told that these were to brighten up the residents of that home and three other homes owned by the operator.

Our investigators interviewed health inspectors who had been to all four homes and who told them that there was nothing resembling described lithographs in the homes for that price but rather there were a few cheap cardboard scenes hung in various locations. The investigators took note of the fact that the address of the vendor was in an area where very expensive shops were located. At first, the vendor was uncooperative. He was subpoenaed—as were his books and records. His attorney quickly understood that unless he could prove that he had purchased 400 paintings, it would be difficult to prove that he had sold 400 paintings to the nursing home operator. The vendor finally admitted that he had sold several paintings including a Utrillo to the nursing home operator for $60,000, and had made invoices out for many cheaper paintings and addressed them to the nursing home.

Our investigation has revealed a number of schemes between vendors and nursing home operators. For example, the use of:

1. Inflated Billings—An agreement in which a vendor gives a nursing home a bill for more than is actually purchased. The bill is then submitted to Medicaid for reimbursement.
2. Phony Billings—Instances where a vendor gives a nursing home a bill without supplying any goods or services.
3. Phony Items—Bills are submitted which include actual goods purchased as well as listing items that were never intended for purchase or delivery.
4. Front Money—Where a vendor, in return for a long-term contract, offers a nursing home operator a loan and the loan is paid back with the help of inflated bills and subsequent Medicaid reimbursement.

Of course, few investigations of fraud can begin without first obtaining books and records. From the beginning of the investigation, we were barraged with motions to quash our subpoenas. To give you some idea, we have litigated more than 400 subpoenas. The fact that we have been successful in more than 95% of these cases is attributable in all candor to a combination of the competence of our lawyers and the frivolousness of the challenges to our subpoenas. Fortunately, we have dealt in the main with reputable lawyers and so ultimately, we have been able to obtain most of the books and records but there have been enough instances of more plagues than those visited on the Egyptians to frustrate us. There have been claims of destruction of books and records through fire, flood, burglary, and employee thievery as well as unexplained disappearances. The history of one subpoena litigation will give you some understanding of that problem.

On April 8, 1975, we subpoenaed the books and records of a nursing home. A motion to quash our subpoena was promptly brought in the lower court. We were successful there and in the Appellate Division and finally, in December of 1975, in the New York State Court of Appeals, which is the highest state court—the nursing home operator then went into the Federal District Court, then to the Circuit Court of Appeals and finally, to the United States Supreme Court. At all stages we were successful. But, it took us until the fall of 1977 when, for the first time, the nursing home operator appeared in the lower State Court and said he could not find his books and records. The judge, in holding the operator in contempt, said eloquently, "Books and records, unlike some ill-starred vessels sailing the Bermuda triangle, do not disappear without explanation upon the presentation of a subpoena from a Special Prosecutor". Now held in contempt, the defendant appealed the contempt citation—first, to the Appellate Division, then, to the Court of

Appeals and up through the Federal system, losing all the while, and finally on April 10, 1978, more than three years after the service of the first subpoena, he was incarcerated and ordered to remain there until he produced the books and records. He remained in jail until mid-August, when he petitioned the Court for a new hearing.

In the petition, he raised the issue that his constitutional right was being violated because he had testified under oath that he simply did not know where the books and records were. The petition was dismissed but the Court released him from the jail to permit him to appeal that decision. The defendant is currently out on bail, awaiting a decision from the Appellate Division. He will undoubtedly go to the Court of Appeals and on to the Federal system once again and we have still not obtained the books and records.

This kind of delay is not unique to the criminal side of our investigation. We have had, for more than a year, a civil recovery component in our office operating statewide. This was as a result of our belief which has been translated into HR–3 that criminal prosecutions alone do not satisfy the needs of a successful health care delivery system.

On the one hand, deterrents for white collar criminals and expulsion from the business of health care is obviously a desired result. It is every bit as important to exact restitution from convicted operators and to pursue recovery of State and Federal money which has been overpaid to operators against whom a successful prosecution will not lie.

So it was in the early part of our investigation, we relied on the Department of Health and its administrative hearing process to recover overpayments. When it became clear that the system was not working, that delay made it impossible for early recovery of health care funds, we obtained, with the cooperation of the Governor, our Attorney General and the Legislature, the necessary allotment to set up a Civil Recovery Unit. The unit has already brought lawsuits which total more than $12 million. The combined efforts have resulted in the recovery, by either cash or absolute assessment of assets, of nearly $7 million.

Our audit reports to date, which represent an indepth review of all private proprietary nursing homes in the State of New York, point to more than $63 million in overpayments. It will be the task of the Civil Recovery Division to pursue the return of these funds.

On the criminal side to date, we have indicted 147 individuals and of the 109 completed cases 8 have had their cases dismissed, 7 have been acquitted and 94 people have been convicted.

We look back today on a health care system in New York which, while not perfect, is on the sure road to the successful containment, if not total elimination of fraud, and yet the elimination of fraud, however critical in the effort to control costs, must not be viewed as a panacea. It is to be Medicaid's most apparent problem. But in terms of our entire health care system, it is not the only problem. This nation has been talking about national health care for many years. Based upon present predictions, total annual health expenditures will go up $85 billion by 1980, reaching $224 billion. Hospital care is already averaging well over $200 a day and at some major medical centers the rate will probably reach $500. Physicians already higher paid than members of any other profession, will probably be earning a median income of over $80,000 a year.

Providers are given little, if any, incentive to economize—cost ceilings, where they exist, are generally based upon operator vs. operator comparisons and nothing more. With Government and private insurers presently paying 90% of our health bill, currently totalling $140 billion, consumers have virtually no chance to directly influence health care costs. However, each of us, as taxpayers and insurance consumers, is affected by uncontrollably rising health care costs.

For in evaluating and comparing any national health policies we have basically three criteria:

- Quality of care
- Cost
- And Distribution of Care

These criteria cannot be carefully analyzed unless some predecisional activities take place, including a careful compilation of facts about our current system.

HR-3 affords us this opportunity. For make no mistake about it, unless we succeed in deter-

mining the cost of quality care minus fraud and mismanagement, we cannot have a successful national health insurance policy in this country.

Anybody who has had experience investigating Medicaid fraud for any period of time knows that the uninstitutionalized elderly poor, to name one group, desperately need some form of national health insurance. And when we realize that 24 million Americans have no public or private health insurance programs, and that 8 million of these Americans have incomes below the poverty line and some 88 million more Americans have no insurance protection against catastrophic medical expenses, it is obvious that we need some form of national health insurance.

But no responsible public official can seriously call for wholesale national health insurance without addressing himself to the need for effective fraud, waste and management control. The tragedy of Medicaid-Medicare in my judgment is that our humaneness was not accompanied by healthy cynicism. That our desire to give to the disenfranchised the benefits of a free society was not tempered by a simple and empirical fact that there are enough parasites abounding in this nation to wreck any social welfare program.

But we have the capability to contribute significant information needed to formulate an economically feasible national health insurance policy. In order to be most consequential we must not define ourselves from a narrow point of view, because we have the chance to not only rid this field of fraud and abuse, but also to determine the true cost of health care.

Oliver Wendell Holmes, Jr., wrote "The life of the law has not been logic, it has been experience."

In the case of health care, it will be our experience that serves as a foundation for national planning.

REMARKS—"MODEL SYSTEMS— ABUSE DETECTION CONTROL"

By William C. White, C.L.U., *Vice President, The Prudential Insurance Company of America*

For many of us working in the health care industry, a new "catch phrase" has now infiltrated our daily language in the last few years called "Fraud and Abuse." It is spoken almost as one word, and, to those charged with its detection and investigation, it seems to be an appropriate and correct linkage, since they frequently coexist. We have all seen coverage in the press and on television about the numerous ways in which

the health care dollar can be obtained unethically.

Interspersed among these sensational stories have been others, featured in a lower key, citing prosecutions, fines, sentencing and loss of licenses for those obtaining Medicare and Medicaid funds fraudulently. Further behind the scenes is another largely unknown story of Intermediary, Carrier, Contractor, and State case investigations which have denied, reduced, or recaptured mil-

lions of Program dollars. It is one which the general public knows little about, and yet one which reflects our continuing concern with obtaining fair and equitable medical care for the Federal and State tax dollars invested in these increasingly complex programs.

Improved tools have also been developed in the form of upgraded penalties for fraudulent acts in both programs contained in the Anti-Fraud and Abuse Amendments enacted last year, and by the continuing improvement of computer detection and screening systems for the enormous volumes of claims flowing through the Medicare and Medicaid Programs. Other panel members will discuss the aspect of Program fraud and I will cover what is often the beginning of the whole process—overutilization and abuse detection.

Computer analysis and screening techniques for various medical services have existed for a number of years in comparatively low volume processing environments. Recognizing the need for high capacity claims processing and management systems, HEW has fostered the long range development of the Model Systems concept which has resulted in several integrated claims processing systems.

Under Medicare, the claim processing concepts are known as the Model A and Model B Systems and in Medicaid the system is known as MMIS or Medicaid Management Information System. Built into the Model B System are pre and post-payment modules which trigger the initial case rejection or begin the careful accumulation of abnormal or unusual patient care statistics in a medical practice. MMIS uses similar techniques.

Before detailing the measures, frequencies and meaningful utilization ratios produced by the respective computer systems, I want to touch upon the basic problem of Program abuse. In its simplest form, abuse represents the provision of services and supplies in excess of those which are considered medically necessary. In my view and experience, abuse has different characteristics and patterns in each Program with only a few similarities. The most common form of abuse in either Program is overutilization of services. Overutilization is a profound subject in itself and a difficult one to resolve. In attempting to have ten health care providers define it, you may get ten answers. Control measures include not only pre and post-payment controls but, also, provider and patient education, law and regulation. Doctors will differ strongly on what they consider overutilization of services. It may depend upon the setting, age, care, availability of services, and many other variables. Its definition

under Medicare can justifiably differ from the yardstick applied to the Medicaid patient. The "cure" in an individual case of overutilization, presuming the absence of fraud, may be worse than the "problem." If the physician is in an underserved area, which is commonly the case in Medicaid, punitive actions resulting in his removal from the area could result in a less personal type of service being rendered at a higher cost to the State. These former patients may seek treatment in the hospital setting at greatly increased Program cost. In many cases, there are significant differences in overutilization factors between the Programs. In Medicare, the problem may be that the patient is receiving very high quality care, perhaps at a higher level than envisioned by the law. Since Medicaid reimbursement per service is generally much lower, it leads in some cases to a different type of overutilization phenomena. Abuse characteristics present in Medicaid data include:

1. Low average time spent with patients per day.
2. Family visits. All members are examined at each doctor visit whether necessary or not.
3. Ping-ponging. High frequency doctor referrals within a group or between other specialists on Program patients.
4. Consecutive daily visits with no appointments.
5. Services rendered which are not related to the physician's specialty.
6. Symptoms rather than diagnoses are submitted on a claim.
7. A variety of diagnoses are given varying from visit to visit on the same patient.
8. A pattern of seeing more than one physician on the same date.
9. A doctor with an unusual number of teenage patients.

Medicare characteristics are generally different and tend to reflect the financial restraints imposed by the deductible and coinsurance payment features built into this Program. Medicare data reveal more abuse in the hospital setting in terms of excessive stays and billings for daily and concurrent specialty care. Some problems also exist in the office and the Nursing Home setting with little or no documentation to support high frequency and acute care visits.

Overutilization is a highly sensitive issue and one which administrative edicts will not resolve and one where the wrong edicts can negatively affect the entire health care delivery system. As always, there is a fine line between overutilization

and abuse which requires the use of human judgment, an element which is necessarily missing in all the massive arrays of computer data.

How do we pull together the telltale clues which are now difficult for the individual case reviewer to associate when manually reviewing recipient and beneficiary case files? Old approaches and methods of review can no longer work in this environment. The streams of high volume data detailing dates of service, diagnoses, procedures and types and places of service must be categorized and organized into a meaningful format. As more claims data is fed into computer networks, data management techniques become important and must furnish an environment in which both the individual patient activity and provider or physician treatment patterns can be more adequately monitored. Computer studies can cover practice patterns over both short and long periods of time and permit the selection of unique or exceptional variations in the delivery of services within areas or peer groups.

In the Model B Medicare System, both pre and post-payment screens are used as devices to control the utilization of services. Some of the commonly used pre-payment screens are:

Provider Flags—These can be broad enough in scope to include all claims submitted by a physician or they can be tailored to select only certain procedures. They are usually inserted into the monitoring system as a by-product of individual claims referred by the claims processing staff which appear to be suspicious, or as a result of unusual billings. They can also stem from wider post-payment investigations of claims which indicate a need to continue monitoring for unusual procedures or they may be derived from previous post-payment reviews which show a need to reduce or stop payment for certain types of excessive medical services.

Duplicate Bills—Every system encounters bills which have previously been paid. Because they may be submitted intentionally or accidentally in combination with recent unpaid services, they need to be carefully separated after the computer screens detect the duplicate service. Incorrect separation of these charges can allow duplicate payments to be paid by the system.

Concurrent Care—This situation occurs most frequently in the hospital where the seriousness of the illness may have required several different specialties to contribute to the care of the patient. Again, the condition as revealed by hospital records may not have been that severe and over-utilization of services exists and must be denied. Consistent and repeated cases of unnecessary concurrent care can lead to further case investi-

gations at this or other hospitals where a physician practices.

Model pre-payment screens provide great flexibility in the application of both quantitative and time measures of service utilization. For example, using time measures of one month and three months, follow-up Nursing Home visits are held to one per month and no more than three in three months. These are the current program limitations for this service, which have generally been accepted. Claims exceeding these parameters either lead to denial or payment after investigation with subsequent education of the physician's staff in the use of the correct descriptive terminology for acute episodes of Nursing Home care. Routine Hospital Out-Patient visits exceeding certain frequencies per month or quarter are automatically screened for further analysis. Services which are being closely reviewed such as Pacemaker check-ups and Telephonic Pacemaker Monitoring are set at "0" to provide more control over these services. The procedures listed in the pre-payment screen can be changed and time periods to be reviewed can be altered to adapt to changing claim conditions. New procedures and techniques of treatment may emerge which require revised time intervals or treatment frequencies. Pre-payment screens must be used efficiently to obtain the greatest benefit since indiscriminate use can often delay payments on legitimate claims. Some ten options are available for screening under the Model System which enable carriers to adapt those which best fit the practice patterns in their area and those which produce a significant number of claim and dollar reductions in payment.

Working in conjunction with this form of utilization screen is the PARE (Payment Review) system which has been in use for a number of years. It reviews provider payments with earnings above a predetermined amount and, where excess services have been generated above medically acceptable norms, a repayment of Program funds is generated. Some 20 carriers are now using, on a pilot basis, a newer Post Payment Utilization System. It has basically four objectives:

1. To monitor the Medicare claims experience of all providers in the Carrier's service area and to acquire statistical data on them and their specialty groups.
2. To identify those physicians by locality and specialty whose utilization patterns differ from medically recognized norms. These are established by calculating basic patient to service ratios for the provider and are compared to those of his specialty group.

3. To correct any program abuse or overutilization of provider services by recovering overpayments.
4. To prevent further abuse in the utilization of services by educating providers in the acceptable norms of practice.

The system calculates for each provider the percentage of deviation from the patterns established by the specialty group in his area and are compared as follows:

1. The percentage of total patients receiving each type of service
2. The average charge per patient
3. The average number of services per patient.

All providers displaying one or more ratios exceeding those established by their peers are selected for closer investigation. The Carrier has the ability to select against some 16 service categories ranging from services in the Office, Home, Hospital, SNF and Nursing Home to injections, EKG's, surgery and laboratory services.

At this point the system has produced indications of abnormal patterns which must be tested. This is where claim review experience is essential to developing the facts to support or explain the abnormalities. Patient claims are selected from a physician's practice and charting of their services begins. Copies of records are requested including any associated hospital and nursing home charts. Members of our Professional Relations Staff assist by visiting institutions to obtain information on the spot. Where the medical facts do not appear to support the frequency of services, cross-checks are also made to see that provider documentation supports the services billed to the Program. The emerging picture supported by worksheets, claims, charts, claim histories and copies of actual records are studied by members of our Medical Staff who may request further information. They may also refer the case file to one of our outside advisors for their opinion on what appears to be abnormal practices within the specialty. In New Jersey alone, we retain a panel of 92 privately practicing physicians to assist with this and other practice questions which arise in the processing of Medicare claims. It is very difficult for a physician to refute a review by someone active and knowledgeable in his specialty. The Advisor's opinion will help to confirm or allay our suspicions of over or misutilization of services and will frequently provide us with medical guidelines for the control of future abuse. Using these assessments and profiles of patients in the doc-

tor's practice, an overpayment assessment can be made by the Utilization Reviewer.

Where cases of suspected fraud are uncovered, the physician case is turned over to the Regional Office Program Integrity staff for direction. Additional claim profiles and histories confirming earlier findings may be requested to more fully document and confirm the fraudulent practice. The Regional staff may also undertake beneficiary interviews and ultimately some of these cases will culminate in the fraud prosecutions mentioned earlier.

As you can see, abuse detection is greatly aided by the screening, checking and cross-referencing abilities of computer systems. Human experience and claim judgment are also basic to the process plus many hours of painstaking data comparisons before an overpayment assessment or suspected fraud case can be brought to an effective conclusion.

In recent years, the attractiveness of enhanced Federal funding for improved Medicaid claims processing systems has led to the development of the MMIS System. With 90/10 funding available for development and a 75/25 match for operations, it has been an inducement to upgrade many State systems. With the combination of Medicaid and Medicare operations under the Health Care Financing Administration, many of the described utilization review techniques resident in Medicare Programs should become available to Medicaid contractors and State personnel. Claim volume is even greater in Medicaid along with a wider range of ages and types of medical coverage. It, therefore, provides more opportunities for abuse to remain undetected if the full capacities of computer monitoring coupled with experienced staff analyses are not used.

In its present form, MMIS makes use of five basic files:

1. *Recipient*—This is used to control and update Medicaid eligibility.
2. *Provider*—Controls provider certification status and eligibility to participate.
3. *Claims Processing*—Processes and records provider payment transactions.
4. *MARS*—Management statistical file showing usage of services.
5. *SURS*—Identifies potential overutilization.

Let me expand upon these last two files, MARS or Management And Review Sub-System) furnishes essential management information about the number of eligible recipients for a period, dollars disbursed, number of claims processed and errors detected. It can also supply, as part

of its information network, budgetary and systems operations reports. Other fiscal and program status reports are available listing expenditures classified for each type of provider and recipient. It assists in the statistical documentation of services in an operating Medicaid system.

SURS or the (Surveillance and Utilization Review Sub-system) is the Medicaid equivalent of the claim screening system just described for Medicare. Depending upon individual State operating preferences, output from the system may be developed by experienced contractor personnel or by an equivalent staff of trained State personnel.

The MMIS System is gradually being adopted and along with other upgraded and certified State systems they will expand upon existing surveillance and utilization review activities. Abuse control is necessary if recipients are to receive essential services and State and Federal taxpayers are to obtain a maximum return for their tax dollars which support the Program.

To add emphasis and urgency to the need for obtaining more prosecutions in Medicaid, the Congress enacted the Medicare and Medicaid Anti-Fraud and Abuse Amendments last year. A section in the bill made provision for the creation of separate Medicaid Fraud Control Units under the Attorney General with, again, the financial incentive of 90/10 matching. Several States have already acted upon this provision and, coupled with other leads developed by surveillance systems, we should begin to see a greater flow of Medicaid prosecutions.

Contained in this same bill were amendments to previous PSRO or Professional Standards Review Organization legislation. This peer review mechanism has been gathering strength and in many States has contracted for the review of hospital services. Binding reviews of hospital stays are being made with data developed by separate PSRO data systems. It provides another means for reviewing lengths of stay and ancillary services in the institutional setting. Growing concern over hospital costs and the need to reduce the rate of growth in per diem charges will draw increased attention to PSRO activities on behalf of both Programs.

I mentioned earlier the millions of dollars which are presently being denied by Carriers, Intermediaries and Contractors through systems of abuse detection and control. In a small way, I think our Prudential experience illustrates the national potential for control of Medicare and Medicaid abuse. Our responsibilities include New Jersey, North Carolina and Georgia Medicare Part B, a portion of Part A in New Jersey and New Jersey Medicaid noninstitutional services excluding drugs. We share the contracting role for Medicaid institutional service with New Jersey Blue Cross. In the fiscal year of 1978 just completed, we denied $2,500,000 for excessive stays in our portion of New Jersey Part A hospitals. Part B denials for overutilization in our three states were almost $8,000,000 and denials on Medicaid institutional and non-institutional claims were $1,250,000.

I have touched in some detail upon the problems of utilization control, its complexities and conflicting applications in each Program. Abuse can be detected and screened even in claims processing systems of this magnitude discussed, by the use of tested data management and statistical techniques coupled with the judgment and accumulated experience of claims personnel. Further refinement of the Model Systems concept and application of stronger peer review mechanisms will produce even greater control by the Federal and State Governments in the future management of the Medicare and Medicaid Programs. I believe it is perfectly feasible and practical to assure high quality care for participants while reducing or eliminating the problems of Program abuse through the use of the data techniques described.

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REMARKS—"ADMINISTRATIVE REMEDIES"

By Paul M. Allen, *Deputy Director for Medical Services Administration, Michigan Department of Social Services*

I was most flattered when asked to speak at this meeting but must admit my ego was deflated somewhat when I learned the subject of my participation concerned the use of administrative remedies in controlling abuse in the Medicaid program. Frankly in my experience in applying administrative remedies I have considered the sensation to be a series of ups and downs akin to riding a roller coaster. Before I explore the subject further let me digress a bit and describe briefly the scope of the Michigan Medicaid program and outline our approach to controlling fraud, abuse and errors.

The Medicaid Program in Michigan, as is the case in many other states, is the single largest state program in terms of allocation of funding, representing some 12% of the total State budget in the current fiscal year. Michigan's program alone accounts for about 5% of total Federal funds appropriated for Medicaid. Since the beginning of Michigan's program in 1966, expenditures for medical services have increased from $67 million to a projected expenditure of nearly $950 million for the fiscal year which began on October 1, 1978. The program provides services to some 900,000 eligible individuals or nearly 10% of the State's population. The Michigan program is one of the nation's most liberal in terms of the scope of benefits provided. We have enrolled over 26,000 individual providers, representing nearly every field of medical service to make these benefits readily available. These providers submit to the Department of Social Services an average of over 75,000 bills representing some 140,000 services every working day of the year. Because the state is its own fiscal agent, observation and evaluation of the management processes of a program of this magnitude represent a microcosm of national health issues, initiatives and problems.

As most of you are aware there are many conflicting pressures brought to bear on any public program. However, because of the many disciplines within the health services professions, all of which impact on the life of the affected beneficiaries, these conflicting pressures are more numerous in public health programs than in any other government program area. To say the least, this makes Medicaid administration difficult and, more importantly, Medicaid management practices more difficult to implement and evaluate in a consistent and understandable way.

Regardless of the myriad of administrative complexities there are two significant but opposing forces at work in the management of the Medicaid program. On the one hand, it is crucial that we review, adjudicate and pay claims in a timely and equitable manner. If we don't we will not be able to obtain the participation of health services providers. Without their participation we deny the indigent, particularly aged and children, access to the mainstream of quality health care. On the other hand, since we are spending in excess of $2 million a day in public funds, it is essential that all claims are carefully scrutinized to ensure that they are valid and proper and that the possibility of program abuse is minimized.

This dilemma, the conflict between the need to keep provider participation at a maximum while intensifying efforts to eliminate inappropriate payments, is common to all State Medicaid programs. We believe that Michigan's approach to the management of the program and particularly to the detection of potential fraud and abuse represents one of the most effective systems among state programs for resolving those conflicts.

To accomplish our objectives we have been using the Medicaid Management Information System (MMIS). The system uses state of the art data entry and data processing techniques to rapidly and accurately process the seemingly overwhelming volume of paper received daily. Our average turnaround time for a request for payment for services provided under the program is 14.6 days. That is the average time it takes us from the date of receipt in our mail room to the date of payment for all 75,000 bills received daily including those pended for any of a variety of reasons. This rapid payment cycle contributes significantly to the high level of acceptance of the program by providers in Michigan. While insuring rapid payment, this advanced data processing system and its complementary selective manual review processes allows us to quickly validate obligations prior to payment and provides the mechanisms and information necessary for post-payment review and analysis. The claim payment system contains nearly 400 checks or edits which, among other things, at the "front end" of the process, validate claim data, verify provider and recipient eligibility, determine proper levels of payment and, critically from an abuse determination point of view, compare current values to those previously submitted, within defined parameters, to prevent duplicate billings and provide indications of possible over-utilization or abuse. At the "backend" of the process, on a post payment basis, the Surveillance and Utilization Review (SUR) subsystem of the Medicaid Management Information System aggregates claim information, on a provider or recipient basis, from historical data over a longer term, usually 3 to 15 months. Through manipulation of the aggregated data the SUR system produces profiles of utilization for providers and beneficiaries. Through review of these profiles, health care professionals and analysts, assist in detecting possibly abusive or fraudulent practices and provide evaluations of allegations of such practices originating from other sources. It is the ready availability of this information combined with an effective organization of investigators and medical professionals which makes Michigan's program integrity system a productive unified effort.

To digress further, Michigan's MA program was implemented rapidly in 1966 when Title XIX of the Social Security Act was enacted. As such, it was not immediately possible to fully develop

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the sophisticated systems essential for program management and control. In fact, it was not generally recognized at that time, that the program would grow as rapidly as has been the case and become such a major force in the allocation and expenditure of state resources. By 1971, however, the Executive and Legislative branches of State government recognized that the existing system, operated through a contracted fiscal intermediary, did not provide the control mechanisms or the information required for effective management. Accordingly, the Legislature and Governor approved financing for the design of a modern Medicaid Management Information System and the State, in 1972, decided to become its own fiscal agent, assigning the administration of the new Medicaid system to the Medical Services Administration (then the Bureau of Medical Assistance) of the Department of Social Services. As an aside, many of the processes developed in Michigan, served as the prototype for that which ultimately was adopted by the Department of HEW as a national MMIS.

I provide this bit of historical perspective to show that there was early concern in Michigan over the direction the Medicaid program was taking and a mutual commitment of the branches of State government to take early remedial action to tighten program control. The inclusion of fraud and abuse detection and prevention systems in these early efforts (Michigan was one of the first states to undertake a large scale coordinated program integrity effort) was instrumental in preventing the occurrence of many of the abusive practices which are evident in other programs and has given us several years of experience in developing and refining program integrity processes.

The current Medicaid Program integrity efforts in Michigan represent a cooperative system involving the Department of the Attorney General, the Office of the Inspector General (OIG), the Medicaid Recovery Division and the Health Services Review Bureau (the latter three units within the Department of Social Services). Although each of these units has a defined responsibility for a portion of the problem, they are in constant communication and coordinate activities through regular review meetings using as their common data base the outputs of MMIS. The Attorney General is charged with the investigation and prosecution of Medicaid provider fraud pursuant to the provisions of PL 95-142, while the OIG within Social Services has parallel responsibility for allegations of recipient fraud. The Medicaid Recovery Division of Medical Services Administration is responsible for the investi-

gation and resolution of all cases involving program abuse, that is, those cases which do not warrant prosecution on a criminal basis. The Health Services Review Bureau of the Medical Services Administration is responsible for the professional evaluation of health care data generated by the system. Since the information on potentially fraudulent or abusive situations may come from a variety of sources, the Medicaid Recovery unit acts as a focal point for the entry of these cases into the system and for tracking the status of cases in process.

Allegations may originate from a number of sources. Individuals, providers or other agencies may report suspicions of inappropriate practice, either by provider or recipient. Management reports generated on a regular basis from the claims processing system provide information on unusual billing or utilization patterns. The SUR system develops information on longer term patterns of practice or utilization which deviate from preestablished parameters based on "normal" utilization or practice.

Once each week, a review committee meets to review all potential cases. Those with obvious indication of possible fraud are immediately referred to the Attorney General for further action. Even so, all cases are subject to initial review for fraud by the Attorney General. Those with potential are retained by the Attorney General while others are returned to the Medicaid Recovery unit for investigation. Any case may be re-referred to the Attorney General whenever developments might indicate the existence of fradulent practices. Since we are primarily concerned here with the treatment of cases of abuse which do not seen suitable for criminal prosecution, I intend to emphasize the resolution of these cases in the remainder of this presentation.

All cases accepted by the Medicaid Recovery unit are referred to the Bureau of Health Services Review (the SUR unit). There, comprehensive profiles of historical practices are generated and analyzed through desk audit by a staff of health care analysts and medical professionals. Following analysis a memorandum of findings is prepared which recommends appropriate action on each case. These actions generally fall into two categories: Corrective Action or Field Audit.

Once each week, a Sample Review Committee meets to develop a sample design for each case. This design represents a statistically determined sample of paid claims pertinent to the case, upon which further investigation and calculations of any refunds due the program are based. If obvious overpayments are evident, for instance from duplicate billings, then recovery is initiated at

once. In any event, as indicated previously, all such cases are referred to the Attorney General for evaluation and, if fraud still is not evident, returned to the Medicaid Recovery unit for further administrative action as may be appropriate.

In those cases where corrective action is indicated, an overpayment amount is calculated, contact is made with the provider, and the repayment process is effected. These cases are those which primarily involve billing errors or misunderstandings of program policy. Upon completion of recovery activity, these cases are referred to the program's provider relations unit which contacts the provider involved either thru letter, phone or a staff of field representatives to explain the problems encountered and to discuss changes in billing procedures necessary to prevent their reoccurrence.

In the more flagrant cases where large sums of money may be involved a field audit is conducted by the Medicaid Recovery unit. This is done by pulling a sample of paid claims as determined by the sample review committee. Field staff then make a visit to the provider's place of business and obtain copies of medical records and documentation supporting these claims. This information is then returned to the medical and analytical staff of the SUR unit, along with any explanatory reports or other information available and pertinent, for evaluation. This evaluation may, at this point, involve review by professional peer groups or by contracted medical consultants as appropriate.

The results of this evaluation are returned to the Medicaid Recovery unit. If the evaluation indicates that the practice observed is, in fact, legitimate, the provider is notified and the case is closed. If, however, aberrant practices are confirmed an overpayment amount is calculated and communicated to the provider with findings. If the provider concurs, a reimbursement agreement is executed and the case is closed. Note that prior to closing any case, the Attorney General is informed. If the Attorney General objects for any reason, i.e. the case may be under review there, the case is held in suspense. If the provider disagrees with any of the findings or on the amount of refund due, the process continues through a system of informal conferences, to administrative hearings procedures and to court if necessary until the issue is resolved.

As discussed earlier, the sophistication of Michigan's payment system with its series of automated edits and the existence, for several years, of an active program of intensive postpayment analysis have discouraged many abusive practices. Our system has been the subject of

several reviews. In 1974, the General Accounting Office reviewed our payment system and procedures for curbing fraud and abuse, and called it the best system they had seen. In 1976, the Subcommittee on Long Term Care of the U. S. Senate Special Commission on Aging concluded that "In (Michigan), some abuses still exist, but blatant wholesale thefts are not as evident (as in other states) reflecting what appears to be a serious effort to root out fraud and abuse". Finally in a report released in August of 1978 an HEW Fraud and Abuse Management Assessment team concluded: "Many of the State's methods and procedures for detecting and preventing fraud and abuse are of such high caliber that they only need to be considered in terms of refinements while others need to be strengthened to improve the overall quality of the Program."

In spite of these successes the program is not without its difficulties. Our initial efforts in this area produced a large return on a relatively small investment in staff and supporting resources. However, as our administrative efforts increased, a curious phenomenon occurred . . . our recoveries actually declined. This can be attributed, I believe, to several factors. First, our early efforts were effective in detecting and eliminating obvious offenders. As knowledge of these efforts became known among the provider community some providers, most certainly, ceased questionable practices. It was not uncommon, in fact, during the early days of this program for providers to mail unsolicited refunds to our recovery unit on the basis of self-discovered billing "errors." Thus the "easy money" dried up.

Second, the increasing experience and sophistication of program efforts were accompanied by a corresponding increase in the sophistication of providers. That is, provider knowledge of program policies, rules and regulations increased to the point that those inclined to abuse the program utilized much more subtle means (and still do) — means which are more difficult to detect and which are more difficult to prove and resolve when detected.

A third factor bearing on this situation is a shift in emphasis from the detection and recovery of inappropriately claimed funds through administrative processes to an emphasis on investigation of fraud and prosecution. This immediately increased the time frames involved in resolving cases and the complexity of the proceedings surrounding them as well as the legal maneuverings of the providers involved.

Another problem area has occurred: As the confrontation between program and provider becomes more sophisticated, it becomes more diffi-

cult to differentiate between fraud and abuse, as perceived by the program, and the provider's interpretation of legitimate medical practice as reflected in the provision of services, which in his professional judgement are necessary. In this area, it becomes obvious that the statement that the practice of medicine is as much an art as a science is not just another cliche. Michigan has achieved some success in interpreting this area through the use of Peer Review Committees and independent professional evaluation. However, I would be less than candid if I told you that our performance in these gray areas was acceptable to us as administrators. As a case in point, in 1975 the Michigan program identified, through post-payment review, a physician in the Detroit area who consistently billed the program for large daily numbers of home visits. The physician, in fact, billed for services provided to 149 individuals during home visits in one day and over a period of several weeks oftentimes averaged 100 a day. Investigations showed that the physician had no established office, but had an answering service which took calls and scheduled visits, and that he operated from his car. He visited inner city housing projects seeing several recipients, usually all members of the same family, at each stop. The physician billed for a limited number of diagnoses, providing similar services to each patient, and billed the program for the full cost of a home visit for each. After completion of our investigation and discussions with the physician, during which he insisted his practice was appropriate and service adequate, a request for peer review was made to the appropriate state professional association. The physician's peers, including one of our staff doctors, accompanied him on his rounds, and reported that he did indeed see the patients and provide the services reported and that, although the peer group did not necessarily concur with his mode of practice, they were not willing to pronounce it illegitimate or even inadequate.

As a result, the physician's claims were paid. The program did, however, after this incident modify its reimbursement policy to limit payment for services provided to multiple recipients in a single home visit. Similar situations have risen.

This case serves to illustrate the extreme difficulty of making administrative or professional determinations of medical necessity or quality of care. Such cases, if pursued to their conclusion, are likely to end up being decided by the courts on a case by case basis.

The difficulties of administratively applying sanctions to a provider's licensing or certification status or to his program enrollment status are another problem in this process. Ideally, health care providers found to be in substantive violation of program policies should be subject to effective sanctions. Existing federal and state law and regulation and the ineffectiveness of procedures for accomplishing these sanctions often make the application of this option prohibitively difficult or impossible. Proposed changes in Michigan law and recently promulgated federal regulations on program participation will alleviate this problem to some extent. However, bringing these sanctions to their full deterrent potential, except in cases of the most obvious fraudulent intent, remains a fruitful area for further development, particularly in view of the complex linking of this option with issues of quality of care and of acceptable medical practices. In this regard we are of the opinion that the federal government would be well advised to establish a task force to develop the additional, realistic administrative sanctions that Medicaid and Medicare managers need to more effectively discharge their responsibilities.

In spite of the difficulties in resolving these issues, the existence of a coordinated, comprehensive and aggressive program of fraud and abuse detection and prevention can both directly and indirectly decrease the incidence of such practices.

Although it is virtually impossible to eliminate all opportunity for fraud and abuse in a program of the size and complexity of Medicaid we believe that the Michigan approach minimizes the opportunity for such practices. Although our reviews are extensive, we have avoided the alienation of providers and consequent refusal to provide services to beneficiaries by taking maximum advantage of state of the art data processing systems to ensure prompt, equitable and valid payment. The Michigan response to this problem, in effect, closes the loop. An important factor in the successes of the Medicaid program in Michigan, both from a programmatic point of view and in terms of minimizing fraud or abuse, has been the role of professional associations of providers. The Michigan program enjoys extremely good relationships with these associations and consults with them regularly on issues of program policy. The cooperation of the Michigan State Medical Society and the Michigan Association of Osteopathic Physicians, in particular, has contributed significantly from an administrative perspective to our fraud and abuse control efforts.

The proof of such practices remains a difficult and lengthy process. Administrative remedies may be hard to apply. Michigan's experience, however, indicates that in spite of the prevailing popular attitude to the contrary, it is possible to manage a publically funded program as large, expensive, and as complex as Medicaid with a minimum of fraud and abuse.

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REMARKS—"EXCESS CAPACITY AND OVERUTILIZATION OF SHORT TERM HOSPITALS IN THE UNITED STATES"

By William H. Stewart, M.D., *Acting Head, Department of Preventive Medicine and Public Health, Louisiana State University School of Medicine*

Public Law 93–641 mandates the Secretary of Health, Education, and Welfare to issue a series of planning guides for the use of Health Systems Agencies as they develop the health services plans for their service areas. Among the standards issued by the Secretary is a maximum of four acute care hospital beds per 1,000 persons at a level of 80 per cent occupancy, and a series of standards for utilization of certain specific types of hospital beds. The latter begin to form a rationale for the efficient use of the hospital beds in a service area.

The determination by the Secretary that there is considerable excess of acute general hospital beds in the country and that there is inefficient and wasteful use of some beds is a very significant and extremely important finding. It signals a major national policy shift in the health care field. For the past several decades, the policy has been that a more equitable distribution of health services could be accomplished by greatly increasing the resources available in the country. Most effort was directed into getting more physicians, dentists and nurses, more facilities, particularly hospitals, and more purchasing power for consumers. Now the policy rests on the premise, that with few exceptions, the nation has enough resources. The new policy goal is a more equitable distribution and efficient use of existing resources through a much more structured system of allocation of resources and a more rational utilization of those resources. The lack of this rationale leads to charges of overutilization, misutilization, inefficiency and waste in the provision of acute hospital care services. Attempts to reduce overutilization of hospitals case by case and hospital by hospital, through utilization review and the activities of PSRO's, may have some success in reducing the more gross patterns of overutilization. But it will have little effect on eliminating or modifying the basic forces in the communities and in the nation which are the principle architects of the excess bed capacity and sometime irrational utilization pattern of the short term general hospitals.

It is the purpose of this paper to examine some of the impediments to accomplishment of the planning goals of the Secretary including identification of some of the basic problems in the health care system which cause excess hospital capacity and overutilization of hospital services.

The determination that there is excess capacity in the acute general hospitals and that proper and more rational utilization of less beds would lead to considerable savings in total hospital expenditures is based on interpretation of national hospital data tempered by specific studies of hospital utilization in varying populations in more delimited geographic settings.

It is beyond the scope of this paper to review the extensive literature on hospital capacity and hospital utilization of short-term hospitals in the United States. The number of short-term hospital beds per 1000 persons has increased steadily over the past several decades. Of particular note is the fact that the expansion of these hospitals has not been accomplished by putting into place more of the same beds that existed in 1960. In terms of personnel required to provide hospital services per bed and the hospital assets required to provide those services, a bed in 1978 is not the same bed of 1960. The capital outlay and the number of high skilled personnel required per bed has greatly expanded since 1960 and it shows no signs of abating.

Not only has the intensity of care provided per bed been rising since 1960, the use of the beds has also increased. In 1960 there were 966 patient days per 1000 persons in acute general hospitals. In 1976 this rate stood at 1262.

The Institute of Medicine of the National Academy of Sciences in a policy statement entitled *Controlling the Supply of Hospital Beds* concluded after extensively reviewing the national data on hospital bed supply: "Although the accuracy of various aggregate national estimates of hospital bed surpluses is debatable, the evidence clearly indicates that significant surpluses of short-term general hospital beds exist or are developing in many areas of the United

States and that these are contributing significantly to rising hospital care costs." They went on to recommend "a national planning goal be established to achieve an overall reduction of at least 10 percent in the ratio of short-term general hospital beds to the population within the next five years."

There is strong evidence to support the determination by the Secretary that significant surpluses of hospital beds exist. However, implementation of a national program to delete the excess beds from the acute general hospitals and to rationalize the use of the leaner hospital capacity will be difficult. It will require across the country decision-making and action by countless numbers of state and local decision-making bodies, both governmental and non-governmental, including the more than seven thousand acute general hospitals.

One of the major impediments to a reduction of the acute hospital capacity is the difficulty of answering the question: How will it be determined, hospital by hospital, which specific beds are in excess and should be abolished? While it is possible to arrive at some total number of beds in a community or health service area and it is possible to roughly divide those beds into general purpose and special purpose beds and to measure their utilization over time, such data, diligently collected by the Health Systems Agency, will not determine, hospital by hospital, which specific beds are in excess and should be abolished. And it is very doubtful that any hospital will volunteer to abolish itself or cut back on its bed capacity.

Hospitals are independent institutions. Each hospital in a community has a history and tradition of service which strongly influences the amount and types of services provided by that hospital. The Board of Trustees and medical staff of the hospital are perpetuators of that history and tradition of service. These are not easily discontinued or transferred to another hospital in some other location in the community.

Each hospital has its own medical staff. It is the medical staff which determines the use of the beds of a hospital. The availability of beds and supporting technical and nursing services in that hospital are essential for the conduct of the practice of each member of the staff for his livelihood. It would be unusual for a physician to consider the resources he uses at his hospital for the care of his patient as shareable with other similar hospital resources in the community.

Some hospitals have developed cooperative arrangements to increase their efficiency. In some communities, there has been a trend toward merging of hospitals to better control costs, and there are indications these trends are increasing.

However, the majority of hospitals in any given service area are in competition with one another on the revenue side of the ledger. A good hospital administrator, having received a chorus of complaints from the medical staff of lack of beds or lack of the latest diagnostic or therapeutic technology, will be before his Board with a capital outlay proposal at the earliest possible moment. And his justification will be based on the possible loss of key medical staff members in the face of the present inadequacies of his institution which could seriously jeopardize the revenue side of the hospital ledger.

Conversely, it is a good hospital administrator who will report to the medical staff at its monthly meeting his concern over the falling revenue of the hospital in the face of continuing or rising costs because the admission and occupancy rates have declined below a certain level.

There are few, if any, hospital service areas of the country where the hospitals of the area are considered by the physicians, board members, or public as parts of a common whole, to be shared equitably by all. In many instances, hospitals are identified with a neighborhood or a subcommunity within the larger community. In some instances they are the major employer of that area.

The application of a program to abolish excess beds in a community without the acceptance of the rational plan of closure of certain beds, and without the presence of clear cut authority by some decision-making body to make the decision that these beds are excess and those are not could lead to greater inequity than now exists. It could result in the designation of the hospital with the least power to resist closing or giving up beds without regard to the efficient and equitable provision of hospital services in an area. Or it could result in an agreement among hospitals to distribute the cut-back of excess beds by each hospital reducing its rated capacity by a small number of beds. This would not be only inconsistent with any objectively determined rationale for utilization of hospital resources in the area, it is highly likely to result in a decrease in the rated capacity of the hospital but an increase in the employees and hospital assets per bed of the remaining active beds. While the results would look nice in the aggregate statistics, the net savings would be minimal.

The identification of excess beds to be eliminated, hospital by hospital in a community without regard to variations in purchasing power is a method of rationing of resources in an important human services area in which there is little experience in communities. And once the identification has been carried out, an even more difficult issue arises. Who or what agency or institution at the level of the delivery of hospital services will have the responsibility and authority to close out, on a hospital by hospital basis, the approximately 100,000 short term hospital beds determined surplus.

Let assume a 100 bed hospital in Kansas City has been declared surplus and should be closed. Can the Secretary of Health, Education and Welfare order that hospital closed and the 250 or so employees dismissed? Or does the responsibility and authority rest with the Governor of Missouri? What role does the Kansas City government play in carrying out this decision? Or does the responsibility lie in the private sector—in the Health Systems Agency or in Blue Cross or Mutual of Omaha?

It is not clear at all who picks up the ball once the Secretary punts. The decision-making processes and powers of the health care system are diffuse and fragmented. This is not intended to be a pointing of the finger of failure at any one segment of the health care system. Rather it is intended to point out that the institutions, private and public, which have developed over the years to increase the purchasing power of the people for modern hospital and medical care and to develop the resources to be purchased are not organized for or charged with the responsibility and authority to ration the nation's health resources. Nor has the responsibility been assumed by State or local government, although many State governments have moved in that direction.

The Institute of Medicine pointed out that the decision-making processes in the health care industry virtually guarantee the wide-spread development of excess hospital bed capacity for short term general care. They further pointed out that the financing system under which the adverse consequences of over-expanded hospital bed supply are primarily felt not by the hospital but by the third party payors. The lack of awareness of hospital costs by physicians and patients at the time of delivery of health services vitiates an economic deterrent to excessive use of hospitals. Moreover, powerful community interests usually favor the building of a new hospital or expanding an existing one and oppose curtailment of services. No politician gets elected by appearing at hospital closing ceremonies.

A major national issue which impedes the implementation of a national policy to control the supply of hospital beds and rationalize their use is, therefore, the lack of any semblance of a social structure, area by area or community by community that clearly can be assigned the responsibility and authority to carry out the control measures and be held accountable for it. Nor

is there any clear notion the Federal government will relate to these local entities; through State government, through branch offices of the Federal government, through private entities under contract with the Federal government or through Fiscal Agents to name a few possibilities. At the present moment, it appears that many of the possibilities are operational in some area of the country. Also, State governments are attempting to institute various instruments to control the use of short term hospitals independent of the Federal government with varying degrees of reported success. At the moment it appears that the principal responsibility to carry out the national policy is left to each of the 7,000 hospitals —an impossible task for them to carry out.

Alan Gregg once used a recollection of a sign he saw in Tokyo to describe a similar situation. The sign read: "S. Maramuri & Company, Transfer Forwarding Agents. Your baggage sent in all directions." We simply do not now have the decision-making structure or processes at the regional and local area in the United States that can implement and carry out successfully a national program of controlling the acute hospital bed supply.

Another major impediment to the implementation of a policy to control the use of short term hospital beds in the nation is the fact that the pattern of use of the hospital in a neighborhood or community is shaped by many forces which are obscured and hidden by the use of averages from aggregate data.

For example, in the annual summary of *The Utilization of Short Stay Hospitals for 1976* published by the National Center for Health Statistics the average length of stay for all people who were discharged from a short stay hospital in 1976 was 7.6 days. While that figure is very useful in describing hospital use from a national standpoint, its usefulness on a local level is on a par with using mean annual temperatures for an unfamiliar area to decide what clothing you should take on a visit there.

When one examines hospital use by measuring patient days used by those individuals who stayed less than ten days in the hospital with those who stayed more than ten days, a different picture emerges. Calculations based on Table 3 of the 1976 report of the National Center for Health Statistics show that while only 20% of discharges from short term hospitals stayed longer than 10 days in the hospital, they accounted for about 52% of the patient days used by all hospitalized persons.

And who are these long stayers in the hospitals? As you would suspect, it is the older popula-

tion who are more likely to have a long term chronic illness. Using the population figures given in the same 1976 report, calculations from Table 3 show there were 2341 hospital days/1000 persons over 45 years of age and 626 hospital days/1000 persons under 45 years of age; just under 4 times more days for the older population than the younger one.

Most hospital use data for individual hospitals in a service area is not population based since hospitals do not have a definable population they serve. Some of the variation in hospital utilization in a service area depends on the variation in the characteristics of the population served by the physicians who are on the staff of the particular hospital. This will tend to obscure the meaning of *excess beds* when applied to any one hospital.

The data on the use of short term hospitals by age groups assume national importance when they are related to the population projections which are available for the next two decades. Significant growth is centered in the older age groups. Hence, given present hospital utilization patterns without the development of satisfactory alternatives to short term hospitalization, the demographic pressure will be to increase hospital use substantially.

There are many other forces in a community which shape hospital utilization. The financing system for hospital care, the method of reimbursement of hospital costs and the benefit structure of the health insurance prevalent in that community are strong incentives for hospitalization. As such they are disincentives to the development and use of alternatives to hospitalization which might be quite appropriate to the needs of the patient. The degree of cost uncertainty to the patient is much higher outside the hospital than in it. Moreover, the non-hospital based services are incompletely developed and scattered throughout the community, making use of them difficult for the patient and the physician. These limitations are aggravated for persons with chronic illness with some limitations in their usual functional capacity. And this group is bound to grow in the future as longevity in-

creases. Unless reasonable alternatives to hospitalization in short term general hospitals are developed which satisfy the requirements of the person in need of health services and the physician providing the services to meet that need, the pressure to increase hospitalization will continue.

In addition, accommodation must be made for the entire range of community based social services needed to enable the long term illness patient to cope with illness in lieu of prolonged hospitalization and to function with the least loss of independence. For the most part, these services are poorly understood, poorly financed, fragmented and of limited value to provide a satisfactory alternative to hospitalization or early discharge from the hospital.

It is not possible to visualize the implementation of a national plan for the rational use of acute general hospitals in this country without a major effort to develop and organize the health and social services into some kind of balanced whole at the level where services are received. There is no existing institution at that level, private or public, clearly charged with the responsibility to develop and organize the health and social services into some kind of balanced structure which permits the appropriate use of these services in meeting the health needs of the people in the most efficient manner.

If the national policy is adopted that health resources, health services and health related social services will be distributed and rationed on some basis other than purchasing power, and this appears to be the significance of the policy decision of the Secretary, then there will have to be developed an organization for the delivery of health services at the local level which recognizes the changing character of the health problems of the people, the need for organizational change in the delivery of health services, and the growing limitation of available financial resources. The lack of such an organization serves as one of the major impediments to implementation of a program to control the supply and use of acute hospital beds in the United States.

REMARKS—"FRAUD AND ABUSE ISSUES IN HOME HEALTH CARE"

By Judith LaVor, *Office of Policy, Planning, & Research, Health Care Financing Administration, DHEW*

The topic I was asked to address today is fraud and abuse among providers of home health services. In looking at the other topics being addressed in this session I realized that home health agencies are the only provider group addressed here, and that the other speakers are concerned with more generic subjects.

After having spoken to a few home health provider audiences in recent months, I am acutely aware of how sensitive these providers are about being singled out, about being accused of defrauding the public and about some of the controls that are belatedly being placed on HEW programs offering home health benefits. In fact, at a recent session in Houston one person informed me that if only 3 or 4 out of 2200 Medicare—certified home health agencies have been brought to prosecution, then the industry is ninety-nine and forty-four one-hundredths pure!

I think it is important to give some thoughts about why home health providers *have* been singled out today.

One reason is that they are the most recent provider group to come to our attention as having the same problems most other provider groups have. Congressional hearings and reports and a few flamboyant and flagrant practitioners of the art of fraud and abuse have brought home health agency problems to national attention in recent years.

Furthermore, home health expenditures, though still small in terms of total health care costs, have been growing quite rapidly, a fact that has only recently been noticed. Medicare expenditures for home health care have jumped from $80 million in FY 1973 to $425 million in FY 1977 and the number of persons served has exceeded half a million. Medicaid expenditures have doubled in the past three years to $179 million in FY 1977, and served over 200,000 people. The title XX program, a combination of social and health related services, adds another $450 million to in-home care expenditures, mostly for personal care and home-maker services. These increases in expenditures mean both higher visibility for the service and more chance for problems to occur.

We have had Congressional investigations and expenditure growth in other areas as well—nursing homes, clinics, doctors' offices and hospitals, so home health is not unique. Home health also

presents a few special problems that seem to worry us a little more. Services in the home are almost impossible to systematically scrutinize. The one-to-one relationship between the provider and a client who is ill, often vulnerable, often very old, and often alone, creates a special problem that doesn't exist in a group care setting.

The other problem goes back to the growth in expenditures; because these were such a minor part of the programs—for years only one percent of Medicare and one-tenth of one percent of Medicaid—the program administrators did not pay a lot of attention to regulations and guidelines on payments to home health agencies. We were unprepared for the growth in expenditures and the problems that went with it. We were not ready with program and reimbursement controls, guidelines to fiscal intermediaries or providers.

What do home health agencies look like? Medicare has certified over 2200 providers of skilled nursing services but who must also provide at least one other service such as physical or occupational therapy or home health aide service. Over half of these providers are official health agencies such as public health departments. One-fifth of all certified agencies are visiting nurse associations; 15 percent are private non-profit and less than 5 percent are proprietary. The number of proprietary agencies has been restricted by Medicare provisions, but many of the private non-profit agencies behave a great deal like them. Most agencies are relatively small, though there is a growth in chains, particularly of proprietary and private not for profits. Over half of the certified home health agencies employ fewer than four full-time equivalent nurses, and less than 10 percent employ ten or more.

Problems of HHA's

Home health agency investigations have revealed existence of many of the same fraudulent or abusive practices as in other provider areas—such as:

- billing for services not rendered
- misrepresentation of services
- altering or falsifying bills and records
- duplicate billings

- payroll and expense account padding
- improper allocation of costs

Over the past 9 years there have been very few prosecutions of home health agencies for fraud; only seven cases have to date been referred to the U.S. Attorney for prosecution. Guilty verdicts have been reached in only two cases, and the rest were either closed or settled out of court. However, with the creation of the Health Care Financing Administration's Office of Program Integrity and the Inspector General's Office, as well as with other increased authority granted by the Medicare-Medicaid Anti Fraud and Abuse Act, we expect to have increasingly effective investigations and prosecutions in this area.

In spite of the attention given to fraud and abuse in some flamboyant examples, many of the problems in home health care are more the result of opportunism than of fraud. Some providers have taken advantage of the relative lack of attention to home health providers as the Medicare and Medicaid programs dealt with more pressing, larger scale issues.

Since for many years home health services consumed only one percent of total Medicare expenditures, and one-tenth of one percent of Medicaid expenditures, home health services remained a little understood, little controlled benefit.

Our new analyses, as well as numerous Congressional hearings, have uncovered a number of problems in our programs that have permitted abusive practices. As I said earlier, much of the problem has been as much if not more a problem of opportunity seizing in the face of inadequate program controls.

Some home health providers have been able to receive excessive reimbursement of their costs. Our reimbursement policies have been vague and often the fiscal intermediaries in turn have not set specific limits on reasonableness or types of costs allowed. Excessive payments have been made for such items as salaries, fringe benefits, pensions and miscellaneous expenses.

Limits on costs have been hard to establish because we have no unified body of data from home health agencies. They have been allowed to compute their costs in five different ways. This has made comparisons among agencies or types of agencies impossible.

Lack of control over costs, limits on proprietary agencies, and some other factors have permitted the influx of the private not for profit home health agency. Some call it the proprietary not for profit. IRS non profit status is granted to a corporation which, instead of reporting profits, plows its excess income into large salaries, administrative staffs topheavy with relatives and cronies, high-living, and the like.

Home health agencies that serve only Medicare beneficiaries are also a problem. The private non profit agency is usually the one engaging in this practice, for it is advantageous to them to have virtually all their costs of doing business, and then some, returned through Medicare's reimbursement of total costs. What it means for the patients is that they will receive services until they exhaust their Medicare benefit, and then they are dropped. Private pay and Medicaid patients are not served at all. The voluntary agencies in the community are forced to absorb a large clientele unable to pay for their care but lose some of the balancing benefit of full-reimbursement Medicare clients.

One final problem that bears mentioning is the fact that with three different funding programs for home care, all with different criteria and standards, it has been possible for some unscrupulous switching. The title XX social services program pays for home care in some states to essentially the same population but with few or no standards. In at least a few cases, home care providers who have been barred from Medicare as a result of audit findings and exceptions have either declared bankruptcy and resurfaced as title XX providers or have simply switched their accounts from one program to the other. Agencies receiving payments from both sources have also been known to submit low bids to obtain local social services contracts and to recoup losses by over-billing Medicare.

In summary, creative enterprise has been possible in home health care.

Now that we recognize these problems, what are we going to do about them?

The Health Care Financing Administration has announced its intent to publish by the end of this year a notice of limits on overall home health costs under the authority granted by Section 223 of the 1972 Social Security Amendments. Included in new regulations will be limits on administrative costs and other areas.

To increase our ability to compare costs incurred by various providers, as well as to establish sound limits, we are using our authority under Section 19 of the Fraud and Abuse Act to establish and require common cost allocation and reporting procedures.

The Department has often stated its opposition to the concept of Medicare only providers, but the legal means of eliminating them are not yet available. However, we hope that by tightening up on what will be paid for, and by increasing our audit surveillance of these providers, we will be able to mitigate the problem.

During the past year we have examined these and other solutions to problems of home health care under Medicare, Medicaid, and Social Service programs. Other solutions we have identified as necessary to strengthen our administration of these programs include increased instructions to fiscal intermediaries, building increased intermediary capacity to review home health care claims by consolidating all Medicare home health reviews in a group of regional or area-wide intermediaries, and in improving Medicaid reimbursement policies.

The home health report that we are preparing for Congress also addresses standards, provider types, benefit packages, and eligibility criteria. Although fraud and abuse have been headline grabbers, there are many other issues, and a great many honest, high-quality providers of home health services. In fact, only a few pages out of a 100 page report deal specifically with fraud and abuse. Our task is to now establish an administrative structure that allows honest providers to serve people in need of care.

Summary of Discussion

Mr. Leonard D. Schaeffer opened the workshop and, in welcoming the panelists, described the challenge to the Department to ensure that monies alloted for providing health care to the poor, disabled and elderly are appropriately spent. He emphasized the need for correcting a growing public impression that the Federal government is poorly managing health care and other human resources programs, and noted the role of the Health Care Financing Administration (HCFA) in restoring the public's confidence. Since HCFA will spend over $40 billion this year financing health services, it is important that the Agency prove its ability to effectively manage those funds.

Some of the initiatives established by HCFA to better manage its programs by eliminating Medicare and Medicaid fraud, abuse, and waste discussed by Mr. Schaeffer were:

- Reduction of overpayments in the Medicare Program.
- Identification and elimination of erroneous payments due to ineligibility, third-party liability, and claims processing costs.
- Improved financial management in the Medicaid program.
- Improved management of the Professional Standards Review Organization (PSRO) program and effectiveness of PSRO's in reducing fraud, abuse, and waste.

Mr. Schaeffer concluded by stating that HCFA is also seeking long-range solutions to the problems of fraud, abuse, and error, so that appropriate, quality health services can be provided at an affordable cost. He reaffirmed HCFA's receptiveness to suggestions from interested parties, as the area of fraud, abuse, and waste will continue to be of high priority.

Charles J. Hynes, Director of the New York State Medicaid Fraud Unit, (prepared text on page 25) discussed the experiences in that State in identifying problems and seeking solutions in the health care delivery system. He emphasized that the real cost of quality health care is not known and called for the full participation of all citizens in curbing mounting inflation in health costs. Since fraud and mismanagement are hidden among the current costs of health care, long-term reforms in the health-delivery system are needed before the crisis will end. Mr. Hynes referred to H.R. 3, which was signed into law on October 25, 1977, and which provided the capacity to detect, prosecute, punish and thereby discourage fraud and abuse by health care providers by providing incentives for States to establish Medicaid Fraud Units. In New York State's Medicaid Fraud Unit a team approach, using auditors, investigators and lawyers, has been extremely successful. Moreover, criminal prosecution has been combined with an assertive recovery procedure for the return of money obtained through fraud. Mr. Hynes asserted that, as a result of several major investigations significant improvements have been made in health care in New York.

Mr. Hynes believes that 8-million Americans, including the elderly poor, need some form of national health insurance, but he pointed out that public officials proposing national health insurance need to direct attention to effective fraud, waste and management control. Significant information is available to aid in the formulation of a national health insurance program and to help determine the reasonable cost of health care.

William White, Vice President of the Prudential Insurance Company (Prepared text on page 28), directed his remarks to overutilization of health services and model systems for abuse detection and control. He referred to HEW's Model Systems concept which has produced several integrated claims processing systems. The Medicare systems are known as "Model A" and "Model B"; the Medicaid System is known as the "Medicaid Management Information System" (MMIS).

The most common abuse of Medicare and Medicare is overutilization of services; a difficult form of abuse to eliminate since health care providers

have different definitions of what constitutes overutilization. Physicians, for example, differ among themselves in defining "overutilization." Differences also exist in overutilization as defined by health programs managed by HEW. Data management techniques furnish an environment in which both patient and provider treatment patterns can be monitored. Computer studies permit the selection of unique or exceptional variations in the delivery of services within geographic areas or peer groups.

Some of the pre-payment screens used in the Model B Medicare System are:

- Provider flags
- Duplicate Bills
- Concurrent Care

In addition, some carriers are now using a Post Payment Utilization System which has the following objectives:

1. Monitor Medicare claims experience of all providers and acquire statistical data on them and their specialty groups.
2. Identify physicians by locality and specialty whose utilization patterns differ from medically recognized norms.
3. Correct program abuse or overutilization of services by recovering overpayments.
4. Educate providers to prevent further abuse.

Abuse detection is aided by screening, checking and cross-referenceing of computer systems.

The Medicaid Management Information System (MMIS) uses five basic files:

1. Recipient
2. Provider
3. Claims Processing
4. Medicare Acception Reporting System (MARS)—Shows usage of services.
5. Surveillance Utilization Review Systems (SURS)—Identifies possible overutilization

Abuse control aided by statistical analysis is necessary if beneficiaries are to receive quality care and essential services, and if taxpayers are to obtain maximum return for their dollars.

Paul Allen, Deputy Director for Medical Services Administration, Michigan, Department of Social Services, (Prepared text on page 32) discussed the Michigan Medicaid program's activities in controlling fraud, abuse and errors. Of the total Federal funds appropriated for Medicaid, five percent are used in Michigan, and the program provides services to ten percent of the State's population. All State Medicaid programs

have the same dilemma: keeping provider participation at a maximum while intensifying efforts to eliminate inappropriate payments.

Michigan has been using the Medicaid Management Information System (MMIS). The average payment time for services is 14.6 days and 75,000 bills are received daily. Key items in the improvement of administrative management include a systematized Medicaid management process, a reliance on automation, and the use of the State Department of Social Services as a fiscal agent to achieve equitable and rapid payment while controlling overpayments.

A review committee meets weekly to review potential fraud cases. Determinations of fraud are referred to the State Attorney General for action. If fraud is not evident, the case is referred to the Medicaid Recovery unit for further administrative action.

Mr. Allen concluded by indicating that Michigan's experience shows it is possible to manage the Medicaid program with a minimum of fraud and abuse. He further indicated that a desired outcome of the Secretary's National Conference would be a national effort to identify more effective administrative and legal remedies for the elimination of abuses.

Dr. William H. Stewart, Acting Head of the Department of Preventive Medicine and Public Health at the Louisiana State University School of Medicine, (prepared text on page 37) discussed excess capacity and overutilization of short-term general hospitals. He cited P.L. 93-641 and the regulations issued thereunder by the Secretary, which allow four acute care hospital beds per 1,000 persons at an 80 percent occupancy level, and provide standards for the utilization of certain types of hospital beds.

Determination by the Secretary that there is inefficient and wasteful use of some hospital beds is an important finding, and creates a new major national policy in the health field. In the past, the national policy was that more equitable distribution of health services could be accomplished by increasing available resources. The new goal is more equitable distribution of health resources through a much more structured system of allocating resources and more rational utilization of existing resources. Lack of this rationale leads to charges of overutilization, misutilization, inefficiency and waste in the provision of acute care hospital services.

Dr. Stewart pointed out that the number of short-term beds per 1,000 persons has increased over the past several decades. Moreover, the capital outlay, the number of skilled personnel required per bed, and the total use of beds have

greatly expanded since 1960.

Dr. Stewart concluded by asserting that it will be extremely difficult to delete excess beds from acute general hospitals. It will require action by State and local bodies, both governmental and nongovernmental, including the more than 7,000 acute general hospitals themselves.

Judith LaVor of the Office of Policy, Planning and Research, Health Care Financing Administration, (Prepared text on page 41) discussed issues of fraud and abuse with relation to providers of home health services. Many Home Health providers believe that they have been singled out as being abusive; thus, discussion of this issue was felt to be especially appropriate for the Conference.

Reimbursement for home health care has created some special problems. Services delivered in the patient's home are difficult to scrutinize. One-to-one relationships between providers and clients, who are often very old and alone, create special problems which are compounded by the increased rate of home health expenditures.

Medicare expenditures for home health care have risen from $80 million in 1973 to $425 million in 1977, and the number of patients served now exceeds half a million. Medicaid expenditures have doubled in three years to $179 million in 1977, and served over 200,000 people. Title XX, which provides for a combination of social and health related services, adds another $450 million to home care expenditures.

To date, only seven cases against home health providers have been referred for prosecution, and guilty verdicts have been returned in only two cases. The creation of the Office of Program Integrity in HCFA and the Inspector General's Office in HEW, and increased authority under the Medicare-Medicaid Anti-Fraud and Abuse Act, should lead to increasingly more numerous and and more effective investigations and prosecutions in this area.

Ms. LaVor concluded by stating that many of the current problems in home health care are the result of opportunism rather than fraud. With three different funding programs for home health care, unscrupulous switching of services for reporting purposes has been possible. As a result: 1) HCFA will issue new regulations under Section 223 of the 1972 Social Security Amendments by the end of this year which will limit reimbursement for home health costs; and 2) under Section 19 of the Medicare-Medicaid Anti-Fraud and Abuse Act, HCFA will establish and require common cost allocation and reporting procedures.

II. WELFARE WORKSHOP

Moderator

Stanford G. Ross
Commissioner of Social Security
HEW

Panelists

John T. Dempsey
Director
Michigan Department of Social Services

Blanche Bernstein
Administrator
Human Resources Administration
New York City

Samuel K. Skinner
Chairman, Illinois Fraud Prevention Commission

Kyle S. McKinsey
Deputy Director
California State Department of Social Services

Honorable Forrest Campbell
Chairman
Board of County Commissioners
Guilford County, North Carolina

Staff Reporters

Richard B. Harron
Social Insurance Policy Specialist
Welfare Reform Planning Group
HEW

Mike Rock
State Operations Specialist
Welfare Reform Planning Group
HEW

Welfare Workshop—Summary of Discussion

Mr. Ross welcomed the participants to the workshop and introduced the panelists. He then proceeded with an opening statement and pointed out that the Social Security Administration has now become the income security agency of the Federal Government with responsibility for the Retirement, Survivors, and Disability Insurance programs; the Supplemental Security Income (SSI) program; and the Aid to Families with Dependent Children (AFDC) program. In administering programs involving large amounts of funds, where even a slight error can result in a huge magnitude of misspent dollars, the challenge is to protect taxpayers and recipients by paying out the right amount—no more, no less. Mr. Ross stated that this workshop was convened to discuss and search for solutions to a major and unacceptable problem in SSI and AFDC: the 1.2 billion State and Federal tax dollars lost annually through incorrect and improper payments. Why are these funds being lost? The reasons are many and varied, including the complexity of the programs, and fraud

which robs the programs of public support and needed dollars. Most of the dollar losses are not the result of fraud; rather, they stem from inadequate program management at all levels of government. It is the impetus to improve management, Mr. Ross noted, that underlies the convening of this conference by Secretary Califano. While some of the changes necessary to program simplification will require legislation, Mr. Ross stated that the commitment and will of managers at all levels are critical factors in achieving improved efficiency and integrity in the income security programs.

John T. Dempsey, Director of the Michigan Department of Social Services, spoke of the progress that has been made in his State—a reduction in AFDC payment errors in Michigan in the last 4 years, from 16 percent to 7.9 percent. Even with this progress, however, 60-million dollars a year are still being misspent in Michigan. What are the causes of such error? One cause is human error; a program administered by people will never be perfect. Another

cause is the failure of government to actively prosecute those who cheat. In the few instances where prosecution has been vigorously and regularly pursued, it has had a deterrent effect. Yet another cause is the complexity of the AFDC program; the burden of this complexity is increased when one considers that numerous complicated programs are frequently administered by the same State agency. For example, huge increases in AFDC caseloads between 1965 and 1975, coupled with the addition of responsibility for administering the Food Stamp program has resulted in a 25-fold increase in workload in the Michigan Department of Social Services. At the same time, resource constraints have permitted only a three-fold increase in staff. What can be done? The Michigan approach has been to simplify, standardize, systematize and humanize, including the use of technology where machines can do the work more quickly, more accurately, and more economically. Targeting efforts on primary locations and categories of error is the next step in reducing error. Using this approach, Michigan hopes to reduce its error rate to 4 percent over the next two years.

Samuel K. Skinner, Chairman of the Illinois Fraud Prevention Commission, and a former U.S. Attorney, emphasized that his remarks were from the perspective of a private citizen. Citing a recent poll of Illinois citizens on government issues, Mr. Skinner noted that 78 percent of those responding favored steps to control costs, with 84 percent of that group ranking the prosecution of fraud as the highest priority. In Mr. Skinner's opinion, this result is to some degree an indictment of the system and those who manage it. Action is needed to improve the system, including removal of inequities (like the failure to apply the 30⅓ rule to those with low-paying jobs who are applying for benefits); increasing prosecutorial efforts, particularly toward public employees wrongfully on the AFDC rolls; and changing the rules, regulations, and laws that have created the current situation. Mr. Skinner concluded by urging a massive lobbying effort to bring about the necessary legislative and regulatory changes.

Forrest Campbell, Chairman of the Guilford County, North Carolina, Board of Commissioners, disagreed with the notion that the primary cause of error was mismanagement. In his opinion, the county is the proper locus for program administration; but the county must have a voice in how the programs are to be managed,

rather than being caught between Federal and State regulations. Fiscal relationships between the three levels of government must be addressed. More funding should be provided for staff training. Incentives should also be provided to cover the cost of prosecuting fraud at the local level.

Blanche Bernstein, Administrator of the New York City Human Resources Administration, cited unreported income as one of the major sources of fraud and error. New York City's experience has been that one must look to mass-production techniques to obtain information on income in a large urban setting. Since 1974, the City of New York has been using computer matches of payrolls. Beginning with a match of the city payroll, this program was later expanded to include the State payroll and those of quasi-government agencies such as the Board of Education. By 1978, 23 different types of matches had been established. The estimated annual saving from case closings and budget reductions are estimated at $50 million annually. The operational cost of the program is approximately $750,000 per year. To date, there has been little success in developing matches with private employers. In 1978, however, the New York legislature passed wage reporting legislation so that records of all wage earners will be available through the unemployment insurance system. Matching of these records will begin in January, 1979.

Kyle McKinsey, Deputy Director of the California Department of Social Services, spoke briefly on four points. First, he stated that he hoped the Secretary's Conference would establish an environment for increased action to reduce fraud and error. Second, he urged a balanced measurement of the program. California has a model which examines effectiveness, efficiency and equity. Management information systems are used to obtain measures on these dimensions, and to portray local-level conditions so that accountability and opportunities for appropriate corrective action are increased. As his third point, Mr. McKinsey cited the error rates for California, currently about 3 percent, which support the efficacy of this approach. Finally, Mr. McKinsey described monthly reporting and retrospective budgeting as effective tools in reducing error.

Mr. Ross concluded the session by expressing the hope that a spirit of mutual support and understanding would lead to solutions for the problems confronting income security programs.

III. SOCIAL SERVICES WORKSHOP

Moderator

T. M. Jim Parham
Deputy Assistant Secretary
  for Human Development Services
HEW

Panelists

Philip Toia
Deputy Mayor for Finance
New York City

Lou Glasse
Director, Office of Aging
State of New York

Honorable Alfredo Gutierrez
Majority Leader
Arizona State Senate

Staff Reporters

Charleen M. Tompkins
Administration for Public Services
Office of Human Development Services
HEW

James E. Huddleston
Administration for Public Services
Office of Human Development Services
HEW

Summary of Discussion

Philip Toia, New York City Deputy Mayor for Finance, opened the session. He asserted that HEW has changed from a professional and client-oriented approach to one centered on the legal and management aspects of its programs. In his opinion, this movement toward more efficient management was the result of: public outrage at expenditures; scarce dollars; and the activity of some outside advocacy groups.

Although much attention has been paid to fraud in nursing homes, fraud in the social service programs has been overlooked. Hidden ownership, vendor kickbacks, and improper billing practices have been noted in the provision of social services. Ineligibility of some clients and expensive facility leases increase the cost and rates of day care services financed by public dollars. In some neighborhood social service centers, there have been reports of diversion of funds to improper uses, inappropriate and excessive reliance on sole source contracts, and instances of kickbacks.

Mr. Toia also noted instances of abuse in social service programs: laxity in regulating child and adult residential facilities because there is often nowhere else to place clients; overutilization of services because they are available; and lack of placement goals which results in the mainte-

nance of children in foster care status for longer than necessary.

Another aspect of the problem involves poor management in establishing and enforcing eligibility, monitoring, evaluation, contracting, and accounting procedures. Inadequate information systems can lead to error. Another form of error results from agency or worker bias, which screens out eligibles but admits ineligibles into programs.

Mr. Toia continued by stating that although the credibility of social service programs is at stake, effective program justification is difficult because ordinary productivity methods do not apply, unit cost measures are not always applicable, and evaluation measures that embrace both objective and subjective criteria do not exist. Mr. Toia stated that in order to find solutions and exert management control over social services, the environment in which services are provided must be examined and understood.

Public welfare departments have often sought the experienced, old-line agencies from which to purchase social services even if those agencies were sometimes unable to deal with shifting State and Federal priorities. Welfare agencies also purchased services from emerging community, neighborhood, and "grass-roots" providers. The welfare agencies sometimes expected too much but accepted too little from these entities, providing classic examples of patroniz-

ing minority ventures but applying different standards of performance. The complex environment of the welfare agency also includes citizens' groups, public institutions, profit-making institutions and a constituency of clients with differing and highly individualistic goals.

Mr. Toia urged that initiatives against fraud, abuse and error must take this diversity into account if they are to succeed. He suggested that the following points should be considered in efforts to avoid social services fraud, abuse, and error: (1) whether social services should be delivered as an entitlement, similar to those of a public utility; (2) the role of data processing equipment and the danger of the servant becoming the master; (3) the difficulty presented by the limits of subjective measurement and the imperfect validity of objective measurement; (4) whether goals announced for a service program lend themselves to measurement; and (5) whether the service system can adapt to change.

Lou Glasse, Director of the New York State Office of Aging, noted that waste sometimes occurs because sufficient time to plan the best use of newly available funds is not available. Without adequate planning, there is a temptation to initiate a service in a manner which might not be most efficient or effective. Laws and regulations sometimes favor the use of expensive, easily identified services, rather than fostering development of a more effective service network. An example is the open-end funding available for child foster care compared to the limited funds available for services to strengthen children's own homes or to make other permanent plans for them. Another example is the greater availability of funding for nursing home care compared to that for in-home services for the elderly.

Ms. Glasse noted that although current management controls might be adequate for perhaps 90 percent of an agency's clients, a much more sophisticated system might be required. Since some newly created agencies serving the elderly do not have the sophisticated management experience of long-established agencies, technical assistance would need to be provided in order to help new agencies minimize the potential for loss of funds through abuse.

Alfredo Gutierrez, Majority Leader of the Arizona State Senate, commented that public demand for reduced expenditures, as shown by

"Proposition 13" type actions, was a forerunner of the pressures that would affect social services. He urged that we look at the phenomena which contribute to fraud, abuse and waste, noting that most fraud associated with medical care costs was committed by providers and not patients. Yet the political process rewards the contributions of providers by favoring their viewpoints. Senator Gutierrez also stated that inflexibility of Federal regulations limits the capabilities of local managers to direct resources and to solve local problems.

Comments and Questions

Comment from Gerald J. Reilly New Jersey Department of Human Services.

Mr. Reilly noted that some non-profit residential agencies used public funds to acquire property worth millions of dollars. He suggested that there be a recognition of the legitimacy of profit but effective public control of rates.

Mr. Toia responded that there are current attempts to incorporate business practices in social services.

Ms. Glasse suggested cost effective controls which might include samples of expenditures.

Mr. Parham responded that sample audits covering both fiscal and program goals were useful. There is difficulty in determining if program goals are met, however, when traditional audit approaches are used.

Comment from Mary Ellen Preusser, City Councilor, Cambridge, Massachusetts.

Ms. Preusser emphasized that local elected officials should be included in planning for social services.

Mr. Parham responded that the Administration had proposed legislation requiring local involvement in Title XX planning, but the legislation failed to pass.

Question from Paul Dahlstrom, Administration on Aging, HEW, Washington, D.C.

He asked if the administration was serious in assuring protection for "whistle-blowers" who reveal fraud, abuse, or error on the part of Federal agencies.

Mr. Parham replied "Yes."

IV. STUDENT FINANCIAL ASSISTANCE WORKSHOP

Moderator

Ernest L. Boyer
U.S. Commissioner of Education
HEW

Panelists

Dr. John G. Kemeny
President
Dartmouth College

Dallas Martin
Executive Secretary
National Association of Student Financial Aid
   Administrators

Charles C. Teamer
Vice President
Dillard University

Joel Packer
Legislative Director
U.S. Students Association

Leo L. Kornfeld
Deputy Commissioner for Student Financial
   Assistance
U.S. Office of Education
HEW

Staff Reporter

Patricia Dorn
Office of the Deputy Commissioner
U.S. Office of Education
HEW

Dr. Boyer opened the session by stating that fraud, abuse, and error are unacceptable in the administration of student financial assistance programs. Practically every college benefits from student aid funds, and these programs can and must be run efficiently. Access to higher education is a policy of this Administration and we must find ways to assure such access.

Dr. Boyer then discussed several specific problems with student aid programs and solutions to those problems:

Problem: The administration of student financial aid programs was fragmented.

Solution: The Office of Education (OE) was reorganized. All student aid programs were reorganized into a new Bureau of Student Financial Assistance.

Problem: Prior to this year, there were no procedures for validating eligibility in the Basic Grant program. As a result, many students who were ineligible for the program were able to submit false information in order to meet eligibility criteria or to receive larger Basic Grant awards than they were entitled to.

Solution: OE initiated a computer screening program to detect and reject Basic Grant applications which are incomplete or contain inconsistent information.

Problem: The 1977 default rate in the Guaranteed Student Loan program was 13 percent. (More than 300,000 loans in default, involving more than $300 million.) Many defaulters were never regularly billed by the Federal Government because there was no effective billing system. Lenders were not making aggressive efforts to collect delinquent loans.

Solution: OE contracted with a private collection agency to assist in collecting from defaulted borrowers, and is also offering preclaims assistance to lenders. This new service permits early identification of student borrowers who are unlocatable, delinquent on their accounts, and those who are potential or actual defaulters. As of October, 1978, the default rate had been reduced to 10.5 percent. By the end of the fiscal year it will be 9 percent.

Problem: In the National Direct Student Loan (NDSL) program, there was a default rate of 18 to 20 percent; and 90 percent or more of the NDSL borrowers at some schools were in default. Many institutions had done little or nothing to collect on these loans.

Solution: OE is working with institutions to bring down the default rate, and has begun enforcing provisions in the 1972 Education Amendments as they apply to this program.

Dr. Boyer closed by reiterating the importance of student financial aid programs in providing access to post-secondary education and OE's determination to eliminate fraud, abuse, and error so that the programs can effectively serve those they are intended to serve.

Dr. John G. Kemeny, President of Dartmouth College, began his remarks by stating that student financial aid programs are vital for the success of higher education. In his opinion, error exceeds abuse in the administration of these programs. Dr. Kemeny asserted that the regulations for these programs are too complex and too difficult to read: Just when you reach the point where you understand them, he said, they change. He recommended that the regulations be written in simpler language, and that there be a 5-year moratorium on changes.

Dr. Kemeny then cited some specific aspects of student aid programs:

- The application forms in the Basic Grant program are too complex. They should be redesigned, simplified and made as easy to complete as the short Federal Income Tax Return. In addition, the Basic Grant program should be totally administered by the Federal Government and validation should be the joint responsibility of HEW and the Internal Revenue Service.
- Because students must select an educational institution before they know the amount of the Basic Grant award, Dr. Kemeny suggested that applicants be permitted to use the previous year's income tax information when completing their applications.
- Dr. Kemeny said he believes there should be a requirement for verification of information for campus-based programs. In addition, institutions should be allowed more flexibility in administering these programs.
- Problems exist in the NDSL program because the early concept of the program

was unclear to many institutions. Dr. Kemeny recommended more flexibility in the repayment schedule for both the NDSL and GSL programs. He noted that the default rates of the NDSL and GSL programs should not be compared because postsecondary institutions cannot be compared with banks.

Dr. Kemeny concluded his remarks by saying that the student financial aid programs were intended to provide educational opportunities for the underprivileged, and that he hoped HEW would not lose sight of this goal in efforts to eliminate fraud and abuse.

Dr. Dallas Martin, Executive Secretary of the National Association of Student Financial Aid Administrators, emphasized the need for close coordination between Federal, State, and local governments—a partnership. OE must see that funds go to those they are intended for, and effective delivery of the programs is essential if we are to prevent fraud, abuse, and error.

Dr. Martin recommended that student financial aid regulations be published on a timely basis, and that they be flexible and consistent.

Charles C. Teamer, Vice President of Dillard University, said that in order to deal with the problems of abuse and error, institutions must make management improvements. OE and institutions must use audits realistically to make improvements in the programs.

Mr. Teamer stated that the Basic Grant program has, in reality, become a campus-based program because individual institutions are responsible for validation, audits, and a number of other aspects of the program's administration. Institutions need financial support to correctly administer all of these elements. The current four percent administrative allowance is not adequate.

Mr. Teamer concluded his remarks by urging the Administration to recognize the need for increased financial support for institutions, so that campus-based student aid programs well be managed correctly and efficiently.

Joel Packer, Legislative Director for the U.S. Students Association, made several recommendations:

- OE and educational institutions should make financial aid information understandable and available to students;
- Students should be permitted to participate in the development of program regulations;
- OE should prevent mismanagement, balance program integrity, and assure that

funds go to the students for whom they are intended;

- OE should protect students from the abuses of shoddy institution policies; and,
- The student aid reauthorization legislation should require campus-based student grievance procedures as a condition for institutional participation.

Leo L. Kornfeld, Deputy Commissioner of the Bureau of Student Financial Assistance, OE, summed up the session by stating that student financial assistance programs can be better managed. He stated that the problem has not been fraud, but rather sloppiness of program administration. Students, he said, are not rip-off artists—the programs were just not being run well. Because the programs are so complex, they invite abuse. For example, if the NDSL program had been administrated properly, instead of the 800,000 loans made this year, institutions would have been able to lend funds to approximately 1.6 million students.

Mr. Kornfeld concluded the session by noting that all student financial aid programs are being carefully reexamined and changes will be made. Validation and simplicity are essential to the elimination of abuse and error.

HEALTH DISCUSSION GROUP A: "FRAUD INVESTIGATION AND PROSECUTION"

Leader

Charles J. Hynes
Deputy Attorney General
Office of the Special Prosecutor
State of New York

Panelists

Joseph Piazza
Director, Program Integrity Unit
New Jersey Medicaid Program

George Wilson
Assistant U.S. Attorney
Southern District of New York

Donald Zerendow
Chief, Medicaid Fraud Control Unit
Commonwealth of Massachusetts

Barry Sax
Assistant District Attorney
Los Angeles County
California

Edwyna Anderson
Chief, Consumer Protection and Economic Crime
Division
Genesee County Prosecutor's Office
Flint, Michigan

Staff Reporter

Robert G. Harrison
Office of Program Integrity
Health Care Financing Administration
HEW

Summary of Discussion

There were three major discussion points:

1. The need for program agencies to recognize the potential for fraud and abuse and to structure legislation, regulations, and operating procedures that will minimize, if not eliminate, opportunities for fraud, abuse, and error.
2. The critical importance of communication among all concerned entities (Federal, State and local) and coordination of all investigative activity.
3. The importance of early consultation with, and involvement of, prosecutors in an investigation and the need for expeditious pursuit of prosecution once an investigation has been completed.

The discussion leader, Charles J. Hynes (Director of the New York State Medicaid Fraud Unit), set the tone of the discussion as he chronicled the development and effectiveness of the team approach in his investigation of nursing homes in New York. That approach, which influenced the structure of PL 95-142, and which can be adapted to other areas of provider fraud investigation, represents the kind of critical interrelationship that must occur at and between all levels of government to facilitate control of fraud, abuse, and error.

Joseph Piazza (Director of the Program Integrity Unit in the New Jersey Medicaid Agency), commented on the vulnerability of the Medicaid program and some possible causes for the incidence of fraud, abuse, and error. He emphasized that poor payment structures, lax claims validation systems, and the absence of cost-

sharing features in Medicaid tend to result in overutilization of services and, therefore, present a temptation to providers who are motivated by fear of malpractice, or simply greed. He cautioned the audience as to the possible adverse impact of P.L. 95-142 on public perceptions of the Medicaid agency and program, particularly as the number of fraud prosecutions increases.

Edwyna Anderson (Chief of the Consumer Protection and Economic Crime Division of the Genesee County, Michigan, Prosecutor's Office) discussed the difficult problems her office faced as it moved into fraud and abuse in health care programs. She cited the major obstacles as:

1. Lack of easy access to provider records.
2. Lack of adequate funds or available expertise in health care fraud.
3. The absence of sufficient statutory authority to prosecute fraudulent or abusive practices uncovered in her State.

Ms. Anderson appealed to HEW to consider funding local prosecutors to enable them to join the effort against fraud and abuse.

Donald Zerendow (Chief, Massachusetts Medicaid Fraud Control Unit) prefaced his remarks by observing that the problems of fraud, abuse, and error in Medicaid and other health care programs are largely the result of the absence of a policing body until now. Even with the establishment of Medicaid Fraud Control Units, the larger responsibility accrues to the program agencies in improving their financing and reimbursement systems. Mr. Zerendow also reminded the audience that the fraud control units have the difficult responsibility of investigating and prosecuting instances of physical abuse and neglect of Medicaid patients. This responsibility will require many of the Units to seek legislative tools to effectively pursue such cases, since many

States presently lack adequate statutory provisions in this area.

George Wilson (Assistant U.S. Attorney for the Southern District of New York) encouraged those involved in prosecuting health care fraud to initiate and maintain relationships with the Department of Justice because of the greater statutory latitude of the Federal prosecutor.

Mr. Wilson emphasized that Federal statutes in the areas of conspiracy, filing false claims and making false statements, mail fraud, racketeering and corruption, as well as the civil damages leverage, are not encumbered by State boundaries. In addition, resources at the U.S. Attorney's disposal may be extremely helpful to State and local prosecutors in difficult cases. He also emphasized that the ideal mix of investigative resources would include prosecutors and audit personnel experienced in health care fraud, and program specialists who can detail criminal circumventions or violations of program provisions.

The last speaker, Barry Sax (Assistant District Attorney for Los Angeles County), dramatically depicted the magnitude of fraud and abuse in California. Mr. Sax estimated that 20 percent of the 3.5 billion dollar medi-Cal budget may be lost as a result of fraud or abuse. He emphasized that the Medicaid fraud units alone are not the answer, but that regulations have to be clarified, streamlined and vastly improved. In addition, he echoed the comments of Ms. Anderson by suggesting the funding of local efforts to pursue violations in health care programs.

Mr. Sax concluded the discussion by urging that fraud, abuse, and error not be allowed to continue unabated for they tend to discourage legislators from expanding needed programs, encourage collusion in various sectors of the health care delivery community, and, most distressingly, deprive beneficiaries of needed health care.

HEALTH DISCUSSION GROUP B: "MODEL SYSTEMS— ABUSE DETECTION AND CONTROL"

Leader

William C. White, C.L.U.
Vice President
The Prudential Insurance Company
of America

Panelists

Thomas Gaylord
Director, Surveillance and Utilization Review Division
State of Minnesota

Janice Caldwell, Ed.D.
Director, Division of Long Term Care
Health Care Financing Administration, HEW

Philip Natcharian
Director, Bureau of Medicaid Fraud and Abuse
Department of Social Services
State of New York

Steward E. Uhler
Director, Utilization Division
Pennsylvania Blue Shield

Eleanore Rothenberg, Ph.D.
Executive Director
New York County Health Services Review Organizations

Staff Reporters

Barbara Hoffman
Office of Public Affairs
Health Care Financing Administration, HEW

Carol Rowan
Office of Public Affairs
Health Care Financing Administration, HEW

Summary of Discussion

The overall theme of this discussion group concerned the role of computer systems utilized in various settings for the identification and control of fraud, abuse and error. A companion theme, voiced by several panelists, concerned potential negative effects on innocent program beneficiaries resulting from computer detection of "fraud, abuse or error."

William C. White, Vice-President, The Prudential Insurance Company of America, discussed the role of the Medicare and Medicaid fiscal contractor in fraud detection and money recovery during the Health Workshop (See Page 28).

The first discussion group panelist, Thomas Gaylord, Director of the Surveillance and Utilization Review Division, State of Minnesota, echoed Mr. White's remarks by discussing the

role played by the Surveillance and Utilization Review System (SURS) in the Medicaid State Agency.

In Minnesota, SURS is the primary tool for post payment review. Information captured by SURS on 211,000 eligible Medicaid beneficiaries and 14,000 health care providers is subjected to a quality review, with emphasis placed on the detection of potential provider fraud or abuse. Health care professionals or social workers analyze the data, and follow-up field audits are scheduled to verify the computer findings. If fraud and/or abuse is verified, prosecution can then begin. This process of identification, analysis, investigation, and prosecution can be done entirely by the State Medicaid Agency. In Mr. Gaylord's opinion, such continuity of activity adds efficiency and credibility to their efforts.

Mr. Gaylord noted several problems relating

to the privacy law (signing of consent forms), the confidentiality of medical records, and time delays caused by the required involvement of Regional Health Care Financing Administration offices in the State Agency's interactions with Medicare providers.

Mr. Gaylord concluded his remarks with several recommended Federal actions for improving the handling of fraud/abuse and error cases by States:

1. Development of guidelines for effective abuse case presentations to peer review groups.
2. Drafting and passage of a model legislative package.
3. Development of guidelines for handling other forms of identified problems.

Dr. Janice Caldwell, Director, Division of Long Term Care, Health Standards and Quality Bureau, Health Care Financing Administration, introduced the "patient behind the computer" perspective to the discussion. Dr. Caldwell related her concern about the quality of care being given in long-term care facilities.

The Division of Long Term Care is responsible, through contracts with State agencies, for surveying over 18,000 long-term health care facilities to assure adherence to quality standards.

Information which can now be produced by sophisticated data systems had led to many instances of cost disallowances and the detection of fraud and abuse. Dr. Caldwell noted, however, that many provider cost disallowances actually become disallowances for patients. Thus, patients must bear the financial brunt of overutilization which results from poor physician practice.

Dr. Caldwell also suggested that patient neglect is another category of fraud and abuse—one which model systems cannot identify—and one which remains concealed because of the vulnerability of much of the long-term care patient population.

Dr. Caldwell ended her remarks by suggesting that close monitoring be given to:

● Proposed fraud and abuse amendments which would give the Secretary final authority in certification of Title XIX only (Medicaid) facilities.
● Possible waste in current licensure procedures for long-term care institutions.
● The possible lack of accountability and the existence of excessively high costs in State-run long-term care facilities.
● The fragmentation of long-term care services which leads to duplication, overlapping, fraud, abuse, and waste.

Steward Uhler, Director of the Utilization Division, Pennsylvania Blue Shield, described the utilization review process used by his organization.

Pennsylvania Blue Shield has developed a system combining both pre- and post-payment utilization review. This system provides a means of detecting providers who may be overutilizing services but avoids the costly process of reviewing each claim prior to payment.

The pre-payment system is beneficiary and claim-oriented. Each time a claim is received, the pre-payment screen, or history file examination, is applied. Screens may be applied in such categories as medical necessity, non covered services, diagnostic tests, durable medical equipment, etc. The screens establish parameters which, when exceeded, will cause a claim to be suspended and subjected to individual pre-payment review by professional and non-professional personnel. In 1977, over 8½ million dollars in claims were denied as a result of pre-payment utilization review for medical necessity alone.

Because some claims do pass through the pre-payment screens, a post-payment utilization review system has also been developed. The post-payment system is essentially provider and practice pattern oriented: an individual provider's pattern of practice is compared to the practices of providers within his peer group (peer group is defined in terms of locality and medical specialty).

A statistical formula (ratio analysis) was devised to resolve the inequity of comparing low to high volume providers within a peer group. The practitioner practice pattern analysis is used to identify unusual practice patterns and individual practitioners who exceed the norms.

Suspect information is forwarded to a Blue Shield Medical Advisor who examines the data for possible over-utilization. If indicated, a Blue Shield utilization Field Representative meets with the physician under review. If necessary, the case may be referred to the peer review committee of the appropriate professional society. In summary, Mr. Uhler stated that Pennsylvania Blue Shield's pre- and post-payment utilization review, involvement of medical professionals in the review process, and strong emphasis on provider education, have produced an effective pre- and post-payment utilization review system.

Dr. Eleanore Rothenberg, Executive Director, New York County Health Services Review Organizations, discussed the role of peer review in abuse detection and control. The New York County Professional Standards Review Organization (PSRO) has a membership of over 5,400

including professionals from five medical centers, over twenty teaching hospitals, several community hospitals, and public health organizations.

PSRO review of the quality of acute hospital care given to Medicare and Medicaid hospital patients has produced some shocking findings:

● In one hospital, patients were admitted to a 16-bed alcoholism detoxification unit which had never been licensed by the State. Moreover, patients were discharged without being drug-free: they were merely given other (non-alcoholic) drugs, and discharged while still in a drug-dependent state.
The PSRO assembled a task force of psychiatrists and internists skilled in the treatment of alcoholism. The task force established criteria and standards for care of alcoholism related to:
● hospital admission
● detoxification treatment
● post-detoxification treatment
● In another acute care hospital, it was found that 40% of those admitted for alcohol detoxification could have been treated in a non-acute care (and less costly) setting.
● A hospital in an underserved area admitted patients for services that could not be provided on a timely basis, or at all:
 ● Patients admitted for concussions waited one to two weeks to be examined by a neurologist and some were never examined.
 ● Patients were admitted with fractures, but the fractures were not treated by an orthopedic surgeon until after one to two weeks had elapsed.
 ● A patient was admitted with gangrene of the feet; yet the hospital's medical notes indicated no treatment of the gangrene but revealed a cataract extraction one week after admission.
 ● Diagnostic workups were either not performed at all, or were performed several days following admission.
The PSRO sent a team of physicians to review a sample of the hospital's charts. Sixty-five charts were examined in detail, and the physician team concluded that 50 percent of the charts documented care that was not merely substandard, but actually dangerous!
As a result of the team's findings, the New York County PSRO recommended sanctions against the hospital. Since, however, the Federal regulations gov-

erning PSRO sanction procedures have not yet been published by HEW, the PSRO is powerless to take action.

Dr. Rothenberg continued her presentation by citing some additional findings developed by the New York County PSRO:

● In 1977, a number of hospitals billed the Medicaid agency for days of care which had not been certified as medically necessary by the PSRO. One hospital even forwarded copies of the PSRO disallowance letters along with its erroneous bills. The PSRO found that the Medicaid agency was paying for the uncertified days of care because its computer was not programmed to reject errors.
At the PSRO's request, the City Comptroller investigated the loss of funds and found that over $2 million had been lost in New York County and in excess of $11 million in New York City as a whole.
Now, the Medicaid Agency computer has been programmed to detect errors and reject them. In addition, past payments are being examined and erroneous overpayments will be recovered.
● One hospital was found to have submitted multiple bills for payments for the same patient, for the same procedure, during the same week. As a result of the PSRO's investigation, the hospital was withdrawn from Medicare and Medicaid eligibility, and subsequently closed.

Dr. Rothenberg ended her presentation by noting that computer systems are powerful mechanisms for detecting fraud, abuse, waste, and overutilization. The verification of the actual existence of these problems may require the services of a well-organized and well-structured peer review organization such as a PSRO; hence, Dr. Rothenberg urged that PSRO's be contacted in connection with efforts to reduce fraud, abuse, and error in the Medicare and Medicaid programs.

Philip Natcharian, Director, Bureau of Medicaid Fraud and Abuse, Department of Social Services, State of New York, was the final panelist.

Mr. Natcharian noted that in early 1977, Governor Hugh Carey announced his intent to concentrate on the problems of fraud and abuse in the New York Medicaid program. The Governor subsequently obtained authority and appropriations to establish an extensive Medicaid Fraud and Abuse Unit within the Department of Social Services. In addition, computer capability was

developed to capture information needed for investigative purposes.

The information now includes records of payments made over a five-year period. This data base has been subjected to computer reviews to help detect defrauding or abusive providers. These reviews have revealed much duplication of payments, excessive numbers of visits, "ping-ponging" (same beneficiary seen by numerous providers within a short time span), and "family ganging" (where a number of members of the same family are seen by the same provider on the same day). This information has been useful in the detection of some providers whose practices are aberrant, and in developing provider profiles. Where warranted, detailed reviews of these profiles are made, and such reviews may lead to further investigation and subsequent prosecution or administrative sanctions.

Mr. Natcharian then briefly described a fraud case involving a medical laboratory which ultimately resulted in referral for prosecution. He concluded by reiterating New York State's recognition of a massive fraud, abuse, and error problem and the strong commitment to resolve the problem through the use of historical payment data, the installation of a newly approved Medicaid Management Information System, and the development of pre-payment controls and improved post-payment detection capabilities.

HEALTH DISCUSSION GROUP C: "ADMINISTRATIVE REMEDIES"

Leader

Paul Allen
Deputy Director for Medical Services
Administration
State of Michigan

Panelists

Michael Tristano
Chief, Bureau of Program Integrity
Illinois Department of Public Aid

Fred Lucas, M.D.
Medical Director
National Heritage Insurance Company/E.D.S.F.

Peter Bloomsburg
Assistant Commissioner for Medical Assistance
Massachusetts Department of Public Welfare

C. Willard Camalier, Jr., M.D.
Member, House of Delegates
American Medical Association

Staff Reporters

Barry Steeley
Program Analyst
Health Care Financing Administration, HEW

Bill Broglie
Program Analyst
Health Care Financing Administration, HEW

Summary of Discussion

Major Discussion Points:

1. The value of educational contacts with providers of services to correct aberrant practices;
2. The use of overpayment control systems to foster the identification and recovery of overpayments;
3. Other types of administrative remedies such as 100 percent review of claims submitted by aberrant providers, and exclusion or suspension of such providers from Medicare or Medicaid program reimbursement.

The overriding concern which was stated in the remarks of each of the five panelists was the need to develop a total system to administratively correct situations which represent fraud or abuse of the Medicare and Medicaid programs.

Paul Allen (Deputy Director for Medical Services Administration, State of Michigan) emphasized that the administrative solutions to provider fraud or abuse are often ill-defined. He spoke of the need to develop a comprehensive system of fraud and abuse detection and resolution including the use of front-end edit and post-payment review techniques, educational contacts with pro-

viders, overpayment identification and recovery, and, in some cases, suspension of the provider from the Medicaid program.

Peter Bloomsburg (Assistant Commissioner for Medical Assistance, Massachusetts Department of Public Welfare) emphasized the importance of effective management of the Medicaid program, and of the involvement of various units (Department of Welfare, Attorney General, the medical community) in the systematic detection and elimination of fraud and abuse. Such a systematic approach to fraud and abuse serves an integral role in the management of the Medicaid program by:

1. Serving as a deterrent to encourage proper provider performance;
2. Providing for the recovery of overpayments made to providers;
3. Insuring high-quality, low-cost health care by suspending aberrant, abuse-prone providers from the program; and
4. Providing feedback mechanisms on the effectiveness of the program's policy, procedures, and systems.

Dr. C. Willard Camalier (Member, House of Delegates, American Medical Association) described the AMA's position on identifying and controlling fraudulent and abusive practices: the

AMA seeks to actively assist in the detection, resolution, and control of fraud and abuse in medical care. Dr. Camalier identified the need for resolution of the current conflict between the position of HEW (which is encouraging greater assistance by the AMA) and the Federal Trade Commission (which holds that peer review determinations as to whether services conform to appropriate professional standards and are delivered in the most effective, efficient, and economical manner possible, may constitute restraint of trade or price fixing); this conflict may undermine AMA efforts to eliminate fraud and abuse.

Dr. Fred Lucas (Medical Director, National Heritage Insurance Company/E.D.S.F.) reiterated the need for a coordinated approach to fraud, abuse, and error detection and resolution, which would include: (1) an effective postpayment review process to identify problems; (2) a provider-education effort when problems are detected; and (3) additional prepayment monitoring of future claims. He noted the State-to-State variations in Medicaid Management Information Systems, and the difficulty of identifying "fraud" through claims processing. He also noted (with the acknowledgment of other panel members) that provider abuse occurs as frequently in Medicare as in Medicaid.

Michael Tristano (Chief, Bureau of Program Integrity, Illinois Department of Public Aid),

echoed previous panelists in his emphasis on the need for comprehensive fraud and abuse detection/resolution systems. He particularly noted the importance of: (1) suspensions/terminations to eliminate abusive providers from the program as quickly as possible; (2) recoupment of overpayments; (3) providing for administrative fines (civil money penalties) for violations; (4) effective legislation and regulations; and (5) computer systems to detect fraudulent or abusive practices. Mr. Tristano indicated that administrative remedies are effective, quick, in-house measures which can be taken to resolve fraud and abuse; while other remedies (e.g., criminal and civil prosecution) are more cumbersome and time consuming, and are not within the control of the agency which administers the program.

Questions and comments raised during the group discussion which followed focused on: (1) the need to integrate the medical community more fully into processes designed to identify fraudulent and abusive practices; (2) the need to simplify procedures, and establish common forms and definitions in connection with Federal health care programs; and (3) the need to more aggressively identify and resolve recipient fraud/abuse (e.g., through educational programs; Medicaid coinsurance/copayment for services; recipient lock-in to one doctor, drugstore, etc., to prevent overutilization of services; and financial incentive programs to promote recipient responsibility in utilizing health care).

HEALTH DISCUSSION GROUP D: "EXCESS CAPACITY AND OVERUTILIZATION"

Leader

William H. Stewart, M.D.
Acting Head
Department of Preventive Medicine and
    Public Health
Louisiana State University School of Medicine

Panelists

Anthony T. Mott
President
American Health Planning Association

John M. Eisenberg, M.D.
Assistant Professor of Medicine
University of Pennsylvania School of Medicine

Reverend A. Gene Parks
Consumer Representative
Florida Statewide Health Coordinating Council

Robert Flanagan
Vice President
American Hospital Association

Neil Hollander
Vice President for Health Services
Blue Cross and Blue Shield Association

Staff Reporters

Dr. Florence Fiore
Acting Director, Bureau of Health Facilities
    Financing, Compliance and Conversion
Health Resources Administration
PHS/HEW

William Berry
Acting Deputy Director
Bureau of Health Facilities Financing,
    Compliance and Conversion
Health Resources Administration
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Summary of Discussion

Anthony Mott, President of the American Health Planning Association, presented the perspective of the health planning community. He indicated that excess capacity and overutilization had, in part, stimulated the passage of Federal legislation (P.L. 93-641) which supports the current health planning structure. While earlier health planning efforts were focused largely on resource development or capacity building, the present approach is more related to data gathering, problem identification, priority setting, and plan development. The current emphasis is upon cost containment, a major portion of which relates to reduction of excess capacity. Health planning agencies are or should be deeply involved in these issues.

The average hospital bed to population ratio in the United States is 4.5 beds per thousand population. The range extends from 3 to 10 beds

per thousand. The new National Guidelines suggest an upper limit of 4 beds per thousand. Capacity in excess of real need, which may vary from place to place (e.g., rural or urban settings) has a major impact on service delivery costs. These costs are borne by governmental and private third-party payors.

In the Rochester, New York, area (served by the Health Systems Agency (HSA) in which Mr. Mott is Executive Director), the bed to population ratio is 3.5 beds per thousand and services are provided at 18 percent below the national average cost for hospital services. Even with this relatively low bed capacity, hospital leaders in Rochester are in agreement that another 300-500 beds can be removed from the system.

In Mr. Mott's opinion, the present hospital system in the United States is too big and its growth is supported by "all the wrong incentives." He noted that the issues involved are primarily political rather than technical, and

that technical capacity to find solutions already exists or can be developed in a relatively short period of time. While there is general support for cost containment, there is little support for specific actions to reduce capacity.

Mr. Mott disagreed with Dr. Stewart's contention that no structure presently exists which can effectively reduce excess capacity and over-utilization. In Mr. Mott's view, Health Systems Agencies and State Health Planning and Development Agencies can have an impact. The question is whether or not they will. Their ability to be effective is currently hampered by limited funding and inadequate Federal direction.

Although hospital closures can be viewed in a context similar to that of school closings, there are fewer incentives for hospitals to stop operation. Until there are increased governmental incentives at Federal, State, and local levels, the health planning process will have little positive impact on excess capacity.

Dr. John M. Eisenberg, Assistant Professor of Medicine at the University of Pennsylvania School of Medicine, stated that the problems of excess hospital capacity are similar to those of energy conservation. These problems relate to the size of the engine and the speed at which the engine runs.

Costs generated by hospitals are only a partial concern, since 70 percent of costs for health services are generated by physicians. Physicians are responsible for decisions which affect the utilization of health care resources. The Roemer effect (i.e., an increased supply of physicians results in increased demand for service) indicates an "error" in the system. Major problems relate to the maldistribution of medical manpower and the oversupply of specialists such as surgeons and internists. The new emphasis on primary care needs to be evaluated in terms of cost effectiveness. In addition, reimbursement policies and procedures must ensure that primary care providers are rewarded in ways that are commensurate with the rewards now received by specialists. These factors will influence the "size of the engine."

The "speed of the engine" is affected more directly by technological considerations. While it has been suggested that increased use of technology is the result of physician concern about possible malpractice suits, some evidence suggests that this hypot. is not true. More important factors may relate to the fact that both physicians and patients are poorly informed about the cost effectiveness of various medical procedures. This lack of knowledge is compounded by reductions in the availability of funds for assessing the efficacy of new technologies. Al-

though such reductions may be appropriate on a short-range basis, they could present serious long-range problems.

Dr. Eisenberg noted that there are currently no incentives to control utilization in fee-for-service settings. He suggested that perhaps reimbursement penalties need to be introduced. PSRO's and third-party payors have the ability to apply such penalties, but they are only infrequently used.

Dr. Eisenberg concluded by stating that in addressing questions of excess capacity and over-utilization, the role of physicians as well as that of hospital bed supply must be considered. As to the role of physicians, it will be important to try to influence the "speed of the engine" through:

1. Decreased fear of malpractice;
2. Increased physician knowledge of cost effectiveness;
3. Increased patient knowledge of cost effectiveness;
4. Increased incentives for physicians to decrease utilization.

Neil Hollander, Vice President for Health Services, Blue Cross and Blue Shield Association, noted that hospitals are growing, self-perpetuating, and maximizing institutions. These phenomena are not peculiar to hospitals. The public interest and the interest of individual hospitals are not synonymous in every instance. Until recently, public policy has encouraged growth, and this policy has resulted in excess capacity and inappropriate utilization. Mr. Hollander indicated the specific issue of controls needs to be addressed. He then raised several questions about Dr. Stewart's proposal for a locally-based regulatory authority:

1. Who should be the authority?
2. To whom would it be accountable?
3. How would it relate to other key actors?
4. How would inter-area differences be resolved?

Mr. Hollander asserted that we often create new institutions as a means for circumventing existing structures; we already have HSA's, SHPDA's, SHCC's and other State agencies with regulatory powers. The problem seems to be how we can increase the effectiveness of these bodies. One way would be to increase the involvement of business, labor, and third-party payors.

In Mr. Hollander's view, the pluralistic approach is sound: this is not an argument for the status quo, but rather a plea to strengthen what is presently being built. Blue Cross-Blue Shield Plans have been implementing approaches

to increased effectiveness and have stood in strong support of health planning agencies.

Robert Flanagan, Vice President of the American Hospital Association, stated that there is a distinction between excess capacity and over-utilization, and we need to understand the difference. Excess capacity basically represents an increase in fixed costs, and has largely resulted from overresponse to programs such as Hill-Burton. Appropriate utilization can induce increased demand, and this situation mainly results from quirks in the reimbursement system. Excess capacity and overutilization overlap but each has distinguishing characteristics.

Excess capacity should not be considered a static situation. For example, capacity must be viewed in relation to population changes.

Mr. Flanagan noted that government-mandated programs immediately provoke resistance because "it's come down from Big Brother." Such resistance hampers implementation, and also raises Constitutional rights questions. In Mr. Flanagan's view, a better approach would be for Government to provide incentives which would encourage the private sector to reduce excess capacity (e.g. more flexible anti-trust provisions). Mr. Flanagan noted that most health facility closures to date have resulted from economic pressures or involved outdated facilities.

Other aspects of reducing excess capacity include:

● Changes in physician behavior, since physicians are responsible for demand;
● Community involvement and support; and
● Possible use of the Medicare "Conditions of Participation" as leverage to close facilities and/or reduce costs. Currently, there are no incentives to close.

Mr. Flanagan concluded his remarks by urging that, in undertaking reduction of excess capacity and overutilization, the following elements be considered:

● Availability
● Access
● Quality
● Cost

The Reverend A. Gene Parks, Consumer Representative, Florida Statewide Health Coordinating Council, opened his remarks by noting that the forces for perpetuating the status quo are very strong. The integration of health and health-related services (as suggested in Dr. Stewart's paper) is a utopian concept. Experiences in some settings suggest it will be a long time in coming. Therefore, we must use the

mechanisms at hand. Reverend Parks stated that his experience in working with agencies created under P.L. 93-641 had led to the following observations:

● Within the planning agencies, there is a high level of hard work and commitment.
● Ninety-two percent of proposals for maintenance, creation, or expansion of health resources are approved. Health Systems Agency Certificate-of-Need approvals are more related to "extenuating circumstances" than to planning objectives. Persuasive arguments by providers sway decisions, especially in the absence of hard data or arguments to the contrary. The only way to overcome these difficulties is through establishment of a cap on expenditures.
● Criteria such as Medicare conditions of participation should be part of the planning process to ensure that adequate services are available.
● Tradeoffs related to closure need to be examined on the basis of:
a) analysis of unmet needs;
b) analysis of excess capacity;
c) conversion to new uses.
● Background data ought to support health planning decisions and should be made available to the public.

In response to comments related to his integrated services concept, Dr. William Stewart indicated that what he had in mind was "a rather modest approach."

Summary of Questions and Answers

Q. Dr. Ritter, Cape Girard, Missouri, PSRO—Are the top ten medical schools pushing the training of primary care physicians? When you are ill (this question was addressed to Dr. Eisenberg), do you see a primary care physician or a specialist?

A. Dr. Eisenberg—In answer to the first question, the response is largely yes. The training of primary care physicians is a rather universal trend. With regard to your second question, it is not unreasonable for any American to go to a general practitioner. The training for general practice has now become a specialty and these individuals serve as an appropri-

ate initial contact with the medical profession.

Q. Peter Wynn, New York State Department of Social Service—Mr. Mott was requested to give more information about incentives which might stimulate closure of excess capacity.

A. Mr. Mott—Most existing incentives are directed toward growth. There should be more incentives for the development of arrangements such as multi-institutional systems. Present reimbursement methods are a disincentive to merger.

Q. Sylvia Kaslow, Service Employees International Union—Does certificate of need deal with closure? What about closures in inner-city areas?

A. Mr. Mott—The New York State certificate of need program has decertification provisions, but most certificate of need approaches do not address the closure of facilities. The special needs of inner-city and rural areas must be considered by planning agencies in reaching decisions related to the issuance of certificates of need.

Q. Dr. Kalb, Eastern Illinois Medical Care Foundation—Will we have enough beds to meet the demand under a program of national health insurance?

A. Mr. Hollander—This will have to be determined on the basis of a need assessment of specific areas, since such needs will vary depending largely upon population mix. These decisions should be made locally under national guidance. The existing National Guidelines can have a reverse impact if they are looked upon by planners as a floor rather than a ceiling.

Q. Bill Eagles, Richmond, Virginia—What is the current status of Hebert Hospital in New Orleans? How does its operation related to the fact that it is not under the jurisdiction of a PSRO?

A. Dr. Stewart—The New Orleans Health Systems Agency has estimated 1,000 excess beds in its health service area. This does not include the beds which are part of Hebert Hospital. It would be unwise to look at that Hospital out of context. It is important to look at the whole system in order to reach reasonable conclusions.

A. Dr. Eisenberg—There is evidence to indicate that increases in the provision of ambulatory care services create increases in the utilization of hospital care. If we have a program of national health insurance, perhaps we will have less hospitalization, provided that ambulatory care is given in group practice settings.

Q. Dr. Bixby, Philadelphia PSRO Member—The insurance approach to coverage for health services has operated to increase hospitalization. Poor record keeping and inadequate filing systems make it difficult to detect and control over-utilization or abuse. Can't there be a common identification number, such as a Social Security number, which would assist in implementing necessary controls? (Dr. Bixby also made reference to the fact that it has been estimated that it costs hospitals approximately $20 per bed to carry out responsibilities imposed by regulatory agencies.)

A. Mr. Flanagan—There is no question that regulation has contributed to additional costs of health care. Some regulations are good and should be supported. Other regulations are overlapping and should be eliminated.

Q. Carl Showalter, Colorado State Legislator—The most expensive health care is generally provided to the elderly population. Do you favor legislation related to the right to die? In connection with his question, Mr. Showalter cited statistics related to the saving of premature infants at great expense.

A. Dr. Stewart—Some States have "living will" provisions. With regard to premature infants, the saving of children's lives has not generally been looked upon as a waste.

A. Reverend Parks—From a personal perspective, I and members of my family would like to have the opportunity or the right to choose to die.

Q. J. Rankin—F.D.A.—A recent conference on medical malpractice suggested that the fear of malpractice suits will have an impact on increasing use of x-ray and other radiologic procedures.

A. Dr. Eisenberg—I know of no studies which support that conclusion.

Q. A New Hampshire HSA Representative—Is the single State HSA concept causing problems in the implementation of Public Law 93-641?

A. Mr. Mott—Yes, it is a problem for which I do not have a solution. (A member of the audience then expressed the opinion that there should be no States with single Statewide HSAs but rather such States should be permitted to come in under Section 1536 of the law.)

Comment by: Dr. Long, PSRO of Los Angeles

—There needs to be improved understanding of the legal implications of medical practice. Dr. Eisenberg does a disservice by minimizing the impact of the legal profession on the practice of defensive medicine.

Q. Mr. B. Henry, New York City Medicaid Program—There appears to be excessive utilization by Medicaid patients who are simply testing the system to find out what is available. Doesn't the second opinion stimulus currently being introduced by third-party payors encourage overutilization?

A. Mr. Hollander—There have been indications of overutilization by the Medicaid population. However, when Medicaid pa-

tients become members of HMO's, this tends to moderate. Also, the health of the poor who now receive care under Medicaid appears to be improving with the consequent lessening of utilization. With regard to second opinions, the cost for the second opinion is much lower than the potential cost of surgery which may not be necessary.

Q. Dick Klinger, Blue Cross of Ohio—Where has health planning succeeded? How was its success achieved? How can a capital expenditure limit be put on local areas?

A. Mr. Mott—Data currently being analyzed by the American Health Planning Association indicate a savings of approximately $2 billion in a three-year period related to certificate-of-need decisions by health planning agencies. Other than this information, there is little hard data to support a claim of success. However, anecdotal evidence suggests that progress is being made. Ohio is probably as good a place as any with regard to the impact of its planning system.

A. Reverend Parks—With regard to limitations on capital expenditures, there are no good answers; however, I believe the decision should be made locally by a representative community group.

WELFARE DISCUSSION GROUP A: "MONTHLY REPORTING AND RETROSPECTIVE BUDGETING"

Leader

Michael C. Barth
Deputy Assistant Secretary for Income
Security Policy
HEW

Panelists

John T. Dempsey
Director
Michigan Department of Social Services

Eddie Schoech
Director, Boulder County Department of
Social Services
Boulder, Colorado

Kyle S. McKinsey
Deputy Director
California Department of Social Services

Adele Blong
Attorney, Center on Social Welfare Policy
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Introductory Remarks— Michael C. Barth

Good afternoon and welcome to the Discussion Group on "Monthly Reporting and Retrospective Budgeting" of *The Secretary's National Conference on Fraud, Abuse, and Error.*

Secretary Califano convened this conference to broaden the discussion of how to manage programs that help people in the most efficient way possible.

This conference is the place for:

- HEW to inform you of what we are doing to protect the taxpayer's dollar, while still protecting the less fortunate; and for
- you to give us your ideas on how we can do a better job. What works and doesn't work? What other procedures do you believe should be tried?

The Department of Health, Education, and Welfare intends to wring out of the programs it administers and funds all of the fraud, abuse, and error that can be wrung out.

To manage programs efficiently is the compassionate way to manage the public's money for it enhances the public's confidence that assistance dollars are going where they are most needed. The American people are willing to help the less fortunate among us, but only through programs that are, and appear to be, efficiently, effectively, and equitably administered. If we want to help the poor, the sick, the unemployed, we shall have to pay more attention to public management than has been done in the past.

Fraud, even if committed by a few, is very serious because, by impugning the veracity of the many, it makes people reluctant to commit resources to help others. But the big dollar problem is error, sloppiness, and inattention to management. Much of this is caused by program designs and rules that render efficient management difficult. Where government is the problem, we need to know and then to make efficient management possible through simpler, comprehensible regulation or legislation.

The subject of this Discussion Group combines elements of all of these points. Monthly reporting and retrospective budgeting

- adjusts benefits more rapidly as income

and family circumstances fluctuate
- bases benefit calculation on actual income rather than the more error-prone concept of projected income
- gives both the client and eligibility worker a clear understanding of their respective responsibilities
- improves the quality and timeliness of program information provided to management
- provides a record of income reports that can be used if fraud is suspected.

Monthly reporting and retrospective budgeting are perhaps best defined in terms of how they compare with current practice.

- Instead of basing eligibility and benefit determinations on projected income, retrospective budgeting bases it on actual income.
- Instead of six-month redetermination of eligibility and benefit, with client reporting of changes, a monthly reporting system sends the client each month a simple mailback form that allows changes in income and family circumstances to be more rapidly taken into account.
- Finally, such a system requires automation. Altogether, this provides a device to organize efficiently the flow of information into and through the administrative system.

Monthly reporting and retrospective budgeting is a concept that grew out of the income maintenance experiments. In those experiments, monthly client report forms based on actual income were used to calculate the bi-monthly payments to be made to recipients of an experimental cash assistance plan. Among the volumes of research and analyses conducted on these experiments was a comparative analysis which taught us that the accuracy of income and family circumstance information was much higher with a regular monthly reporting system than with the usual irregular, less-frequent reporting. Somewhat predictably we also learned that recall of last month's circumstances is more accurate than projections over a future period.

The State of Colorado submitted a grant proposal to HEW to test the same administrative approach in the regular AFDC program. Preliminary research results from that test indicate significant reduction in outlays, even after netting out the increased administrative costs for computer support from the benefit payment savings.

These findings have recently led other States to submit grant proposals to conduct additional tests of monthly reporting and retrospective budgeting. We have funded planning activities for pilot tests in Boston, Massachusetts; Detroit, Michigan; Peoria, Illinois; and New York City. In addition, we have funded statewide conversion to Monthly Reporting and retrospective budgeting in Colorado and Vermont.

While I have emphasized the genesis of our interest in a highly *automated* retrospective budgeting and reporting system, the monthly reporting concept has also been developed by individual States. The best known case is California which initiated monthly retrospective reporting in 1975. More recently, several other States (among them are Oregon, Washington, Iowa, and Nevada) have adopted retrospective reporting systems that vary in the nature of the reporting requirement and the rapidity with which payments are made.

In the face of this growing interest in retrospective budgeting and the general diversity in evidence in State budgeting procedures, the Department recently drafted proposed regulations designed to clarify the budgeting procedures which States may use in their AFDC programs. The proposed regulations would permit States either to use prospective budgeting or to adopt a retrospective budgeting approach.

The comment period on the proposed regulations has just closed. We shall be revising the proposed regulations in light of the comments, prior to final publication sometime early next year.

To discuss this concept today, we have a distinguished panel of experts, all of whom have been working for the last few years with this afternoon's subject.

The format for this discussion will be as follows: Each panelist will speak for ten minutes, telling us of their interest in and relation to the concept of Monthly Reporting and Retrospective Budgeting. There will then be a few minutes for an exchange among the panelists. This should leave ample time for comments and questions from the floor.

Summary of Discussion

Eddie Schoech, Director of the Boulder County, Colorado, Department of Social Services, stated that the primary reason for his Department's involvement in the HEW-funded Monthly Reporting Demonstration in its AFDC program stemmed from the desire to find an administrative system for income maintenance

programs which would maximize financial integrity and accountability as well as service delivery. He then summarized the essential components of the system now operating in Boulder (and Denver) county: 1) a Monthly Status Report to be completed by the client and agency in a timely manner; 2) a retrospective accounting period which bases benefit payments on actual information; and 3) a high degree of automation, including cross-checks with other systems (which has led the County Department to propose integrating the Medicaid and Food Stamp programs into their system).

Mr. Schoech then summarized the first year research results, which showed a 6.1 percent net payments saving under monthly reporting with retrospective accounting, compared to payments under the conventional system of six-month redeterminations. In addition, three times as many status changes were recorded under monthly reporting as under conventional reporting; retroactive benefit adjustments decreased by 68 percent; check cancellations decreased by 76 percent; and recoveries by 78 percent. The evidence on clients' ability to handle the new system is less consistent. While 90 percent file by the first deadline of the month and 8 percent more file by the second deadline, only 40 percent of the reports filed are complete and correct. The remaining 60 percent require review by a worker, and, of those, 10 percent require follow-up with recipients.

In concluding, Mr. Schoech warned that a major problem in any monthly reporting system is the transition from the old to new system, because the change is intimidating to both clients and staff. He urged that implementation be phased slowly.

Adele Blong, Attorney, Center on Social Welfare Policy and Law, declined to debate Mr. Schoech's presentation of Colorado's experimental results, but suggested, instead, that the audience ask themselves the following question: "If my kids are hungry today, can I feed them by telling them what they ate two months ago?" The essential point, she asserted, is that we must distinguish between retrospective accounting, on the one hand, and monthly reporting and automated systems, on the other. The inclusion of retrospective accounting in the Conference agenda is symptomatic of the confusion between reporting system changes to improve information flows—an appropriate goal—and accounting period changes. She took issue with Dr. Barth's statement that voluntary reporting is the cause of breakdowns in current AFDC information systems and submitted, instead, that

the breakdowns result from the inability of clients to break through systems barriers and give the necessary information to agencies.

Ms. Blong offered some advice and warnings to those who might be considering adoption of a monthly reporting system: 1) consider the need for safeguards so that the new reporting system does not become a new procedural hurdle where those who fail to file are removed from the program (though still eligible) and spend several months trying to get reinstated; 2) take time to break in the new system slowly, assure that lack of reporting is truly unwillingness and not inability to cope with the new form; and 3) avoid adopting a retrospective budgeting period because no matter how it is constructed, client families will preceive that the money provided for the upcoming month will not necessarily reflect need or even the State standard. Finally, Ms. Blong stated that there is an awful irony in the fact that while welfare programs are moving toward modern technology to achieve efficiency and responsiveness, they are simultaneously encouraging unresponsiveness by looking backward in their accounting systems.

Kyle S. McKinsey, Deputy Director of the California Department of Social Services, related the genesis and experiences of California's four-year-old monthly reporting and retrospective accounting system. He noted that while most would agree there is no perfect budgeting system, one has to look at the range of options and the actual or projected error rates under each, in order to choose the most accurate system. The California Department determined that actual income was the most accurate determinant of a grant payment because it produces the least opportunity for over- and under-payments and less recoveries are required. Mr. McKinsey pointed out that the only cases of real concern are clients with earned income—a very small percentage of the total caseload. For those clients with no earned income, the choice between a prospective or retrospective budgeting period makes no difference.

Mr. McKinsey concluded by stating his belief that the new system is the substantial reason for a marked reduction in error rates in California. He also echoed Mr. Schoech's and Ms. Blong's admonition to phase in a new system slowly, with initial pilot tests and willingness to make continual refinements.

John T. Dempsey, Director of the Michigan Department of Social Services, stated that he is a firm, but frustrated, supporter of monthly reporting. He supports the system because the

major reasons for error are either failure of a client to report, or failure of the agency to act. Monthly reporting solves both problems. Retrospective budgeting is the most accurate, but not always the fairest or most sensitive, accounting approach. He said he favors retrospective budgeting for the vast majority of clients with a good supplements program (which Michigan has) for the remainder. Mr. Dempsey then described the source of his frustration: three years ago Michigan began a monthly retrospective reporting system for all AFDC cases in two pilot counties

(Ingham and Genesee); but because of complaints from legal services, the legislature proscribed expansion to additional counties until the cost-effectiveness of the system could be adequately demonstrated. Mr. Dempsey concluded by expressing regret that monthly reporting and retrospective accounting does not exist on a statewide basis. He expressed confidence that such a system could result in millions of dollars in payment savings, which could then be used to increase benefit levels for clients.

WELFARE DISCUSSION GROUP B:
"COMPUTER MATCHING TO DETECT/PREVENT INCORRECT PAYMENTS"

Leader

Blanche Bernstein
Administrator, Human Resources Administration
New York City

Panelists

John Allen
Office of the Inspector General
HEW

Marvin Sammon
Bureau Chief
Bureau of Collections
Iowa Department of Social Services

Wayne Carpenter
Manager, State and Local Branch
Tymshare Corporation

Staff Reporters

John J. Gallagher
Deputy Chief
Systems Development Branch
Office of Family Assistance
SSA/HEW

Richard L. Boyce
Chief, Systems Approval Section
Office of Family Assistance
SSA/HEW

Ronald J. Lentz
Acting Chief, Development Section
Office of Family Assistance
SSA/HEW

Summary of Discussion

Blanche Bernstein, Administrator of the New York City Human Resources Administration, opened the session by introducing the panel members.

John Allen, of the HEW Inspector General's Office, began his presentation by reviewing the status of HEW's computer match programs. He also noted the availability of two publications: "A Summary of Computer Matching Programs Underway" produced by the DHEW Office of the Inspector General; and the Office of Family Assistance "Report on the Use of Wage Data in the Administration of the AFDC Program." He encouraged attendees to use these publications as resource materials.

Mr. Allen described HEW matching programs in six areas:

1. *Project Match I* identified Federal employees receiving AFDC payments. Although States are currently matching AFDC Files against wage data maintained by State Departments of Employment Security, Federal employee wage data are not included in the State data base. Thus, Project Match I was undertaken.

Project Match I identified 33,000 individual cases which warranted further study. Of those cases, 18,000 are currently under review by States. Based on initial review, States report finding 1,996 over-payments and 1,875 ineligibles.

Estimated annual savings for Project Match I are in excess of $12 million (half of the savings are State funds and the remaining half are Federal funds). The Federal processing cost is $1 million. The estimated savings described above do not include indirect savings which may be realized by other welfare programs whose basic eligibility is derived from the AFDC program.

2. *Project Match II (SSI)* Compares Federal civilian employee wage data with the Supplemental Security Income (SSI) file. Results of this match will be announced in the near future.

3. *Interjurisdictional Matching (AFDC)* Phase I of this match compared 26 State and jurisdictional files to identify individuals who appear in more than one jurisdictional welfare file. The files compared were of active AFDC adult recipients as of August 31, 1977. The match identified about 9,154 cases with possible duplicate payments. Review of these cases indicated 4,462 instances of legitimate eligibility, 658 cases involved overpayments, and 222 cases of total ineligibility. Phase II of this match compared 50 State and jurisdictional files in the same manner as Phase I. The results of this phase will be available in the near future.

4. *The Summary Earnings Record (SER) Match (AFDC)* Compares State AFDC files with the SER file maintained by the Social Security Administration (SSA). The SSA has processed 13 State AFDC tapes thus far, and 5 additional State AFDC tapes await processing. In addition, 9 other States have expressed interest in this matching process. Reports on the effects of the match have been received from Franklin County, Ohio, and New York City. New York City estimates annual savings of $9.6 million and Franklin County's estimate of annual savings is $2 million.

5. *Project Cross Check* Phase I matches HEW employee files with Guaranteed Student Loan default files. Phase II matches active Federal civil service files against student loan default files, and Phase III matches active military personnel files against defaulted guaranteed student loans. Estimates of Phase I savings are in the range of $250,000 to $300,000, and Phase II savings are estimated at over $7.5 million. Phase III results will be announced in the near future.

6. *Project Integrity I (Medicaid)* Selective review of pharmaceutical and physician Title XIX (Medicaid) claims resulted in savings in excess of $6.4 million.

Marvin Sammon, Chief of the Bureau of Collections, Iowa Social Services Department, described the Iowa automated fraud referral, investigation and collection system, and the process which is used when a client is suspected of fraud and is referred for criminal investigation and possible prosecution. Fraud sanctions include either recoupment or imprisonment, or both. About 1,036 referrals are made annually (240 AFDC, 400 food stamps, 360 Title XIX providers and 36 nursing homes). These referrals result in collections of approximately $217,000 per year, at a cost of about $240,000. Despite the fact that program costs currently exceed collections, Mr. Sammon noted that the deterrent value of the system probably "scares off" thousands who would otherwise be tempted to commit fraud.

Mr. Sammon concluded by stating that his Department has a goal of savings and collections of $840,000 per year through increasing referrals and the introduction of computerized tracking and matching techniques.

Wayne Carpenter, Manager, State and Local Branch, Tymshare Corporation, commented on the supporting role that his company has played in AFDC/QC, Food Stamps/QC, Medicaid/QC, and a variety of automated tracking systems. These activities have been carried out over the last five years in 35 States.

Mr. Carpenter said that, as a citizen, he agreed with DHEW's objectives to detect, correct and prevent error, fraud and abuse in social programs. He recognized the Department's initiatives in computer matching, but noted that large volumes of data are being processed under current matching techniques. He suggested that methods must be found to reduce the size of files which must be reviewed. One approach would be to reduce file size by the use of error prone profiles constructed from Quality Control sample data. Mr. Carpenter recommended that consideration be given to using customized criteria to select small files of cases which are likely to have a high probability of matching, when compared against files like the Summary Earnings Record.

Summary of Questions, Answers and Comments

Q. John Horan, formerly with the welfare Inspector General's Office in New York, questioned the integrity of the social security number and suggested that a real problem was one of "multiple registra-

tion" where one individual receives more than one welfare grant under different social security numbers.

A. Mr. Allen acknowledged that the problem did exist and Mr. Jim Trainor, of the Office of Family Assistance (OFA), indicated that his office was attempting to determine the significance of the problem by computer matching using AFDC Quality Control data.

Comment: Richard Jensen, Utah State Auditor, said that his office has attempted to recover funds from persons who are identified as having unreported income, defaults on student loans, etc. He noted that Utah has had success in matching State income tax refunds against files of persons who owe the State money with a 10-1 benefit/cost ratio.

Comment: Dick Bakely of the Camden, New Jersey Welfare Department, commented on the difficulty in coordinating DHEW interjurisdictional data with county offices and other State agencies. Mr. Matt Marsiglia, Pennsylvania Department of Public Welfare, responded by saying that in Pennsylvania an initial review is performed at the Headquarters level. This review eliminates approximately 60 percent of the cases before they are submitted to County Offices. Mr. Allen noted that OIG is attempting to streamline interjurisdictional matches to reduce the incidence of duplicate reviews by States (lead State concept).

WELFARE DISCUSSION GROUP C: "CORRECTIVE ACTION BASED ON QUALITY ASSURANCE FINDINGS"

Leader

Sally Richardson
Deputy Commissioner
Planning and Evaluation
West Virginia Department of Welfare

Panelists

Pat Livers
Director, Bureau of Supplemental Security Income
SSA/HEW

Samuel P. Bauer
Director, Cuyahoga County Welfare Department
Cuyahoga County, Ohio

Bert N. Smith
Director, Support and Fraud Division
Vermont Department of Social Services

Staff Reporters

Judith Brundidge
Regional Liaison Specialist
Office of Family Assistance
SSA/HEW

John Marros
Regional Liaison Specialist
Office of Family Assistance
SSA/HEW

Summary of Discussion

This discussion group focused on the reduction of waste, fraud, and program abuse through positive correction actions. The panelists examined various approaches to this objective, including the use of error prone profiles, comprehensive county level planning, and state fraud units. The relationships between agencies having corrective actions responsibilities at the Federal, state, county, and local levels were considered, with emphasis on problems and solutions.

Samuel P. Bauer, former Director of the Cuyahoga County, Ohio, Welfare Department, pointed out that corrective action after the fact is not sufficient to reduce waste, fraud, and abuse; rather, preventive techniques are needed to correct these problems. Cuyahoga County found that quality assurance findings were the most logical source for identification of problem areas and the subsequent development of preventive techniques.

The County"s Corrective Action Task Force pursues an explicit process of problem identification by analyzing individual error cases. The Task Force has concluded that the "real problem" is that it is easier to get on welfare than to get off welfare; therefore, a preventive technique of con-

centrating manpower and skills at the point of intake has been developed. The County initiated a Corrective Action Project which involved subjecting approximately 25 percent of the intake caseload to a conventional rather than a simplified application method. Analysis of quality assurance findings demonstrated that five characteristics were common to most erroneous applications. As a result, all new cases with these characteristics must undergo a conventional application process requiring full verification of all eligibility information.

The five characteristics are:

- an unexplained lack of resources prior to application
- a recent separation from a spouse
- inability to verify birth or school attendance
- the presence of unrelated persons in the home
- the presence of support payments or income

In order to implement this corrective action, and develop proper staff attitudes, extensive intake staff training was undertaken. This training concentrated on review of the "prudent person"

concept, dealing with inconsistencies in information, and examining data comprehensively. The success of the county's Corrective Action Project has been demonstrated by a more than 50 percent reduction of the ineligibility rate, and by an error rate which is substantially lower than the State average. The Ohio Department of Public Welfare has accepted the Cuyahoga County technique for Statewide application.

Sally Richardson, Deputy Commissioner for Planning and Evaluation, West Virginia Department of Welfare, discussed the value of utilizing an error prone profile system at the State level. In the early 1970's, the West Virginia Department of Welfare began working to reduce fraud and abuse in the programs which it administers. After nine years of analysis, development, testing, and application, the State has produced an error prone profile which has been proposed for Federal use in connection with corrective action in the AFDC Program. The West Virginia Department developed a profile of those AFDC case characteristics which are most likely to be present in error cases. The profile also identifies those case characteristics which are likely to be present in non-error prone cases. The State's corrective action planning group utilizes these case profiles to define specific error correction actions. Corrective action steps are then formulated as desk guides for eligibility workers to use as supplements to AFDC handbooks.

Ms. Richardson noted that utilization of such profiles is invaluable as a corrective action and as a management tool. By concentrating extra worker effort on error prone cases, welfare dollars can be saved without a significant increase in administrative costs. Ms. Richardson did point out that there are some problems with this system, however. The success of the process depends on selective activity. In addition, the cost effectiveness of the system cannot be assessed unless specific corrective actions are identified and case workers implement only those specific actions.

Pat Livers, Director of the HEW's Bureau of Supplemental Security Income (SSI), reviewed the use of an error prone profile at the Federal level. From 1975 to 1977, the Social Security Administration (SSA) viewed all SSI recipients as equal. With limited staff and a large caseload, a "shotgun" approach to reviewing cases for eligibility was ineffective. In order to determine where best to concentrate review efforts, SSA turned to its quality assurance system to develop a regional error prone profile. Under this system, cases with a high probability for error will be

personally reviewed in one of SSA's 1300 district offices. Those with low error probability will be subjected to a mail contact from SSA's central office in Baltimore. The results of these mail contacts will be sampled and checked for accuracy. To reinforce the effectiveness of this selective system of concentrated review, several other data collection techniques are used to check on the accuracy of decisions:

- an "end-of-the-line" sample review of all SSI initial claims to verify the accuracy of decisions by claims representatives;
- a review of overpayment resolutions to determine the validity of decisions; and
- a review of retroactive payments of over $5,000.

In addition, in 1979, specialized staff will be assigned to deal with SSI recipients only. Ms. Livers concluded her remarks by stating that these corrective action techniques, along with the implementation of the error prone profile system in SSI, should enhance Federal program integrity.

Bert Smith, Director of the Support and Fraud Division, Vermont Department of Social Services, discussed how State fraud units can make unique contributions to the elimination of fraud and abuse in the AFDC program. Such units contribute both in the prevention and elimination of client errors, and they can work in three distinct ways toward improved program integrity:

- they lend credibility to the fact that the system works and that action will be taken to protect program integrity;
- they make direct contributions to the corrective action process through participation on the State's Corrective Action Panel and through review of proposed policy changes; and
- they participate in the training of eligibility workers in recognition and reporting of fraud, and in developing evidence necessary to prove willful withholding of information.

Mr. Smith noted that some limitations must be recognized and overcome in this area of fraud detection and prevention. Quality assurance activities will not always reveal willful withholding of information by clients. In many cases, this type of fraud is only discovered if there is an effective interface between fraud unit staff and eligibility workers. Joint training of fraud unit and eligibility staff can contribute to the creation of a team effort and the reduction of duplicated effort.

WELFARE DISCUSSION GROUP D: "CRIMINAL PROSECUTION AS A DETERRENT TO WELFARE FRAUD"

Leader

Samuel K. Skinner
Chairman, Illinois Fraud Prevention Commission

Panelists

Ellen Chestnutt
Chief Deputy District Attorney
El Paso County, Colorado

Robert E. Neilson
Director of Special Investigations
Washington Department of Social and Health Services

Paul Kramer
Deputy U.S. Attorney
Baltimore, Maryland

William T. Burkett
Inspector General
Kentucky Department of Human Resources

Jaime Cervantes
Attorney
Legal Aid Foundation
of Los Angeles, California

Staff Reporters

Dave Tomlinson
Program Operations Integrity Staff
SSA/HEW

Jerry Hockstein
Program Operations Integrity Staff
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REMARKS

Samuel K. Skinner, *Former United States Attorney Northern District of Illinois*
Chairman, Illinois Fraud Prevention Commission

I appreciate the opportunity that Secretary Califano has given me to appear before you today and to discuss my perspectives concerning the problems of welfare fraud and abuse. An examination of the list of conferees would show that most of you are either municipal, state or federal employees concerned with the problems of welfare fraud and abuse.

At this time in my career my involvement with the problems of welfare fraud is not as a paid public servant, but as a private, non-compensated citizen who has been asked by the Governor of his State to bring a private perspective to the problems of welfare fraud and abuse in Illinois. I think that before I discuss criminal prosecution as a deterrent, I should for a minute share that perspective with those of you at this conference because I think it is imperative that the conferees here today understand the sentiment of our citizens concerning these problems.

Recently a respected Illinois research firm

conducted a telephone survey of almost 800 voters in Illinois. The results of this survey identify the concerns of Illinois citizens, and I think these concerns are consistent throughout our Nation. The two major concerns of Illinois voters this year involve taxes and spending and law and order. The survey shows that Illinois voters are not nearly as concerned with rebates or even tax reductions as they are with controlling government costs. Seventy-eight percent of the voters in Illinois rated the controlling of costs a paramount issue. Seventy-two percent of those surveyed indicated they are willing to face a decrease in services in order to keep their taxes at the same level. It is not surprising that the second important issue, law and order, continues to be a major controlling issue in Illinois, but the results of the survey astonished even the most knowledgeable. The prosecution of welfare and medicaid fraud and abuse was the highest single issue of concern

to Illinois voters. It ranked higher than controlling government costs, increased state aid to education and reduced state taxes. Eighty-four percent of the people surveyed rated this issue the highest priority. I am sure that if a similar survey was taken in any large state in the Nation, the results would be the same. This result is tantamount to an indictment of the entire welfare program and those that manage it. It demonstrates clearly that the people's confidence in the administration of medicaid and welfare programs is at the lowest point in history of our Nation. It is also an indicator that unless some drastic changes are made in our current welfare systems, the public will no longer accept the concept of these programs and will on their own take drastic actions. It would not be surprising to me to see the Proposition 13 fever that runs throughout this Nation be expanded to the problems of welfare fraud. I suggest that unless something is done, and done now, by those in this room and their counterparts throughout the country, we will see a rash of binding referendums limiting Federal and State welfare spending before the end of the next decade. This action will substantially hamper the ability of any administration to deal with these very difficult problems.

I do not have enough time to discuss with you in depth the reasons that this issue is of such great concern. It is the result of many years of deficient planning, an absence of program testing, an absence of criminal and civil prosecution, as well as an unfair and inequitable administration of benefits. The inequities of our system can be best demonstrated by a story told me by one of the employees of the Illinois Department of Public Aid.

He told me of a small factory in his county which employs approximately 150 people. He told me that all employees were receiving the same wage yet some were also receiving several thousand dollars of additional funds from AFDC as well as food stamps and medical assistance. A number of others working at the same salary and who had more dependent children received no aid at all. The only difference between these two groups of people who worked side by side on the production line was that the group receiving aid had been unemployed for a period of time prior to obtaining their current job. The other group had been gainfully employed for most of their adult life. In other words, we rewarded those who didn't work and penalized those who did. The mandated Federal 30⅓ incentive program had created this inequitable situation. I have been told that similar situations exist in small factories and companies through-

out the United States. While changes to this program have been discussed for years, no action has been taken. Similar inaction is present throughout government and explains in part the public's dissatisfaction with the program.

The American people have demonstrated over the years their willingness to share their resources with others less fortunate. They have only asked that their tax dollars be administered in an efficient manner and on an equitable basis. Their desire for efficiency has never been greater than it is today and their lack of confidence has also never been so high.

As a Federal prosecutor who led an office which many people believe was a model for our Nation in the area of welfare prosecution, I assure you that an examination of the AFDC program shows clearly that many people within government do not understand the need for and role of criminal prosecution. It is impossible for the criminal system to locate and prosecute every single welfare recipient who is guilty of fraud. There is no question, however, that those who commit fraud in many cases do so knowing full well that they will go undetected. What is even of greater concern to me and to the citizens is that even when a recipient is caught, the chances for indictment are small and the chances that the recipient will receive a jail sentence are even more remote.

In Chicago over the last several years several hundred welfare recipients have been indicted for wholesale fraud on the welfare system. Last year over 90 indictments were returned in one day after a four-month investigation. Estimates have been made that the fraud detected in those cases alone amounted to several million dollars annually.

This effort was a result of a joint program between the Illinois Department of Public Aid and the United States Attorney's Office. Over 2,000 public employees were found to be illegally receiving welfare and in addition several thousand private sector employees were also uncovered.

One of the best ways to insure you have an effective prosecutorial effort is through the establishment of a joint Federal, local task force for the prosecution of welfare fraud. Much of the funding for such a program is available currently from the Federal government. The task force should include those persons within the welfare system who have the responsibilities for fraud and abuse detection. The effort in Chicago was only successful because a task force was formed with Federal prosecutors, agents of the Federal Bureau of Investigation, United States Secret Service, Department of Health,

Education and Welfare, Internal Revenue Service, Postal Inspectors and the Illinois Department of Law Enforcement. An integral part of this task force was a specially selected group of Illinois Department of Public Aid employees whose full-time assignment was the development of case histories and quality evaluation for those cases detected by computer. Local prosecutors also joined this effort on a county-by-county basis. The results in Illinois were astounding because prosecution had become a reality. An examination of some of the cases shows that some had been involved in welfare fraud for as long as ten years.

Prosecutors within your district can assist you in establishing this effort. The resources available to them are many and varied. He can communicate effectively with law enforcement officials who must in the long run assume the major responsibility for welfare fraud. The resources available to local police and prosecutors is substantially greater than the resources available to the Federal government.

Today with the accompanying publicity and massive prosecutorial effort that has occurred, those who would cheat the welfare system surely know that in Illinois there is at least a possibility they will be detected and punished—and the fear of punishment is the real deterrent. If those of you within the State and local systems have not taken the opportunity to meet your local prosecutors or United States Attorneys, I encourage you to do so. I am sure he will welcome your assistance in this very difficult area and will assist you and will provide leadership in your effort to obtain a meaningful prosecutorial program.

I must remind you, however, that prosecutorial efforts alone will not solve the problems of welfare fraud and abuse. They are merely a stop gap measure until those legislators and executives at the State and Federal level recognize that many of the welfare programs they have designed have created as many problems for the citizens of this country as they are solving. I am convinced that many of these people have no idea as to the magnitude of the problem. Because if they did they would have taken substantial action already.

I am sure I share the frustrations of many of you concerning this failure of Congress and the Federal agencies to recognize the inadequacies of the welfare programs in this country and to take appropriate action. I am hopeful that as this conference continues, those here in Washington will become fully aware of your concerns. They must learn that it is no longer enough for the Federal government to mandate programs and to provide funding. They have the responsi-

bility to make sure that the programs they mandate are effective programs which can be administered efficiently and on an equitable and fair basis. Those of you who are employed by municipal and State government are truly the men and women in the trenches. It is important, however, that as you perform your work on a day-to-day basis you identify the inequities and inefficiencies within these programs and lobby vigorously at all levels possible for change.

When you see a program which is poorly designed at the legislative level, let your legislators know. Use your employee and management groups as a lobbying force in Washington to make Congress and HEW take notice. From time to time veterans, farmers, businessmen all go to Washington in large groups from throughout the country. Maybe it is time that those public employees who have had enough of mismanagement and poor legislation use similar techniques to demonstrate the need for action. When the leadership of our country receives this message and begins to understand the magnitude of the problem and the public concern, they will harness the creativity, ingenuity and industry that has made this Nation so great and use it effectively to deal with the programs that are so badly needed by the less fortunate and the elderly in our society.

Summary of Discussion

In introducing the panel discussion, Mr. Skinner indicated that its purpose was practical in nature. The panelists hoped to provide useful guidance in prosecutorial theories and practical applications.

Ellen Chestnutt, Chief Deputy District Attorney, El Paso County, Colorado, presented the highlights of the organizational structure of her office. She expressed hope that this structure could serve as a model of an effective way to deal with fraud investigation and prosecution at the County level. Within the El Paso County District Attorney's office there is a separate Division that handles both the investigation and prosecution of welfare fraud and non-support allegations. The staff includes four employees of the local welfare department, some of whom are skilled eligibility technicians. Such organizational structure allows for specialization and expertise at all levels—from initial investigation through prosecution. This unit handles recipient, provider, and employee fraud, in addition to non-support cases.

The second area discussed by Ms. Chestnutt concerned the type of dispositions which might be expected in various types of cases. Only if

a case is very weak—witnesses out of State for instance, is restitution sought in lieu of filing. In a few instances where cases have been filed the case has been dismissed, but restitution ordered. In the majority of cases where the accused has either been found guilty or has pleaded guilty, probation and restitution are ordered. Restitution is paid through the court, and Ms. Chestnutt noted that restitution ordered and paid in this way is the most effective. In a few flagrant cases a short period of imprisonment in the county jail has been ordered in addition to probation and restitution. Such time may be ser..d either on consecutive days or perhaps on weekends. Incarceration in the State penitentiary is rare and usually imposed only in cases where previous probation has been violated. Ms. Chestnutt's concluding comment indicated that, throughout this range of case dispositions, the primary goal is law enforcement. She noted that her office has found that their operation is cost-effective, with restitutions exceeding the unit's operating costs.

Robert Neilson, Director of Special Investigations, Washington Department of Social and Health Services, briefly described the organization and operation of his office. The key element in establishing an effective operation, according to Mr. Neilson, is to have the strong support of top State officials. The support of the Governor and the Department Director in Washington have set the tone for a strong campaign against fraud and abuse in that State's welfare programs.

Another key factor in Washington's aggressive campaign against welfare fraud is the fact that such crimes are felonies in that State. Eleven percent of the convictions obtained by the Office of Special Investigations led to imposition of prison sentences ranging in length from a day or two up to 15 years. Many judges in the State have made public statements about the deterrent value of prison sentences on others who may be considering defrauding the welfare system.

Mr. Neilson's final comments focused on cases where prosecution has been declined. In these situations, restitution of funds erroneously obtained is still sought. Restitution is regularly obtained by a 10 percent reduction in any continuing welfare grant. In addition, if the individual is no longer receiving aid, the State may place liens against that person's property.

Paul Kramer, Deputy U.S. Attorney, Baltimore, Maryland, portrayed the issue and problems of welfare fraud from a Federal prosecutor's viewpoint. In a jurisdiction that has seen great emphasis on political corruption—including the prosecution of a Vice President, a Gover-

nor, and other State and local officials—welfare fraud cases can take a back seat in importance. Because of this possibility, it is often better to explore State and local prosecutorial resources. These sources often have more staff and smaller caseloads than the U.S. Attorney's offices, and more immediate attention and prosecution of welfare-related cases is possible.

Given this background, Mr. Kramer described some techniques for whetting the appetite of a Federal prosecutor for welfare fraud cases: present these cases in such a way that they will have publicity value; present them so that they will have definite deterrent value; develop an approach to combatting welfare violations that will be popular with the public. In short, suggested Mr. Kramer, find a way to capture the prosecutor's attention.

Mr. Kramer then made three specific suggestions: First, use the "cluster" approach. Instead of preparing a whole series of cases with relatively small dollar amounts, group the cases and present them all at one time. The combined numbers and dollar amounts are much more attractive from both prosecutorial and publicity standpoints. Second, look within! Internal fraud generally has greater appeal to the Federal prosecutor, than does prosecution of recipients themselves. Finally, use the vehicle of a special short-term project. Mount a 3- to 6-month campaign, including the "clustering" of cases that are found during this period. With the prosecutor's cooperation, publicize the campaign and give it a catchy name. Make sure that prosecution/restitution are used to follow through at the end of the special campaign. Such an organized attack on welfare fraud probably has the greatest deterrent value.

William T. Burkett, Inspector General, Kentucky Department of Human Resources, addressed the problems of fraud and abuse from a State "umbrella agency perspective." In his view, prosecution must be coupled with vigorous investigation to be a true deterrent. Studies have shown that the high likelihood of detection, combined with prosecution, equals the best deterrent to welfare fraud. In the same terms, restitution alone is not much of a deterrent. Persons simply view it as an interest-free loan, if they are caught. The Office of Inspector General in the Kentucky Department is a relatively new position but it has already proven to be highly effective. In a 2-month period, 300 cases were reviewed, and the first 36 cases referred for prosecution all resulted in convictions and the imposition of prison sentences. In a second jurisdiction within the State, an additional 250 cases are now pending.

As a representative of recipients, Jaime Cervantes, an attorney with the Legal Aid Foundation of Los Angeles, reflected yet a different point of view. He stated that no one is more outraged over blatant abuse, such as California's "Welfare Queen," than legal services attorneys; such abuses reflect badly on the people they regularly represent. Mr. Cervantes classified persons who abuse the system as follows: the professional thief; those who succumb to temptation and take advantage of an honest error; those who are "fed up" with the bureaucratic system; those who feel that there is no moral standard, so cheating isn't wrong; and finally, those who are truly in desperate financial need. He noted that it is very difficult to measure what will deter many of these categories of persons, since many people act before considering the consequences. Imprisonment may only provide more incentive to be dishonest as a result of contacts with others during incarceration. Most deterrents to welfare fraud and abuse probably affect only those contemplating such actions, not those already involved in them.

Mr. Cervantes concluded with comments on the system of criminal law and on the concept of welfare fraud. He expressed concern about the inconsistent handling of civil proceedings—including the fair hearing process—and criminal charges involving the same case. He also stated that we should be more concerned about recipients cheated out of their rights and out of amounts to which they are legally entitled. Such situations often occur because of the bureaucratic jumble that surrounds welfare. Mr. Cervantes urged that we learn to apply the law and regulations evenhandedly.

Summary of Questions and Answers

Q. What do you think of indictments brought against public officials in the District of Columbia lately where there was a great deal of publicity, but the charges in many instances were ultimately dropped? Where do you draw the line between publicity and the protection of personal rights?

A. Mr. Kramer: We try to be sure of the cases that we present to the grand jury. We do not bring cases simply to bring cases. It is probably better to hold publicity until after conviction rather than after indictment.

Q. Is it desirable to have Federal cases tried before a U.S. Magistrate as opposed to a full court trial?

A. Mr. Kramer: In the case of misdemeanors it is normally faster to have the cases heard by a U.S. Magistrate. Because of this the defendant may well agree to appear before a magistrate as opposed to waiting for a full trial.

Q. Are employees in your States unionized and does this require or allow union representation at hearings involving employee fraud?

A. Ms. Chestnutt: To my knowledge our employees are not unionized. This has never been a problem for us.

A. Mr. Neilson: The set of rules that my office must follow in these cases are established in the union management agreement. Representation is allowed.

Follow-up Comment from Questioner: In Pennsylvania the required grievance procedure can actually interfere with prosecution.

Q. Please give more details on the lower limit of $10,000 that some Federal prosecutors set for prosecution.

A. Mr. Skinner: This is simply one way to set priorities because of heavy workloads in U.S. Attorneys' offices.

Q. Who makes the best investigator, someone who is a law enforcement officer and receives special welfare training, or someone who is a welfare worker and receives investigator training?

A. Ms. Chestnutt: Either one is equally good; the real secret is a specialized unit that handles welfare cases only.

SOCIAL SERVICES DISCUSSION GROUP A:
"PURCHASE OF SERVICES"

Leader

David St. John
Assistant Deputy Under Secretary for
  Intergovernmental Officers
HEW

Panelists

Merle E. Springer
Deputy Commissioner for Finance and Social
  Programs
Texas Department of Public Welfare

Orlando Romero
Director, Department of Social Services
Denver County, Colorado

Geraldine Aronin
Assistant Secretary, Office of Program Planning
  and Evaluation
Maryland Department of Human Resources

Staff Reporters

Gaylord Swersky
Administration for Public Services
OHDS/HEW

Corrine Hairston
Administration for Public Services
OHDS/HEW

Summary of Discussion

Mr. St. John welcomed the group and introduced the panelists. He outlined the format for the discussion, and then listed the types of social services which are purchased through contractural arrangements. Such services include: Adoptions, day care, education, training, foster care for adults and children, homemaker services, information and referral, protective services for children and adults, case management, residential care, special services, transportation and medical related services.

Mr. St. John noted that expenditures for service programs funded through the Office of Human Development Services exceed $5 billion annually, plus another $2 billion of State and local matching funds. In addition, many State and local governments operate service programs with little or no Federal funding; hence, the overall expenditure total is above $7 billion. He pointed out that the purchase of Title XX services has grown from the 1971 level of 25 percent to the present level of 60 percent. He suggested that the group consider the following questions, particularly in relation to the rapidly growing area of purchase of social services:

1. To what extent do fraud, abuse and error exist in social services programs?
2. How do we know there is fraud, abuse, 'd error?
3. What roles can the various levels of government play in attempting to reduce fraud, abuse, and error?

Mr. St. John then polled the audience and found that about 75 percent had attended the preceding Conference Workshop on "Problems and Solutions in Social Services."

Merle E. Springer, Deputy Commissioner for Finance and Social Programs, Texas Department of Public Welfare, stated that in Texas, of the total services provided under Title XX and IV-B, between 55 and 60 percent are purchased. These services are purchased from other public agencies, non-profit providers such as the United Way, proprietary providers, and individuals. He said that the funding mechanisms for these organizations are varied and complicated. Some providers are single-purpose while other are multi-service organizations. Some have very sophisticated information systems, others do not. This lack of uniformity compounds ordinary management and monitoring problems.

Is there fraud, abuse, and error in social services programs? Mr. Springer said: "Yes, probably greater than we know. He added, however, that we should strengthen efforts to minimize what is probably the largest problem area, that of error or mismanagement. He suggested the following approaches:

1. Acquire individuals with skills to develop policies and procedures, to work closely with requests for proposals, to manage contracts, to improve the audit function, and to investigate fraud and abuse. Mr. Springer said that his Department uses investigators to look into fraud and abuse, and although some are sensitive to this approach, when used widely, such investigators are of real value.
2. Improve information systems. For example, a "providers register" designed to furnish such information as names of provider organizations, types of services, unit costs, funding sources, etc., would be very helpful to State agencies. The level of sophistication of information systems varies widely from provider-to-provider. States need fiscal and management technical assistance in this area. Mr. Springer emphasized that technical assistance should be separated from auditing efforts designed to identify weaknesses which could threaten Federal funding.
3. Broaden Title XX regulations in the area of training. In particular, service providers need training on how to be better managers.
4. Encourage technology transfer; that is, the sharing of what works well in one community with other communities having the same goals.

Orlando Romero, Director of the Denver County, Colorado, Department of Social Services, stated that their program is county-administered. He noted that the entire area of contracting for services is very complicated. Problems result from involvement of many levels of government and many individual parties. Vendors and providers are subjected to too many conditions and restrictions imposed by various levels of government, and this situation alienates good providers. Mr. Romero suggested that the contracting process be simplified. He remarked that one contract with which he had been involved took twelve months to negotiate. He also cited a day care center which should have been closed for serious licensing violations; one child served by the center died. Because of a technicality in the contract, however, the center is still operating.

Mr. Romero noted that the present system does not afford enough local participation in the beginning stages of program development. Local communities have a variety of interest groups, and while not all groups may be satisfactorily accommodated, all should be heard.

Colorado has well defined statutes on fraud and abuse in relation to money assistance programs, but not in relation to social services programs. Such programs are so subjective that it is often difficult to judge whether or not fraud or abuse is occurring. Intent is one of many factors which must be examined. Precisely when, for example, is a child in a foster home ready to be returned to his or her natural home?

Mr. Romero concluded his remarks by urging that incentives be provided to Administrators to stimulate better management. Currently, Administrators are faced with the constant threat of funding cuts. More and better resources should be made available, and soon.

Geraldine Aronin, Assistant Secretary for Program Planning and Evaluation, Maryland Department of Human Resources, questioned how much "willful fraud" exists under Title XX. In Maryland, the social services program is State administered, and $22 million of the $48 million Federal allotment is spent on purchase of services. Most of the services are purchased from other State agencies; only $1.2 million are used to purchases from non-profit organizations. Ms. Aronin listed the offices or units directly involved in the management of the purchase of services program: Legal, Compliance, Contracts, Negotiation and Monitoring (including sub-contracting), Evaluation, Research and Analysis, Fiscal and Audit. All of the above offices or units are involved in the negotiation process. In addition to Federal contracting requirements, State requirements must also be satisfied. Sub-contractors are subject to all of the requirements of first-level contractors. Providers are required to submit quarterly statistical program and fiscal reports. When problems are indicated, the cooperation of vendors is sought. Many of the offices Ms. Aronin listed are involved in this process as well.

Ms. Aronin noted that, although it is encouraging that Maryland's information systems are 75 percent developed, administrative costs appear to be climbing with the increased demand for information. Accounting systems are complicated because many providers have several sources of funding. Ms. Aronin suggested that Maryland must become more involved in aiding providers in establishing these systems. She indicated that

fees for services is an area closely watched by her State.

Currently, Maryland is involved with HEW in sensitive negotiations over the "declaration" method of eligibility, where verbal statements offered by clients are accepted. HEW has asked that Maryland conduct a quality control check on the validity of individual client eligibility. Ms. Aronin noted that Maryland is resisting this request because of uncertainty as to whether a massive quality control effort would be cost effective.

Summary of Questions Answers and Comments

Q. Ray Willis, Special Assistant on Health and Welfare, Governor's Office, New Jersey. Mr. Willis expressed disappointment at not hearing, throughout the conference, more examples of fraud and abuse and how these situations are handled. He said an auditing effort in New Jersey several years ago turned up problems with eight day care providers. He said his State prosecuted several caseworkers who received payments for foster children who were not in their care. Mr. Willis asked: "Just where does most of the fraud and abuse take place?" He suggested that possibly accounting systems are not sophisticated enough to discourage this type of activity.

A. Mr. Springer commented that in Texas there have been some prosecutions in the area of homemaker services, but they have not been extensive.

A. Peter Rinn from Kansas said that his State is investigating some Title XX providers who appear to have deliberately inflated costs, and may have engaged in deceptive practices involving the switching of funds.

Q. Gerald J. Reilly, New Jersey Department of Human Resources, said that his State has not turned up deliberate fraud or abuse, but has encountered sloppy practices. He said that when a State audits, and shares its findings with the Federal government, States are then asked to return funds to the Federal level which they often cannot recover from providers. This situation acts as a disincentive to State-level audit activity. Mr. Reilly stated his belief that the Federal government

should share such losses with a State that demonstrates a good faith effort to recover funds from providers.

A. Mr. St. John said that we, on the Federal level, are presently looking at legislation on this very matter.

Q. Jim Smith, State Representative from Missouri, said that in Missouri fraud has been uncovered in nursing homes where recipients are not receiving services to which they are entitled. Moreover, many such recipients have had their Supplemental Security Income checks stolen from them. He added that many of the providers are arrogant and that some States have chosen to take over these programs. Mr. Smith asked Mr. Springer if they investigate errors in Texas? Mr. Springer answered, "Yes."

Comment: Lou Glasse, Director, Office of Aging, State of New York, expanded on the concern expressed by Mr. Reilly of New Jersey that the Federal government penalizes States for improving systems which identify errors.

Comment: Mr. St. John stated that a more equitable system calling for the recovery of a median figure, rather than the total amount, is being considered.

Comment: Michio Suzuki, Deputy Commissioner, Administration for Public Services, HEW, commented that where States have demonstrated a good faith effort to meet eligibility requirements under Title XX, the Federal government does not attempt to recover funds. He added, however, that for whatever system of eligibility a State may use, there must be a system designed to check on and control it. In situations where a State discovers that providers did not meet requirements, monies should be recovered.

Comment: Ernest L. Osborne, Commissioner, Administration for Public Services (APS), HEW, commented on an earlier remark regarding training. Mr. Osborne said that APS is presently in the process of revising its training regulations. Attempts are being made to improve them, in general, at the same time examining the regulations with a realistic eye on provisions likely to raise costs. Mr. Osborne anticipated that this work would be completed within a couple of weeks.

SOCIAL SERVICES DISCUSSION GROUP B: "ELIGIBILITY"

Leader

Alain Roman
Human Services Division
The President's Reorganization Project
Executive Office of the President

Panelists

Gordon Bourne
Director, SPAARS Division
Colorado Office of Human Resources

Jeanne P. Johnson
Administrative Coordinator
Allied Community Services
Gainesville, Georgia

Juanita Wills
Acting Director, Program Analysis Branch
Administration on Aging, HEW

Staff Reporters

Vilma G. Guinn
Regulations Officer
Office of Policy and Management Control
OHDS/HEW

Stephen C. Grant
Management Analyst
Office of Policy and Management Control
OHDS/HEW

Summary of Discussion

Alain Roman, Director of the HEW-OMB Eligibility Simplification Project, which was announced by the President during the Conference Luncheon Session, described how the eligibility determination process is the major culprit contributing to fraud, errors, and "monstrous" government waste in welfare and social services programs. Almost $3 billion is spent each year to determine who gets what and how much—yet old people, blind or disabled people, and people who can't speak English or read, simply drop out because they can't cope with all the red tape and paperwork.

Mr. Roman pointed out that since the same rates of error of fraud and abuse continue, the problem lies with the process. The administration of welfare and social services programs is so complex and incomprehensible that applicants and workers alike are faced with almost unmanageable situations.

In order to rectify the situation, Mr. Roman said that we must *simplify the process.* Simplicity and compassion are not mutually exclusive, however. In Mr. Roman's view, the following actions must be taken:

- Establish eligibility with simple, consistent and reasonable questions;
- Find out what the applicants' real and total needs are and link them to services without red tape and wasted motions;
- Simplify and standardize terms and definitions; define a consistent accounting period for reporting income; and consolidate intake, verification, and pre-screening procedures;
- Provide incentives for improved use of automated data processes to improve efficiency and to cross check to eliminate errors and fraud; and finally,
- Develop a clear, concise Federal policy to ensure that all agencies comply with these improved and available procedures.

Mr. Roman pointed out that the review of Federal procedures affecting eligibility for public assistance programs will be arduous and frustrating. Federal codes and regulations are not only complex and confusing; they are also subject to varying interpretations by more than 100 programs operated by 10 Departments and 50 States, with oversight, budget and program legislative responsibility vested in 21 Congressional committees.

In Mr. Roman's opinion, the task is gargantuan, but doable. The HEW-OMB Project has three basic objectives: To standardize Federal eligibility requirements; to simplify the process for clients; and to assure government-wide implementation. Policy recommendations are due to the President in July. Following the President's review and approval, OMB will develop Federal policy on standard terms, definitions, and procedures for eligibility determination. In Fiscal Year 1980, agency rulemaking will begin to bring program requirements into conformity with the established Federal policy.

Mr. Roman then introduced Gordon Bourne, Director, SPAARS Division, Colorado Office for Human Resources, who described the Single Purpose Application with Automated Referral Service (SPAARS) project. The SPAARS project produced some of the basic research which the Office of Management and Budget used to design the Eligibility Simplification Project. The Community Services Administration (CSA) funded the SPAARS project in 1974 to examine the feasibility of a "single purpose application with automated referral service." A related study of Legal Constraints was conducted in 1977, and concluded that a single application was not feasible. The study found that myriad legal constraints compound the eligibility process and result in multiple interpretations in related, but administratively disjointed, human services programs, including: AFDC, SSI, Medicaid, Section 8 Housing Assistance, Food Stamps, CETA Employment Services, and Title XX Social Services.

The SPAARS Project is currently engaged in a multi-State effort to draft language options for terms and definitions found most troublesome by the Legal Constraints Study. In addition, a Human Development Services Simplification Study will describe the legal constraints affecting Human Development Services programs for older persons, handicapped persons, Native Americans, and children, youth and families.

Juanita Wills, Acting Director, Program Analysis Branch, Administration on Aging, reported on preliminary analyses comparing eligibility requirements of various Office of Human Development Services programs against each other and against Title XX social services eligibility requirements.

These analyses found that large generic programs (social security, SSI, Medicaid, Medicare, etc.), and not the categorical programs in the Administration on Aging, account for most Federal spending for older persons. She illustrated how generic and categorical programs, sharing similar purposes and objectives, inhibit coordination of aging services and make it difficult for persons in need to participate. Another problem encountered is that "services" are so broadly defined that two or more major programs may provide the same services to older persons but require different eligibility standards. This problem is not unique to aging programs. "Youth" are defined as "aged 4-25," "aged 8-13," "aged 16-22," etc. "Income" is defined through CSA poverty guidelines in one program, as "economically disadvantaged" under another, and as from "an economically disadvantaged family according to poverty guidelines established by OMB" in still another.

Jeanne P. Johnson, Administrative Coordinator, Allied Community Services, Gainesville, Georgia, provided a local perspective on the eligibility problem. Local communities must make application to multiple funding sources in order to provide needed services. Differing eligibility requirements impose hardships on both clients and staff, and perpetuate errors. For example, Head Start eligibility is based on the poverty guideline established by the Community Services Administration. The guideline is actually lower than the minimum wage, and that fact alone causes error and abuse in determining eligibility. DHEW has not updated the poverty guideline in years. The Department has indicated that updating the guidelines is the responsibility of the Community Services Administration (CSA), but CSA claims it has been too busy to do so.

Ms. Johnson stated that another part of the problem is the need for standardized poverty or income guidelines to determine eligibility. Presently, local communities must use various Federal poverty guidelines which differ considerably. She indicated that there is no way staff can be expected to deal with numerous, varying guidelines to determine eligibility without error, and no way to justify the resulting client confusion and humiliation.

Summary of Questions, Answers and Comments

Comment: Clarence Olsen, Grand Forks Social Services, North Dakota, indicated that directives from Washington would defy a good lawyer. "Food Stamps are a good example, and SSI gets the booby prize for being a program which doesn't help people in need."

Q. Frank Roddy, President, Macro Systems, Silver Spring, Maryland, said that most regulations restrict entitlement. "Changing them may mean an expanded pool of eligibles and increased costs—how can this simplification be done without expanding funds?"

A. Mr. Roman stated that savings from administrative cost cuts could be shifted to take up some increase in services.

Comment: Dr. Doris Fraiser, Office of Administration and Management, State House, Boston, Massachusetts, commented that the old philosophy of the English dole must be changed. Welfare assistance must be seen as just another system of money transfers and used as a economic development tool. She indicated that the dollar expenditure for welfare assistance makes it the biggest business in her community and this fact should be used as a positive asset. It is in the interest of the taxpayers to have everyone participating, and might also help the value of the dollar. She also related that some States, such as hers, have the tried and tested technology to interrelate services and that this interrelation can be done administratively.

Comment: Mr. Roman closed the session by stating that the President's Reorganization Project recognizes the legitimate responsibilities of State and local governments who have the primary responsibility for administering our welfare and social services programs. Hence, a conscious effort will be made to consult with State and local officials and representatives of public and special interest groups, to gain the experience and knowledge so necessary to the Project's success. As policy options are developed, outside comments and criticisms will be solicited. Without active participation by all interested parties, the project will fail.

Mr. Roman concluded: "We have the public commitment of the President that this undertaking is important to him. The rest is up to us."

CONTINUED
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SOCIAL SERVICES DISCUSSION GROUP C: "STATE AND LOCAL FINANCIAL MANAGEMENT SYSTEMS"

Leader

James A. Johnson
President
State Welfare Finance
　Officers Association;
Assistant Deputy Director
　for Fiscal and Administrative
　Operations
Illinois Department of Public Aid

Panelists

Catherine Williams
Deputy Commissioner
Iowa Department of
　Social Services

Charles F. McDermott
Comptroller, Department of
　Instituitons, Social and
　Rehabilitative Services
State of Oklahoma

Lewis A. Harris
Director, Fiscal Services
Tennessee Department of
　Human Services

Don McClure
Director, Human Resources
Jacksonville, Florida

Staff Reporters

Agnes Magnino
Grants Management Specialist
Rehabilitation Services
　Administration
OHDS/HEW

John Eger
Grants Management Officer
Rehabilitation Services
　Administration
OHDS/HEW

Summary of Discussion

James A. Johnson, President of the State Welfare Finance Officers Association, and Assistant Deputy Director for Fiscal and Administrative Operations, Illinois Department of Public Aid, opened the session by stressing the need for changing current confidentiality regulations to allow for more unrestricted exchange of income and employment information among the States, Federal Government, and private agencies. Without access to this type of information to prove or disprove client eligibility, the States have no choice but to honor assistance claims. The current lack of access frequently results in the payment of illegal claims over long periods of time until other means are discovered to determine claim validity. Mr. Johnson indicated his belief that as much as 60 percent of his Department's clients may have unreported income which might affect their eligibility for services. He then described various attempts at working with the U.S. Attorney's Office, Department of Law Enforcement, FBI, Post Office, IRS, Bureau of Education, City of Chicago, Illinois Municipal Retirement Fund, U.S. Steel, etc., to uncover fraud and abuse.

Mr. Johnson described the Illinois "direct delivery system" and highly recommended it for adoption by other States. This system provides for State warrants which are issued to financial institutions eleven times a month for cash assistance grants. The financial institutions retain the warrants for five days—during which time, clients with proper identification can pick them up. This system eliminated the problem of duplicate claims being made by clients who claimed that they never received their checks.

Ninety-four percent of the Illinois Department's total caseload is enrolled in this system. In three years, there has not been a duplicate claim case.

Catherine Williams, Deputy Commissioner, Iowa Department of Social Services, described her State's management control system and recommended its implementation by other States, volunteering technical assistance to all who were interested.

The system involves the development and distribution of three books:

- *Gold Book (Goal Book)*—Published monthly, covering items selected by Division Directors, Institutional Superintendents, and Deputy Commissioner which reflect movement toward objectives.
- *Green Book*—Contains plan for action and monitoring of stated objectives for the 16 Districts which plan, organize, and control the delivery of services at the local level.
- *Red Book (Dictionary)*—Explanation of the programs and items which are reported in the Gold Book.

This system provides managers with heightened awareness of expenditures of dollars and manpower efforts in accomplishing responsibilities of the Iowa social service programs. It also provides a means for the Social Services Commissioner to hold managers and staff accountable for their respective areas of responsibility.

Charles F. McDermott, Comptroller of the Oklahoma Department of Institutions, Social and Rehabilitative Services, stressed the need for accountability—being able to show that dollars being spent are valid expenditures, that service costs are reasonable (as related to fee schedules, other vendors' fees), and that payment does not duplicate a previous payment.

Mr. McDermott warned that there *are* vendors who will try to take advantage of weaknesses in audit systems (if there are any), and will bill for excessive fees or duplicative services. A management system must be in place which prevents vendors from taking such advantage.

Don McClure, Director of Human Resources, Jacksonville, Florida, noted that cities could teach the States and Feds something about fraud and abuse.

He discussed the importance of an internal audit section, such as the one in Jacksonville—citing the need for checking two main points:

- Eligibility as to service, and
- The capability of the individuals providing services.

Mr. McClure then described Florida's form of "government in the sunshine," introduced by Lawton Chiles. Under this system, every document (or working paper) is open to the public; every meeting or conference of two or more people is open to the media; the press have constant access to public offices (including the Mayor's office). "An interesting management situation" which keeps you on your toes, Mr. McClure stated.

Mr. McClure believes that there should be incentives for doing a good job in detecting fraud, and feels that some officials are now being penalized for "cleaning up their act." He noted that something is wrong with a system which punishes for unearthing fraudulent claims, and indicated that his city's internal audit section has 12 to 15 fraud cases now before the courts, with claims totaling about $100,000.

> *Comment:* Al Pritchett, Administrative Aide to the Mayor of Chicago, commented on a statement by Mr. McClure that some not-for-profit community organizations which were funded had not operated before or had operated without the fiscal capacity to do a good job. While Mr. Pritchett concurred with that statement to some extent, he noted that many new and effective organizations had been assisted in their development, and that these organizations had filled serious gaps in service delivery.

Mr. McClure responded that he did not intend to chastise non-profit community agencies, but merely to point out a trend. Mr. McClure noted that it's easy to predict the outcome where an organization is run by persons who have not been trained to be good managers, and many examples of these situations could be given. Mr. McClure also urged that public officials be made aware that service delivery organizations must demonstrate management competence before funds are awarded to them. He noted, however, that there can be considerable community pressure to award funds to a particular organization regardless of that organization's management ability. Hence, officials must find ways to encourage community based organizations to develop the management ability to do an effective and responsible job.

Mr. Pritchett responded by expressing his belief that public officials have some responsibility for assisting in the development of management capability by community-based organizations.

Mr. McClure agreed that assistance should be

provided, but questioned whether such assistance should precede or follow an award of funds. He noted that if the award of funds precedes the development of management competence, the organization may be in financial difficulty by the time the necessary staff training has been provided to the organization.

Mr. Pritchett noted that requiring demonstrated management capability prior to an award of funds results in situations where community-based organizations will never be able to develop their capacity.

Mr. McClure suggested that such organizations could be awarded funds and provided a grace period before strict accountability is required.

Mr. Pritchett agreed that the purchase of services from community-based organizations involves difficult decisions.

Lewis A. Harris, Director of Fiscal Services, Tennessee Department of Human Services, noted that his State has been a leader in the purchase of social services. About five or six years ago, an audit staff was developed which has grown to about 20 people. Originally, the audit staff primarily conducted audits of agencies. The first audits conducted projected an assessment of agencies across the State and found that possibly 60 to 70 percent of the funds being expended in those agencies were misused either for ineligible clients, undocumented expenditures, etc. Since then, the Tennessee Department has taken a different approach in that the audit staff provides technical assistance on the front end of contracts, especially new contracts. As a result of this approach, there are agencies which are today "models" of fiscal responsibility, where fraud and abuse had been found in early audits.

Mr. Harris concluded by noting that his Department is now developing a staff which will be primarily assigned to provide technical assistance upon the initiation of a contract. In Mr. Harris' opinion, the provision of technical assistance has been the most effective tool in improving the integrity and management of social services.

STUDENT FINANCIAL ASSISTANCE DISCUSSION GROUP A: "STUDENT PROTECTION AGAINST FRAUD AND ABUSE"

Leader

Rosemary Pooler
Executive Director
Consumer Protection Board
State of New York

Panelists

Stephen Blair
Assistant to the Deputy
Commissioner
Bureau of Student Financial
Assistance
OE/HEW

Terry Latanich
Bureau of Consumer Protection
Federal Trade Commission

Frank Jackalone
President
U.S. Students Association

Dr. James Kauffman
Vice President
University of South
Carolina at Aiken

Staff Reporter

Lynn Trundle
Editor-Writer
Office of the Deputy Commissioner
OE/HEW

Summary of Discussion

Rosemary Pooler, Executive Director of the New York State Consumer Protection Board, opened the session by summarizing the Board's recent report, "The Profits of Failure: The Proprietary Vocational School Industry in New York State." The report concludes that many vocational schools in New York use deceptive advertising, misrepresent potential job markets, enroll ill-prepared or ineligible students, and offer poor courses taught by unqualified teachers. The Board's position is that easy access to student financial assistance has made systematic deception of students not only possible but highly profitable.

Ms. Pooler then stated her belief that the U.S. Office of Education (OE) should take greater responsibility for eliminating fraudulent practices. In her opinion, OE is more concerned with "maintaining the flow of dollars" and collecting defaulted loans than it is with eliminating practices that often cause students to default. Ms. Pooler recommended that OE increase audits and take stronger disciplinary action against schools using unethical or illegal methods. This action might include regulating schools' promotional techniques, barring or suspending fraudulent institutions from participating in OE programs, and requiring institutions to pay a penalty for enrolling improperly certified students or for failing to repay funds owed to students.

Ms. Pooler concluded her opening remarks by stating that HEW should "raise questions publicly about the wisdom of funding, so-called education that fails to deliver what it promises"—that is, jobs, or at least specific training in a career field. She reiterated her belief that OE must take much stronger initiative to supervise the practices of the vocational school industry.

In response to Ms. Pooler's remarks, Stephen Blair, Assistant to the Deputy Commissioner for Student Financial Assistance, OE, noted that there should be "truth in education" just as we have "truth in lending," but this concept must be applied equally to all educational institutions, not just to one sector. Even-handed treatment must be given public as well as proprietary schools—it does little good to point a finger at one segment of education, when all are guilty of a certain measure of deception. For example, public institutions are offering careers, just as are proprietary schools. Yet, when students enroll in public institutions, they are not told about the often poor job prospects for teachers, journalists, or lawyers. Why is there no requirement that placement statistics be made available for these training areas? If a student enrolls at a public institution and then cannot attend or withdraws shortly after classes begin, he or she must still pay a considerable portion of the tuition and, in some extreme cases, must pay for the entire year. Why aren't refund policies required for public schools? Why shouldn't standards of conduct be applied to both types of institutions?

Mr. Blair continued by stating that the Federal Government cannot protect students from the results of their own choices but it can ensure that students know their rights and responsibilities so they can ask the right questions, receive answers that are not misleading, and make educational choices that are right for them. For students to make the right choices, institutions need to provide information on job prospects, the institution's retention and placement rates, its refund policies, and the availability of student aid. Students should also be told about a school's facilities, curriculum, and faculty. The Government can also ensure that its own programs are administered correctly.

Mr. Blair concluded his remarks by suggesting that the education industry must do its part to eliminate fraud and abuse by policing itself. The industry must establish and enforce standards for "truth in education" or the Government will be forced to take over more of this responsibility—and the Government's rules may be heavy-handed.

Following Mr. Blair's remarks, there was considerable debate between him and Ms. Pooler. Ms. Pooler stated her belief that "even-handed treatment" was merely an excuse for OE not supervising more vigorously the fraudulent practices of proprietary vocational schools. Mr. Blair replied that Ms. Pooler's interpretation was not his description of "evenhandedness."

He alleged that the New York State Consumer Protection Board's report was misleading, sometimes inaccurate, and was polarizing the educational community, rather than encouraging all sectors to work together on common problems and stop bad practices.

John Esposito, co-author of the Board's report, then joined the debate. Mr. Esposito asserted that the report did acknowledge that both public and proprietary schools share the same problems and suggested that the report had not been read thoroughly and carefully. The discussion continued, but was inconclusive, with Mr. Esposito defending the report and Mr. Blair questioning the validity of its data.

Terry Latanich of the Federal Trade Commission's (FTC) Bureau of Consumer Protection, discussed possible Federal Government actions to help protect students against fraud and abuse. Mr. Latanich described a forthcoming FTC regulation aimed at controlling some vocational school practices. The regulation covers four areas of student protection:

1. Vocational institutions must provide dropout and graduation rates to students.
2. These schools must provide placement data to prospective students, that is, the percentage of a school's graduates who are successful in obtaining jobs. (Mr. Latanich noted that even graduates presently unavailable for placement must be included in these data.)
3. The use of sales personnel to promote a school's course will be regulated to help ensure the honesty of these persons. Included in this provision is a controversial pro rata refund policy: a student would pay only for the portion of the course completed; the rest of the tuition would be refunded to the student.
4. Before a contract with a vocational school becomes binding, there will be a 14-day "cooling off period," during which a student may withdraw if he or she chooses.

Frank Jackalone, President of the U.S. Students Association, discussed the growth of student consumerism in the 1960s when students began to question whether education was meaningful. As the concept of institutions serving *in loco parentis* decreased, students began to take a more active role in determining what they wanted from education and from educational institutions.

Because students have begun to ask more

questions, better information is needed about student financial assistance, and all entities need to work together to provide that information: institutions, States, the Federal Government, and students themselves.

Mr. Jackalone recommended increased student involvement in accreditation and in the governing bodies of institutions. He noted that students must believe that they can obtain answers from their institutions about financial aid, especially since many financial aid application forms are confusing. Finally, Mr. Jackalone recommended establishing an appeals mechanism to act on the grievances of students who believe they have been cheated.

Dr. James Kauffman, Vice President of the University of South Carolina at Aiken, stated that negative publicity about abuse should be counteracted, and honesty, integrity, and accuracy emphasized. In his view, increased training for financial aid officers and higher institutional authorities should emphasize the importance of proper aid management. Better communication among institutional, State, and Federal levels would also help eliminate abuse and error.

Dr. Kauffman urged student and educational organizations and OE to develop a joint statement of principles on student financial assistance. He suggested a statement that encompasses the rights, responsibilities, and resources for students, including student rights to: 1) accurate and timely information, 2) humane and responsive treatment; student responsibilities to: 1) submit accurate information, and 2) discharge all legal obligations; and student recourse to: 1) institutional grievance procedures, and 2) governmental adjudication processes.

Summary of Questions, Answers, and Comments

Q. Bernard Erlich, legal counsel for a number of proprietary school associations, asked Mr. Latanich if the problems found in proprietary schools were not also found in public schools.

A. Mr. Latanich replied that both sectors shared similar problems, but there was less abuse in public schools. He said that, although the regulations currently applied only to vocational schools, he hoped they would eventually cover public schools.

Q. Joel Packer, Legislative Director of the U.S. Students Association, asked Mr. Latanich if the upcoming reauthorization of higher education legislation should include the FTC's reforms among its requirements.

A. Mr. Latanich stated that he was not involved in that area, but including the reforms might be a good idea.

Q. The Director of Vocational Schools for New York asked whether the FTC excluded public schools from its regulation because it has no authority to control them.

A. Mr. Latanich replied that this was one consideration, but not the primary one; the FTC simply believed the two types of schools were different.

STUDENT FINANCIAL ASSISTANCE
DISCUSSION GROUP B:
"INSTITUTIONAL ACCOUNTABILITY"

Leader

Dr. Robert M. O'Neil
Vice President
University of Indiana—
Bloomington

Panelists

Dr. Francis Finn
Executive Vice President
National Association of College
    and University Business Officers

Peter Voigt
Director, Division of Policy
    and Program Development
Bureau of Student Financial
    Assistance
OE/HEW

Lawrence E. Braxton
Director of Student Administrative
    Services
Charles R. Drew Medical School
Los Angeles, California

Dr. Guadalupe Quintanilla
Assistant Provost
University of Houston
Houston, Texas

Staff Reporter

Keith Stanford
Program Analyst
Bureau of Student Financial
    Assistance
OE/HEW

REMARKS

Lawrence E. Braxton, *Director of Student Administrative Services, Charles R. Drew Medical School, Los Angeles, California*

Good afternoon, I am Larry Braxton, Director of Student Administrative Services at the Charles R. Drew Postgraduate Medical School in Los Angeles, California. Among the responsibilities of that job is the direct supervision of the Financial Aid Office. I am the current President of the California Association of Student Financial Aid Administrators and a member of the Executive Council of Western Association of Student Financial Aid Administrators. These two associations boast of a combined membership of more than one thousand committed, concerned and active financial aid administrators and I have received their approval of the remarks I will deliver here this afternoon.

By entitling this group of discussions, "The Secretary's National Conference on Fraud, Abuse and Error," the onus for these conditions is placed directly on the heads of educational institutions and upon the heads of those who, in this instance, administer financial aid programs. Briefly, I will attempt to refocus some issues concerning the matter of Institutional Accountability.

I would be the last person to deny that there have been some instances of the maladministration of the federal financial aid programs by institutions of higher education. But so have there been such instances of maladministration within the Office of Education, within the executive branch, within the legislative branch and within the judicial branch of our government as well. Causes of maladministration are numerous; however, I would like to share with you my perceptions of a few of those causes.

First, nearly all of us from time to time hear about or read about some institution which is either in the process of being disqualified from participating in the programs, or has been disqualified from such participation. However, many institutions adopt the attitude that "it could never happen to us." Unfortunately, given the history of OE follow-up on problem program reviews and audits, that attitude may have some validity. Many of us who consider ourselves to be competent financial aid administrators have heard of cases of abuse and fraud where we, as peers, would have disqualified some institutions from participation in federal financial aid programs. However, we also hear that those institutions still receive more funds that will probably be similarly misused or misdirected, or institutions are given the opportunity to "negotiate" repayment. Being allowed to negotiate a $10,000 settlement when hundreds of thousands of dollars have been misused hardly encourages other institutions to toe the line.

Second, educational institutions, though they are a lot of other things, are a business. Each year, just like United States Steel and General Motors, they have to balance their books and make a report to the shareholders, whether those shareholders are a corporate board or the regents of some statewide system. One of the formidable costs of operating any business is the cost of labor.

It is sometimes out of consideration of cost that institutions hire barely qualified and totally untrained persons to administer those functions not considered "essential" to the academic excellence of the institutions. By so doing, labor costs are minimized. Among those "unessential" positions often falls the institutional financial aid administrator. We all know that, year after year, the financial aid director is listed either second from the bottom or third from the bottom when salaries of educational administrators are published in the *Chronicle of Higher Education*. Hiring an unskilled and untrained employee to administer programs as complicated and as complex as federal financial aid programs is itself an injustice. But that injustice is twice cursed when neither the institution nor the federal government allocates funds to the financial aid office so that these persons can avail themselves of meaningful training experiences and attendance at conferences where their skills can be enhanced.

Much of the problem surrounding this phenomenon of using unskilled labor bears directly with the cost of administering these programs and the amounts and manner in which the administrative allowance is paid to institutions to help offset the cost of such administration. As you might be aware, institutions receive an administrative expense allowance that is equal to 4% of the dollars loaned, awarded or earned by students participating in the National Direct Student Loan Program, the Supplemental Educational Opportunity Grant Program, or the College Work Study Program. This amount, no matter what the dollar volume is that an institution handles, is woefully inadequate. It is of particular concern to financial aid administrators that the Congress has not seen fit to appropriate funds for administrative expense allowances for the Basic Grant Program and the Guaranteed Student Loan Program. Has anyone from the Office of Education ever tried to approximate the real cost, from an institutional point of view, of administering the BEOG Program? Though the administrative burden may be less at a "typical" four year undergraduate university which only enrolls full-time students during quarters, semesters or trimesters, the administrative burden is increased geometrically when the institution is a community college which charges no tuition or low tuition and which must monitor enrollment for thousands of students on, sometimes, a monthly basis to escape the possibility of having to collect vast sums of money in overpayments. Is that burden any less for the proprietary school that enrolls students in programs of six months, nine months, and 15 months duration, and enrolls a new class each month? What about the Guaranteed Student Loan Program which recently included in its regulations a statement that *individuals* must be counseled about the benefits and obligations incurred prior to the making of a loan? How much does that cost?

Let us take a look at the cost of operating a well administered financial aid program in 1977-1978 at a California liberal arts college with an enrollment of 3350 students, 1248 students received federal campus based funds in that year and the dollar volume was $1,381,408. Total expenditures for all financial aid programs including state, federal, institutional and private sources of funds totaled $7,800,000. Administrators at the institution sense that no less than 85% of the time spent in administering all financial aid programs was spent admin-

istering the campus based programs, although the campus based dollar volume represented only 17.7% of total financial aid expenditures and students receiving campus based funds represented only 50.3% of students receiving financial aid. Administrative costs incurred are:

Operating Expenses, Financial Aid Office (includes salaries, supplies, equipment, etc)	$111,677
Operating Expense, Computer Center	21,328
Operating Expense, Fiscal Office	12,514
Operating Expense, CWSP Placement & Payroll	12,000
Total Cost of Operation	$157,519
Federal Cost of Operation (85% × $157,529)	133,891
Administrative Expense Allowance	$55,256
Institutional Cost	78,635

Some schools just can't afford that kind of added expense, especially public schools in the post-Proposition 13 era in California.

This brings me to my third observation. The cost of administering the federal financial aid programs is excessive. Excessive regulations cause greater administrative headaches, necessitate more staff and more expense, and cause more resentment of federal intrusion into the internal affairs of educational institutions. Much of this could be ameliorated through the establishment of a committee that could allow for input into the regulatory process *before* the issuance of Notices of Proposed Rulemaking. Perhaps if you, Department of Health, Education and Welfare, would sit down with some knowledgeable financial aid administrators, share with us whatever it is *that you want to do and tell us why you want to do it*, we might be able to suggest means more acceptable to members of our profession. After all, it is us, not you, who feel the daily impact of these words tht you put down on paper.

The fourth observation that I wish to share that affects institutional accountability is the *inconsistency within the Bureau of Student Financial Assistance* when it comes to responding to questions of policy and procedure from institutions participating in your programs, and the misuse by BSFA of the process whereby regulations are put into effect. It has often been said in one of the regions which shall remain unidentified that, were a financial aid administrator to call the four different program administrators in that region and pose the *same question to each* of them, four different, specific answers would be given. Well, the new Office of Education devised a

method that would do away with that. The financial aid community was told that policy interpretations can only come from the central office. BSFA then published phone numbers and names of specific persons to contact about specific kinds of problems. The only problem is that the phone numbers are, by and large, incorrect and names of contacts have changed due to the weekly reorganizations of the Office of Education, and it still takes unusually long periods of time to get an answer to a written inquiry.

On the issue of the regulatory process, the General Provisions Regulations which were approved by Congress in 1972, define that process. To my knowledge, this is the latest update of those procedures. The timing of interim and final regulations have been falling upon us at odd and mysterious times. We have consistently written to OE about their time frames and have complained of the procedures that have been used. More recently, we have complained substantially about the procedures that will be used in this year's allocation of campus based funds; however, I think again, you can see from the November 8th *Federal Register* that the final rules and regulations were signed off on August 23rd by the Commissioner of Education, and I have found out that they were also completed on *August 25th by the Assistant Secretary for Education*. It's particularly interesting to note, however, that the Secretary had not signed on these rules and regulations until October 27, 1978. This delay coupled with the final publication of the rules, in essence insures that the procedures were not even distributed until well after the thirty days, when institutions were required to have their total applications in.

The financial aid community has just this past week, in addition, finally received the expected family contributions that are to be used in the formulas which are not even included in the November 8th publication. This type of regulatory procedure must certainly be changed if we are expected to respond in a positive and thorough manner. In spite of our continued complaints about the process, nothing has changed. We are now down to our last, unpleasant recourse, that being to notify our congressional representatives of the kind of bureaucratic redtape that we are experiencing in trying to administer the programs that they enacted.

I am here today deeply involved in the spirit of this gathering, that being to determine processes and procedures that will minimize the opportunities for maladministration of taxpayer dollars, my specific interest being in the area of federal financial aid programs. In summation, I would like to make a general statement about

the beleaguered Financial Aid Administrator, and I would like to offer recommendations directed at the four points that I have raised concerning not only institutional accountability but OE accountability as well.

Sometimes it appears that those members of the federal bureaucracy whose duty it is to regulate the will of the Congress seem to forget the various roles of the institutional financial aid administrator. He must, first, be an advocate for the student. He must be a representative of the Office of Education. He must be an employee of his institution. He must be a representative of his state if that state has its own financial aid programs. He must be a counselor. He must be an accountant, and above all he must be able to see clearly through muddy water and see at least twelve months into the future. So many of the regulations he must effectively work within are directed at particular institutions where there is fraud, and there is abuse, and this manner of "worst case" regulation requires all kinds of extra and unnecessary work to be imposed on the conscientious institution where these problems do not now and never have existed.

I leave you with four recommendations:

1. If and when all legal processes have been exhausted and it is determined that an institution or an individual has criminally maladministered federal funds, then that individual should be punished to the fullest extent provided by law.

2. Pay a reasonable administrative expense allowance. We appreciated the increase from 3% to 4%. We would like to see it raised to 8% which is the administrative expense paid to institutions for administering such programs as Upward Bound, Talent Search and research grants. An administrative allowance for processing Basic Grants and Guaranteed Student Loans is a must. Not including the added burdens of the much maligned validation process (we do not disagree with the concept of validation, just the process) some 23 separate and distinct administrative actions had to be taken in the Basic Grant award, disbursement and reporting cycle. Add on to that the time consumed in the validation process and even the OE recommended administrative allowance of $10 per basic grant recipient does not even cover half the cost of managing this program. The same can be said about the time and paperwork

requirements inherent in the Guaranteed Student Loan Program.

3. Stop legislating and regulating against the worst possible instances of maladministration. Prior to beginning the regulatory process, sit down with some of us who are just as concerned as you are about maladministration. Share with us what it is that you wish to accomplish through the regulations. Maybe we have some workable ideas that can be used to meet your need without creating excessive burdens on the 95 plus percent of institutions who honestly carry out the intent of the regulations to the best of their abilities. You might use the NAS-FAA Title IV Committee for such liaison.

4. Do whatever it is that you can so that the public is not presented with an image that "many" or "most" educational institutions are guilty of fraud, abuse and error. The problems are with a few, and it would be in the best interest of all of us if that point were unequivocally presented to the public. And, last but not least, make whatever real, reasonable, honest and meaningful attempts that you can to put your own house in order.

Summary of Discussion

Dr. Robert M. O'Neil, Vice President of the University of Indiana-Bloomington, opened the session by characterizing the present student financial aid community mood on campus as "a time of anxiety." He noted that because of the rapid changes taking place in financial aid programs, student aid administrators often are apprehensive and even paranoid about government. It is, therefore, important to distinguish which of these concerns are ephemeral and which are more substantial.

Dr. O'Neil pointed out that tension between government and academia over academic autonomy is not new. The Dartmouth College case of 150 years ago, for example, resulted in the legal establishment of academic independence. The higher education community's response to outside requirements also has longstanding historical precedents; the founding of the accrediting associations was cited as an example.

Dr. O'Neil continued, citing the importance of situations where demands had been placed on academic institutions for accountability. The Morrill Act was an early instance of the establishment of the concept that some obligations may

legitimately be imposed on campus from outside.

Dr. O'Neil stressed the great fragility of academic independence, however, since academic institutions frequently lack the power of other institutions to resist unwarranted intrusions. He noted that there are Constitutional limits applicable to some cases of illegitimate pressures for accountability. Pressure to reveal names of students who had participated in "civil disturbances" was cited. Dr. O'Neil commented that demands for accountability were now coming from students and parents, and not merely from government. As an example, he mentioned demands for refunds during school closings at the time of the Cambodian invasion. Dr. O'Neil also cited as noteworthy the proposals now being circulated by educational institutions for increased self-regulation. He stressed the irony that it was now conflict between academic institutions and *government* which demanded creative resolution, rather than the conflicts between campus officials and students which were commonplace during the 1960's. Dr. O'Neil concluded his remarks by urging the clarification of methods, strategies and, to some extent, expectations as government and academia move toward closer cooperation over student financial assistance.

D. Francis Finn, Executive Vice President, National Association of College and University Business Officers (NACUBO), stressed the importance of management training and good management data for financial aid personnel. Mr. Finn stated that many have forgotten the enormous size of financial aid programs and the speed with which they have mushroomed. He cited efforts by his own association—the NACUBO accounting guides and their manual on loan collection—as examples of personnel training and data provision tools. Mr. Finn added that his Association is developing a financial aid guide to be published in the Spring of 1979 which will be aimed at presidents and vice-presidents of educational institutions.

The discussion group audience responded strongly when Mr. Finn stated that campus decision makers must be made aware that student financial aid is no longer a minor subject which can be shuffled to subordinates. He concluded his remarks with observations on some specific cases of Federal unreasonableness. He urged that Federal officials consider the 99 percent of schools which are honest, rather than the 1 percent which are not, in preparing regulations. The regulatory requirement of separate bank accounts for certain student financial aid funds was cited as an example of Federal concentration on "worst possible cases." Mr. Finn urged greater sharing

of accountability by Federal officials and stressed the importance of regular meetings with campus student aid officers.

Lawrence E. Braxton, Director of Student Administrative Services, Charles R. Drew Medical School, Los Angeles (prepared remarks on Page 92), stressed that his work with the California association of student financial aid officers (over 800) had provided him with considerable "firing line" experience. He then questioned the assumption that financial aid officers are mainly at fault for all of the problems in student financial aid. Mr. Braxton saw his mission as one to "re-focus blame" and cited conditions which should be noted in assessing difficulties in the financial aid community:

- First, criminal acts must not be "forgiven," but prosecuted fully.

Mr. Braxton cited instances of government officials making settlements with certain schools of large amounts of money owed to the government.

- Second, an administrative allowance of at least 8 percent must be paid, as opposed to the present 4 percent limit in some aid programs. In addition, administrative allowances must be paid for the BEOG and the Guaranteed Student Loan Programs.

Mr. Braxton cited data from his institution as evidence of the administrative expense of student aid programs and as proof that current administrative allowances are too low. The serious consequences of inadequate administrative allowances include the invariably low salaries paid to financial aid officers and the resultant inability to recruit experienced and skilled persons for those positions.

- Third, regulations must be published with far greater advice from student aid personnel, with greater attention to timely publication and with greater access to policy guidance once regulations have been published.

Mr. Braxton cited as inexcusable a two-month delay by the Office of the Secretary in approving a recent set of regulations. He also noted that the telephone numbers of OE and HEW officials from whom student aid officers might seek policy guidance were badly out of date and/or wrong. Mr. Braxton stressed that, above all, regulations must not be drawn up with the "worst possible cases" in mind.

- Fourth, Mr. Braxton lamented the tendency of government and the media to imply that all, or even many, schools are participants in fraud and abuse. He stressed that the opposite was, in fact, the case and that the public should be informed that the vast majority of schools perform well.

Peter Voigt, Director of the Division of Policy and Program Development in OE's Bureau of Student Financial Assistance, remarked on the amazing extent of agreement about what constitutes the problems in student aid. He noted the major future increases in the flow of monies and students which will take place in financial aid offices as the middle income student aid program comes into effect. Projections have shown that as much as 70 and 80 percent of some student bodies will be recipients of student financial aid. Mr. Voigt emphasized that this coming quantum increase in student aid programs means putting the student financial aid house in order on every level—from educating campus decisionmakers on the magnitude and importance of the problem, to allocating funds for sufficient office equipment and materials.

Mr. Voigt also touched on numerous areas which had been cited as problems. He emphasized that while the regulations process was still far from perfect, it has been shortened and simplified. He noted instances of consultation with financial aid associations and pointed out that public comments were being aggressively sought and carefully considered. In fact, the regulatory comment process led the Office of Education to reconsider its requirement of separate bank accounts for certain student aid funds. Mr. Voigt also cited instances where program regulations were being consolidated and simplified. He commented at some length on the BEOG validation process. He observed that there seemed to be a general consensus that it was a very worthwhile effort, though one that must be streamlined and improved. Mr. Voigt concluded by observing that much of the public dismay and outcry over student financial aid scandals has, in effect, become public insistence on academic quality; and that dropout incidences of 80 percent, as have been the case in some schools, simply had to be reduced through self-policing by educational institutions.

Dr. Guadalupe Quintanilla, Assistant Provost, University of Houston, presented some of the results of a study she had conducted among 17 institutions of higher education in Texas. Her study touched on such questions as: how financial aid officers define institutional accountability

to the Federal government, who should set standards of institutional accountability, and who should have main responsibility for enforcement of accountability standards. In addition, operational questions which affect financial aid programs on campus were posed, including: whether upper level administrators were aware of the importance of aid programs and responsive to the programs' needs; whether management problems were receiving adequate attention on campus; and whether adequate resources were being provided to the financial aid offices. The results of Dr. Quintanilla's survey revealed almost total confusion about what "institutional accountability" was, although there was agreement that accountability had thus far been defined too much by the government. The aid officers felt that the schools themselves should play a much stronger role in defining accountability standards. The responses to questions about the operational adequacy of aid programs were distinctly unfavorable. The lack of qualified financial aid officers and lack of administrative funds were often cited, as were more prosaic problems with inadequate space and supplies. Dr. Quintinilla stressed that the study revealed that upper-level administrators on 16 of the 17 surveyed campuses simply *did not know* about financial aid programs. The survey also revealed strong feelings among student aid officers against the small minority of actual fraud and abuse cases and a consensus among aid officers that such cases should be left to the Department of Justice.

Summary of Questions, Answers, and Comments

Comment: Thom Brown of the Illinois Student Financial Aid Officers Association, said that the *aid officers* felt abused, and his comment drew widespread audience agreement. He supported his claim with a detailed elaboration of problems he had experienced with staggering numbers of student eligibility reports. He strongly recommended that government consider alternative methods of verifying income; including new legislation, if necessary, to obtain the information inter-governmentally, i.e. directly from the Internal Revenue Service.

Response: Mr. Voigt responded that it was indeed useful that the legislation for the student aid programs was expiring, so that such suggestions could be considered in recommendations for new legislation.

Comment: A representative of the Ohio Student Financial Aid Officers Association suggested a high-level letter to top administrative officials to cue them on the enormous importance of the new student financial aid legislation.

Response: Mr. Voigt responded that just such a letter was being drafted, and pointed out that a "President's Column" had been created in the BSFA Bulletin. He also stressed that top BSFA officials had been speaking regularly at appropriate meetings of school officials.

Comment: Bob Pike of the Nebraska Student Financial Aid Officers Association laid additional stress on the need for administrative funds.

Comment: Dr. Quintinilla pointed out that her survey showed that 13 of 17 institutions have done absolutely nothing to prepare for the new middle income legislation.

Comment: Walt Martin of the Texas Student Financial Aid Officers Association emphasized that the problem of 80 percent of students at some campuses getting aid was going to catch colleges totally unprepared.

Comment: A North Carolina Student Financial Aid Officers Association spokesman stressed the importance of mundane details—filling cabinets, for example—so as to give higher level campus officials a better sense of the flood of students implied in the new legislation.

Comment: Mr. Finn declared that he thought it especially important for those who had spoken about undue government interference to take upon themselves the job of raising the consciousness of campus decision-makers. Members of the Texas and Mississippi Student Financial Aid Officers Associations echoed similar themes. The Texas Association had contacted every institution in the State but received a general response of "there just isn't any money for this." A similar situation was cited in Mississippi.

Summary of Panelists' Concluding Remarks

Dr. Quintanilla suggested the Tables in the November 6 Bulletin of the National Association of Financial Aid Administrators as excellent data for convincing school administrators of the impact of the new legislation.

Mr. Voigt stressed a commitment to work with student aid associations and recapitulated accomplishments which have already taken place.

Mr. Braxton cited the general sense of inundation which aid administrators had experienced with the Basic Educational Opportunity Grant program during the past year. He suggested that the Office of Education needed to carefully develop planning models as the student financial aid community—government and schools alike—takes on new programs or activities.

Mr. Finn stressed that his Association's publication list of 10,000 (as well as his own personal participation at such places as ACE) would convey the messages discussed during the session.

Dr. O'Neil noted that the discussion had been useful and had sharpened some issues. He adjourned the session by observing that the Conference should perhaps have been called the "Secretary's Conference on Fraud, Abuse, Error and *Penury*."

STUDENT FINANCIAL ASSISTANCE DISCUSSION GROUP C: "INSTITUTIONAL SELF-POLICING —VOLUNTARY ACCREDITATION"

Leader

Dr. Lloyd Elliott
President
George Washington University
Washington, D. C.

Panelists

Charles B. Saunders, Jr.
Vice President for Governmental Relations
American Council on Education

Dr. Alfred L. Moye
Deputy Commissioner for Higher
 and Continuing Education
OE/HEW

William Goddard
Executive Secretary
National Association of Trade
 and Technical Schools

Dr. Thurston E. Manning
Director
 North Central Association
 of Colleges and Schools
Commission on Institutions
 of Higher Education

Staff Reporter

William Moran
Chief, Policy Section
Basic Grant Branch
OE/HEW

Summary of Discussion

Dr. Lloyd Elliott, President of George Washington University, opened the discussion with a brief historical summary of the development of accrediting agencies as institutional self-policing organizations. From the time of establishment of the first institutions of higher education in the American colonies, an informal exchange of information occurred among them. Through general, unstructured exchanges, the particular strengths and weaknesses of each were known to all. By the nineteenth century, several hundred colleges had been founded in the United States, and a need was perceived for more formal, organized means of exchanging information. The result of this need was the establishment of regional accrediting organizations, with member institutions located in specific areas of the country. In addition, other accrediting agencies were established for institutions in specific fields, such as medicine or law; and these agencies might have a national membership rather than one limited to a particular area of the country. Currently, the activities of the modern multipurpose university may come under the supervision of a number of accrediting agencies.

Self-policing through accrediting agencies developed in the United States because there is no centralized ministry of education to perform that function. As a result, we have a great diversity of educational institutions, and these institutions have had the opportunity to grow and expand without the restraint of rules emanating from a centralized governmental agency.

Charles B. Saunders, Jr., Vice President for Governmental Relations of the American Council on Education, emphasized that institutions must act vigorously to strengthen self-policing mechanisms for preventing fraud and abuse. Institu-

tions have a fundamental interest in maintaining the accreditation process and in keeping it free of Federal intervention.

Thet idea that the Office of Education should assume a more dominant role in policing institutions is a Federal response to concern about massive amounts of funds institutions receive through various Federal programs, and the need to ensure that these funds are properly used. The Office of Education does not know all of the problems that exist in the abuse of student aid programs. Despite offers by the higher education community to assist in defining problems and seeking solutions, the Office of Education has not sought much assistance from that source. The Office of Education has had the tendency to use the bad examples of a few institutions as the basis for regulations governing all institutions. Thus, the Office of Education's response to the bad actions of a few has been the creation of an administrative burden for all. This type of Federal response could become unnecessary if institutions would vigorously police themselves. Thus, the higher education community should resist Federal efforts to establish policies on fraud and abuse; rather, such policies should be established by institutions themselves through the accrediting agencies.

Dr. Alfred L. Moye, Office of Education, Deputy Commissioner for Higher and Continuing Education, noted that there is a triad of agencies which share interest in the prevention of fraud and abuse. The triad includes: State approval agencies, accrediting agencies, and the U.S. Office of Education. Dr. Moye pointed out that the basic thrust in fraud and abuse prevention must be self-policing by each individual institution. The more actions taken by individual institutions, the less action necessary by the triad of agencies. The Education Amendments of 1976 gave the Office of Education the authority to limit, suspend or terminate student aid institutions programs which fail to comply with program regulations. However, the Office of Education first encourages institutions to regulate themselves. In this connection, the Office of Education stands ready to assist accrediting agencies in developing institutional self-regulating procedures.

William Goddard, Executive Secretary of the National Association of Trade and Technical Schools, stressed that the best prevention of fraud, abuse, and error is achieved through a cooperative effort by institutional accrediting agencies, State licensing agencies and Federal agencies. Full implementation of such a cooperative effort requires better communications among these three components than currently exists.

For example, State agencies need a greater degree of involvement.

Mr. Goddard concluded by stating that in dealing with fraud, abuse, and error, more guidance needs to be provided to institutions in preventing error. In his view, if error could be reduced, reductions in the incidence of fraud and abuse would follow.

Dr. Thurston E. Manning, Director of the North Central Association of Colleges and Schools, noted that in attempting to correct abuse, care must be taken to ensure that the correcting mechanism does not itself cause abuse. As an example, he cited a new Federal Trade Commission regulation on tuition refunds. This regulation, in Dr. Manning's view, will ultimately cause hardship by resulting in increased tuition charges for students who do not drop out. Thus, sanctions in regulations may ultimately harm the wrong party. As a further example, the Office of Education's Limitation, Suspension, and Termination regulations may intend sanctions against institutions, but may ultimately harm students.

Dr. Manning asserted that the determination of educational quality is a professional judgment and cannot be made through pre-established criteria contained in a regulation. He noted that the rapid growth of Federal student financial aid programs has had a significant impact on American higher education. More than 50 percent of students currently enrolled in postsecondary education programs depend on a single financing source for their educational costs. With this point in mind, it is important that self-policing be strengthened, or, the aid source may assume the policing role.

Summary of Questions, Answers, and Comments

Comment: Richard Stillwagen, of the Missouri State Department of Education, noted that a problem of program abuse arises when an "otherwise reputable institution" establishes a program of questionable educational merit such as a "life experience program." He felt there was a need for careful examination of new programs by accrediting agencies.

Response: Dr. Manning responded, agreeing that accrediting agencies should be apprised of all programs offered by member institutions and should determine if they meet the general standards maintained by the institution.

Q. Mr. Saunders asked what trigger mechanism would cause an accrediting agency to begin an investigation of an institutional program.

A. Mr. Goddard responded by saying that some accrediting agencies require notification by member institutions of each new program and the accrediting agency then conducts an on-site review.

A. There was a general agreement among the panelists, however, that given the number of institutions and the rate at which new programs may be established, accrediting agencies have difficulty in responding in a timely manner

Comment: Sister Anne Elise Tschida, President of the Minnesota Association of Financial Aid Administrators, suggested that perhaps accrediting agencies should, as a matter of practice, make an evaluation of the administrative capability of financial aid officers.

Responses: Mr. Saunders indicated that some

accrediting agencies are already undertaking efforts to provide training and technical assistance for financial aid officers and other college administrators He expressed approval of this trend.

● Dr. Moye agreed that more emphasis needs to be placed on training for college administrators.

● Mr. Goddard added that lack of sophistication, not incompetence, is the issue involved. He urged that student financial aid administration should not be seen as a new profession requiring certain entry-level qualifications. Rather, emphasis should be placed on providing more and better training for the existing financial aid office staff.

● Dr. Manning agreed, noting that the financial aid programs have grown dramatically in a relatively few years, and people who formerly held other posts in college administration are now administering large amounts of financial aid funds.

STUDENT FINANCIAL ASSISTANCE DISCUSSION GROUP D: "STATE FEDERAL COOPERATIVE RELATIONSHIPS—ROLE OF STATE POSTSECONDARY LICENSING AGENCIES"

Leader

Dr. T. Edward Hollander
Chancellor
State Department of Higher Education
State of New Jersey

Panelists

George Arnstein
Education Consultant
Veterans Administration

Ernest E. Smith, Jr.
Executive Director
Florida Student Financial
    Assistance Commission

John R. Proffitt
Director, Division of Eligibility
    and Agency Evaluation
OE/HEW

Steven B. Friedheim
Executive Vice President
Association of Independent
    Colleges and Schools

Staff Reporter

Norman B. Brooks
Chief, Policy Section
Division of Policy and Program Development
OE/HEW

Summary of Discussion

Dr. T. Edward Hollander, Chancellor of the New Jersey State Department of Higher Education, began the discussion by noting that although the prevention of fraud and abuse is important, it is less important than assuring the overall good health of postsecondary institutions. In this context, the principal importance of preventing fraud and abuse is to protect the credibility of higher education, because credibility is linked with taxpayer willingness to pay.

Fraud and abuse extend into areas other than financial. Among these are:

1. Offering substandard programs (e.g. a master's degree in clinical psychology in States where a doctorate is required for practice).
2. Encouraging enrollments in programs of study for which job market opportunities are limited (e.g. teaching).

Dr. Hollander suggested that better consumer protection should be developed to help prevent abuses in these areas, as well as those in purely financial areas such as refunds.

Requiring institutions to offer full and complete disclosures of information is one approach to the needed protection.

Disclosure of information cannot, however, assure minimum levels of quality. Quality assurance is a job that the States can do; it is within their constitutional powers. While some States are currently exercising these powers, others are not.

Dr. Hollander concluded his remarks by noting that the American Institutes for Research (AIR) had recently issued a report on various State practices in this area, and a number of the report's recommendations deserve support. Among those recommendations is one that the Federal Government should provide financial support to State agencies which have legal authority to license institutions. The States and the Federal Government have a mutual interest in protecting their financial investments in higher education, and the States still make the major resource commitment to the support of such education. Hence, the Federal Government can most effectively protect its financial interests by helping the States protect theirs. Institutions cannot provide high-quality educational programs without also practicing financial accountability. The States have the constitutional authority to require that educational programs be of high quality. By helping them do so, the Federal Government will be helping to protect its own financial interests.

George Arnstein, Education Consultant to the Veterans Administration (VA), began his remarks with a quotation from Max Cleland, the Administrator of Veterans Affairs. The quotation stated, in effect, that VA has helped more students and disbursed more education funds than anybody. It has also dealt with more fraud.

Mr. Arnstein then noted that problems with fraud in the original (World War II) GI bill led to some of the changes enacted in the Korean G.I. bill.

He stated that nobody knows the dimensions of fraud and abuse. The diversity and pluralism in higher education, and the deliberate policy of encouraging their continuance, make it difficult to establish standards which will prevent fraud and abuse. Such diversity and pluralism also prevent outside agencies from interfering in the internal affairs of colleges.

Mr. Arnstein listed several lines of defense against fraud and abuse:

- State licensing (which is variable, as the AIR report shows).
- Private voluntary accreditation.
- State approval, which can be combined with State licensing. The VA provides financial support to States to help them operate their approval systems.

He noted that none of these three has been very effective. To help improve their effectiveness, we need:

1. Training. Courses and workshops should be developed.
2. Better communications.
3. Simplification and consolidation of Federal programs.

4. Leadership. Who's in charge? Nobody currently has an explicit mandate.

Mr. Arnstein concluded by observing that what appears to be fraud is frequently nothing but error based on misunderstanding.

Ernest E. Smith, Jr., Executive Director of the Florida Student Financial Assistance Commission, noted that all institutions are eligible for OE and VA programs, implying that eligibility criteria do not screen out undesirables.

Mr. Smith then stated that Florida first began licensing postsecondary schools five years ago. At first, efforts were primarily devoted to enumeration; merely compiling lists of schools in operation. Lately, standards have been raised, and inadequate schools have been closed. At present, however, licensure is no guarantee of quality or honesty.

Mr. Smith commented that a double standard is something used in dealing with proprietary schools. Public and private nonprofit schools are given preferential treatment.

Mr Smith asserted that, from an investment standpoint, we should not finance training in oversupplied occupations, such as teaching. Investors such as States and lenders wish to minimize risks; hence, effective State licensure which assures quality education in fields for which there is a demand could stimulate the supply of GSL funds.

Finally, Mr. Smith observed that the Federal Government has been inconsistent in delegating responsibilities to States. It should not delegate and forget; rather, it should require the States to do the job right.

John R. Proffitt, Director of the Office of Education's Division of Eligibility and Agency Evaluation, distinguished between accreditation and legal authorization. Both are conditions of institutional eligibility.

In the past, because of great variance in State laws the Office of Education has not been able to place sufficeint reliance on the State authorizing function. Mr. Proffitt indicated that OE plans to work more closely with the States to bring about changes which would justify increased reliance on State law in determining institutional eligibility. It is necessary to know whether the institution has integrity and quality

Of the 7800 U.S. institutions eligible to participate in OE programs, 7000 are accredited or hold pre-accreditation status. The other 800 comply with statutory alternatives which are equivalent to accreditation. All 7800 are legally authorized to operate in a State, but State requirements for granting legal authorization to operate vary.

Mr. Proffitt asked how the Federal Government

could best assist States in improving their licensing requirements. Should grants be awarded to State licensing agencies, as recommended by AIR? Should States be encouraged to evaluate both the academic quality and the fiscal integrity of institutions? These two characteristics are inseparable.

Mr. Proffitt observed that States generally say that they do not want Federal funds with strings attached. However they generally accept the proposition that they need help to do a better job.

To improve Federal/State cooperation in assuring quality, Mr. Proffitt suggested that new relationships are needed. In addition, grants are needed for training, development, demonstration, information systems, and specialized needs.

Steven B. Friedheim, Executive Vice President of the Association of Independent Colleges and Schools, stated that, from an institutional standpoint, student financial aid programs are complicated to administer. His association turns to Dallas Martin for counsel when it needs assistance. (Mr. Martin is Executive Secretary of the National Association of Student Financial Aid Administrators.)

He noted that part of the problem of fraud and abuse is the fact that student financial aid officers turn over too fast. Institutions don't pay enough to get and keep people of the quality needed.

Mr. Friedheim asserted that simplistic approaches to the problem are often the wrong ones. For example, the dropout rate is not necessarily a good measure of an institution's output —the dropout rate of an innercity community college does not measure the same underlying factors as the dropout rate of Dartmouth.

Mr. Friedheim agreed with previous speakers that most of the problem of fraud, abuse, and error is error. However, fraud and abuse capture headlines; error does not.

He also agreed with Mr. Smith's observation that there is prejudice against proprietary institutions and their accrediting agencies.

Mr. Friedheim concluded by expressing concern that the FTC's new regulations may be difficult to comply with.

Summary of Questions, Answers, and Comments

Q. Harold Orlans, Senior Research Associate at the National Academy of Public Administration, raised the question of how much "Fraud, abuse and error" is error.

A. Richard Hastings, Acting Deputy Director of the Division of Certification and Program Review in the Bureau of Student Financial Assistance in OE, offered figures based on reviews of 460 institutions. All 460 institutions were selected for review because of known problems. About 25 to 30 percent involved abuse. Mr. Hastings defined "abuse" as intentional error which is not indictable.

Q. Mr. Hastings' comments caused a lively audience response. Several additional questioners sought clarifiation. One questioner asked for examples of abuse.

A. Mr. Hastings replied that it is hard to give examples of abuse, because it is difficult to determine exactly where to draw the line. One example offered was misuse of restricted Federal funds.

Q. Other questioners asked whether Mr. Hastings' figures shows that 60 to 65 percent of cases of error were based on misunderstandings, rather than fraud or abuse.

A. Mr. Hastings replied that they did.

Q. Al Reynolds, Inspector General for the Veterans Administration, stated that a number of vocational technical schools have been successfully brought to prosecution in the last two years. The source of knowledge about the problems in these schools was not the regular licensing process. He asked whether we have 4 to 5 years to preclude some of these schools from operating.

A. Dr. Hollander replied that we've created our own problems. States have created a diversity of licensing agencies. OE recognizes too many accrediting agencies. No clearly defined accountability is placed on the State. We should pinpoint responsibility. The Federal Government could establish standards that States would have to meet. If a State did not do so, institutions in that State would not be eligible to receive Federal funds.

Comment: One commenter stated that the bulk of the abuse that has been identified has been in public junior colleges.

Q. There was considerable discussion of statements by two of the panelists to the effect that insufficient use has been made of the

statutory requirement for licensure. That requirement has been in the VA statute since 1954. (A comparable requirement was in OE's original student aid statute, which was Title II of the National Defense Education Act of 1958.)

A. Dr. Hollander replied that the real issue is that of guaranteeing that students receive an academically adequate education, and preparation for a viable career. With reference to proprietary schools, those which offer well-established, high-quality programs should be supported. Others should not be. The Federal Government should demand that the States be accountable for exercising their legal authority to permit institutions to offer programs of post-secondary education.

Q. Mr. Friedheim asked Dr. Hollander whether his statement concerning preparation for a viable career implied restrict-

ing course offerings when labor market demand declines. If so, Mr. Friedheim said, that should also apply to teacher training.

A. Dr. Hollander agreed emphatically that it should.

Q. Mr. Proffitt was asked several technical questions concerning the eligibility of various schools. One concerned the eligibility of foreign schools. The questioner noted that American students attending foreign schools can be found eligible for a Guaranteed Student Loan if the school is comparable to an eligible school within the U. S.

A. Mr. Proffitt described the procedures used for determining comparability and referred to forthcoming regulations concerning foreign medical schools. Those regulations are being jointly developed by OE and PHS.

Introduction of the Honorable Jim Wright

By the Honorable Joseph A. Califano, Jr., *Secretary of Health, Education, and Welfare*

Ladies and gentlemen, the Dallas-Fort Worth Metroplex has produced two great institutions well-known for their power over Washington: the Dallas Cowboys—and Jim Wright.

And Jim Wright's won-loss record is better.

Indeed, as Majority Leader in the House of Representatives, Jim Wright is to Speaker Tip O'Neill what Roger Staubach is to Tom Landry. The only difference is—Jim Wright gets to call his own plays.

It is especially fitting that Jim Wright should be our speaker this evening.

For not only does he bring to the platform the wit and sparkle and story-telling skill that we associate with his region; he also brings the insights of a public servant with a deep interest in human wellbeing.

Jim Wright came to the Congress as a Progressive, devoted to liberal goals and programs that help people; he has pursued these goals in a tough-minded, prudent way. He combines compassion and intelligence—a worthy goal for us all.

I'm sure I'm not telling you anything you don't already know about power in Washington. But when Jim Wright accepted our invitation to give the keynote address of this Conference, the President of the United States had to settle for speaking at lunch.

Ladies and gentlemen, the Majority Leader of the House, Jim Wright.

REMARKS

Honorable Jim Wright, *Majority Leader, U.S. House of Representatives*

After an introduction like that I think any lawyer worth his salt would be well advised just to rest his case. It has been observed, and appropriately, I think, that there are only two kinds of people in the whole world who appreciate flattery . . . that's men and women! Undeserved though it is, I want you to know I enjoyed it.

We in the Congress are vitally concerned and greatly interested in what it is that you're doing here. It's unique in many respects, and, of course, it is one of those things in which the American public, and, therefore, those of us in the Congress who represent the American public, have a vital and personal interest.

I'm tempted to tell of an episode that occurred a few years back. Jere Cooper of Tennessee was Chairman of the House Committee on Ways and Means, the tax writing committee, the tariff writing committee, the committee that has to do with Social Security, and that has something to do with hospital cost containment and legislation of that kind; probably the most prestigious post in the House. And, there was a fellow who will remain nameless because he later came to Congress, though not on that particular occasion, who ran against Jere Cooper in the Democratic Primary in Tennessee. And his standard speech as he made it up and down the byways of small country towns in Tennessee went something like this. He said, "Now everybody knows that the way a Congressman helps his people is to get hisself put on a committee where he can render service to the District. Yea, Jere went up there to Congress . . . he could have got hisself on a committee to help y'all out down here in Tennessee . . . but what did Jere do? Did he get hisself put on a public works committee . . . where he could build you all some dams, and some roads, and build some public buildings to help out the economy of this region? No sir, he didn't get hisself on no public works committee. Jere could've got hisself put on a agriculture committee, done something to help your own farmers get a better price for your crops. Jere didn't get on a agriculture committee. You know what Jere got hisself put on? Jere got hisself put on what they call a Ways and Means Committee! That's the committee that figures up all the new *ways* and *means* to get in your pocket and raise your taxes! And Jere, he was so good at it, they made him the Chairman of the Committee!"

Well, I'll tell you, when Secretary Joe Califano spoke up publicly last March about the subject of waste and abuse in his own Department, he committed an act as courageous as it was unusual in these parts . . . almost as though Macy's had invited the public to find out about all the great savings they could find available at Gimbels. Almost as though the Cowboys had offered to the Redskins their book of plays the week before the game.

Will Clayton once told me a story that occurred when he was Director of Lend Lease during World War II. He said his Russian counterpart came into his office in a very stern way one day and announced, "I have come to tell you, you are behind in your shipment of jeeps; you're behind in your shipment of tanks; and we want it corrected." And Will Clayton said, Well, I'm glad you brought that up because we have a report that says there are 75 tanks on the boat landing at Murmansk, there are 150 jeeps that haven't even been uncrated from the rail yards at Leningrad and it's you who are behind; it isn't we who are behind." The Russian drew himself to his full height and said, "I did not come to talk of our behind, I came to talk of your behind."

I don't think ever before, in my recollection, has a Cabinet officer of our government suggested the possibility that six-billion dollars a year could be saved by tightening up the controls against fraud, waste and abuse in his department. You know, a lot of people are awfully good about talking about savings that could be made in other programs . . . but very few of us can speak of savings that might come about in our own department. I think it was unique in the annals of administrative government.

Well, the news, of course, had an electrifying effect upon the public. Many, of course, quickly forgot that it was Califano who had brought this disclosure to them initially and remembered only vaguely that some reliable source had revealed six-billion dollars of waste and fraud in the Department of Health, Education, and Welfare, and pretty soon some of them were blaming it on Califano. A few even began to demand his resignation because of this great waste that was said to go on in his Department.

And it wasn't very many months then before Congress, certain members of Congress, at least, were proposing broad, deep, across-the-board slashes in the budget for labor and HEW appropriations based upon the now accepted axiom that the Department was wasting six-billion dollars a year. They ignored the fact, of course, or overlooked the fact that most of the potential savings that had been pointed out by the Inspector General's report, commissioned by, and reported by, Secretary Califano, had been directed to changes that could be brought about by legislation. And,

they hadn't, we hadn't and still haven't . . . brought those changes into effect . . . not many of them.

Well, certainly, most emphatically, if it is possible to save six-billion dollars a year, or any substantial part of it, all of us, Congress and the Administration together certainly owe it to the Nation to do whatever is necessary to bring those changes into effect.

The Secretary has identified some two-billion seven-hundred million dollars which he believes is capable of being saved by tightening up administrative procedures . . . without changes in the law . . . and he thinks that a massive, diligent application of effort at this juncture might save one-billion one-hundred-million dollars this year . . . Fiscal 1979. Well, it's to begin the implementation of that that he's called this Conference. If the effort is to succeed, I'm convinced that it has to have the voluntary and innovative help of State and local agencies through the country, learning from each other, and not expecting each to submerge its individuality, its identity, so that it is no more than a pale carbon copy of all the others, nor to be only a sort of a cynical competitor in a game of grantsmanship. It will take the efforts of all of us.

Now those of us from my State of Texas are not really noted for our modesty, though we're very proud of our humility down there. I suppose I ought to correct a gross misimpression that's abroad in the land; a lot of people have a wrong notion about Texas—a lot of people think that all Texans are rich, uncouth, swaggering braggarts; and, it isn't true at all. We're not all rich, by any manner or means. But, I do think that we can take justifiable pride in an effort begun by the Texas Department of Human Resources in 1974, a pioneer effort at rooting out waste and fraud and abuse in the welfare program.

Since that effort began in July of 1974, the Department in Texas has succeeded in recovering more than eight-million dollars in payments obtained under fraudulent circumstances; has chalked up some 1,000 criminal convictions; and 4,000 restitutions from people who attempted to defraud the government under the Aid to Families with Dependent Children program. And in the Food Stamp program there have been more than 1,000 convictions and 7,000 restitutions. There have also been convictions against two doctors, 17 pharmacies, and one nursing home.

I am very pleased with the able professional who heads that Department. Jerry Chapman is here with us this evening, and I want to take this occasion to salute him and those who have worked diligently with him in that Department,

and others in other Departments throughout the country who already have begun on what is, I think, one of the most exciting prospects for the American taxpayer and public administration.

Addressing a Conference of this kind has got to be a pleasure because I know that I am talking with people who are committed to the idea of making America work. I know that each of you is committed to the proposition expressed so well by President Carter, to the end that we can have a humane welfare program that is both compassionate and competent, and that we can prove that it is possible to eliminate waste and abuse without eliminating 50 years of social progress.

In hardly any other function of our government are the strengths and weaknesses of the American public so clearly seen or thrown into such bold relief as they are in the programs that many of you administer.

Here we see the greatness and generosity of the American character . . . and we see the beginnings of a self-destructive rot which must be expurgated.

It reveals a stingy meanness at the economic top when national banks absolutely protected against loss refuse to extend government-guaranteed student loans because they can get higher interest rates elsewhere.

It reveals widespread retreat from responsibility, an alarming thing to me, when students in wholesale numbers assume bankruptcy to avoid repaying those guaranteed loans.

Something is grossly wrong when a small community is penalized for asserting civic responsibility, raising money by a local subscription to begin work on a badly needed hospital, rather than waiting passively for a Federal grant.

Something is fundamentally amiss in administration when guidelines and regulations become so detailed and so exacting that local units cannot comply with them, or when compliance adds greatly and unnecessarily to costs, or when red tape becomes so rampant that people would simply rather not deal with the Federal government at all.

Something's wrong when the young people tell you, as a few have told me in the last couple of years, that they can't afford to take a job at modest pay.

The American people are a generous and humane people—they have never resented helping the helpless. They want their Nation to do that, and do it graciously, but to preserve the dignity of those who must look to society for subsistence. But they do certainly, and increasingly, resent paying for programs that they believe are wasted; programs that don't do the job for which

they are intended; and particularly, for any program that provides a disincentive to work. If I correctly interpret the mood of the American people, it is essentially this: People do not believe that Government owes everyone a living, but they do believe that a society as rich as ours emphatically owes to every American the opportunity—the real opportunity—to earn a living.

In the past two years we have made enormous strides in reducing the unemployment that beset this country when this Congress and this Administration began. We have reduced the unemployment rate since January of last year by more than two percentage points—from a little more than eight percent of the work force down to slightly less than six percent of the work force. Six-million more Americans have found gainful work, and it isn't as though they've all been employed by the Government—far from it! Eighty percent of them have found work in the resurgent private sector of our economy. Now that's cause for rejoicing. And as a matter of plain fact, as the President pointed out the other day, and may have mentioned to you today, because of this increase in employment, and the availability of jobs, the welfare rolls have been reduced by one-million, three-hundred-thousand people.

But there lingers a problem which is relatively new to our society; what has come to be called structural unemployment, fed by chronic unemployability. There are families which now are in the second generation as welfare recipients. Some have never worked, and unless something is done to give them marketable skills, perhaps never will work. That's a situation that shouldn't be tolerated. It is this that your agencies deal with and are going to have to deal with increasingly.

The newly emerging problem, it seems to me, is the number of people who are out of the mainstream of American society, and who lack either the means or the incentive to get into it. Some, of course, are disabled and can't work. We must provide adequately and generously for them. There are some who have the responsibility of caring for small children. We cannot leave them stranded. But there are some who are able bodied and could be providing productive work in society; and for them to remain idle serves neither them nor the public who must carry the burden of supporting them.

It's a condemnation of our imperfect efforts that thus far we have failed to enact a comprehensive welfare program that will recognize the distinction between these two groups—the unemployables and the employables— and treat each as it deserves to be treated: the unemployable with a combination of compassion and understanding, and the employables with a combination

of opportunity and discipline.

I think President Carter does recognize this in working with the Congress. He hopes to enact a welfare program that will be equitable to welfare recipients; give relief to State and local governments; provide job training and economic incentive to get people off the unemployment rolls and onto private payrolls; and reassure those who want to see an end to fraud, waste and abuse in the existing welfare program.

Of course, you are familiar with his proposal; cash payments for those who are unable to work; jobs for those who can, training to transform as many as possible of the former into the latter.

It has been my experience in Congress that the big reforms, significant bills that change public policy in very important ways, usually take time. I know there has been a degree of cynicism which has grown up over the idea that welfare reform has been around so long that it really is never going to go anywhere. When you stop and realize that civil rights took a good many years of steady effort—when we enacted the civil rights bill in 1957, it was the first one in 75 years; Medicare took about 15 years; Federal aid to education was around at least 10 years as an active issue before it was enacted; five years after the Arab oil embargo, we still are struggling to build all the components of a comprehensive energy program for the Nation; and now it's been nine years since President Nixon first proposed what he called the "Family Assistance Plan," which, with variations, has been recommended to us from time to time by each succeding President. I think the time may be approaching when the issue is likely to be resolved; at least, when we make a serious beginning on its resolution—simple economics dictates the necessity for a solution.

Ten years ago, income security—that portion of the Federal Budget which includes unemployment compensation and welfare, in general— accounted for less than half the amount that the military budget consumed. In 1970, the beginning of this decade, it was about 40-billion dollars— the military budget was about 80-billion dollars. Well, in 1974, income security had passed defense as a Government cost item, becoming the most costly item in the budget. Last year it was 37 percent higher than the total budget of our defense establishment . . . up from less than 40-billion dollars in 1970 to 159-billion dollars, compared to the 116-billion for National defense. Now not all of that, nor indeed a majority of that, was consumed in the welfare programs that you administer; I think the biggest part of it was Social Security . . . and increases in Social Security, of course, are understood by all of us. But let's look briefly just at those welfare programs.

In 1969, as part of Federal dollars, those programs we identify strictly as welfare programs accounted for about 2½ cents of each taxpayer's dollar. In Fiscal 1979 they come to about 6.2 cents out of every taxpayer's dollar. Now, what I'm suggesting is that the Nation simply cannot afford to perpetuate chronic unemployability, nor can we afford a hodge-podge system which in some cases makes it more attractive for a person not to work, than to work.

Every percentage point of unemployment generates an adverse impact upon the Federal budget, in the equivalent now of about 22-billion dollars. Let me say that again— every time we tolerate an increase of 1 percent unemployment in the Nation's work force, we automatically add some 22-billion dollars to the National debt. Now the reason for that isn't too hard to fathom if you just stop and realize that first of all people who are not working are not paying taxes. And every time unemployment goes up by 1 percentage point, the Government loses approximately 17½-billion dollars that it otherwise would receive. In addition, the Government assumes responsibility for paying about 4½-billion dollars in unemployment compensation and related welfare costs.

The taxpaying public is entitled to the assurance that their money is not being used to keep people out of the mainstream of American life. That's why I think we have the responsibility to put together a combination of packages: we've got to support job training to make every able-bodied American employable; we need a restructuring of the welfare program to make it more financially attractive for every employable American to work and to learn the dignity and self-respect that comes from making a contribution in this society. That would help us to afford the truly compassionate and humane assistance which a civilized society owes to those of its number who for reasons of age or health or disability or family requirements simply cannot be expected to work.

I think in many ways the American dream was different from that of any other major country. Unlike other civilizations, we set out from the beginning neither to bring down the nobility nor to install it as a permanent ruling class. Unlike the French and Russian revolutions which sought to destroy the aristocracy and set up instead a dictatorship of the proletariat, the American Revolution sought something entirely different— to expand the aristocracy—to make it available to the humblest citizens.

And that's what we've tried to do. The American dream has been of a decent life for every citizen—an emancipating life—a life of dignity that gives rise to all the great promise that lies

locked up inside the humblest human creature. Any welfare system that ignores man's spirit and his potential for self-esteem is doomed to failure.

Vachel Lindsey said it well when he wrote:

"Let not young souls be smothered out before
They do quaint deeds and fully flaunt their pride.
It is the world's one crime its babes grow dull,
Its poor are ox-like, limp and leaden-eyed.
Not that they starve, but starve so dreamlessly,
Not that they sow, but that they seldom reap,
Not that they serve, but have no gods to serve,
Not that they die, but that they die like sheep."

May we find wisdom in the ancient Chinese proverb which says, "If you give a man a fish, you've given him a meal. If you teach a man to fish, you've given him a life."

And in this season when we celebrate the birth of one who came that we might have life, and have it more abundantly, may we find the grace to do justice, and to love mercy, and to walk humbly with our God.

I. THE ROLE OF AUDITING AND ACCOUNTABILITY — PANEL A- "ACCOUNTING SYSTEMS AND INTERNAL AUDITING: THEIR ROLE IN THE PREVENTION OF FRAUD AND ABUSE"

Moderator

Edward W. Stepnick
Assistant Inspector General for Auditing
OIG/HEW

Chairperson

Donald L. Scantlebury
Director, Financial and General Management
Studies Division
U.S. General Accounting Office

Panelists

Robert J. Freeman
Professor of Accounting
University of Alabama

Martin Ives
First Deputy Comptroller
New York City

James Harmeyer
President
Institute of Internal Auditors

Staff Reporters

Tom Robertson
HEW Audit Agency—Region III
Philadelphia, Pennsylvania

Frank Zuraf
HEW Audit Agency
Washington, D.C.

Summary of Discussion

Edward W. Stepnick welcomed the audience, briefly described the general purpose of the Workshop, and introduced the members of Panel 1 on "Accounting Systems and Internal Auditing: Their Roles in the Prevention of Fraud and Abuse."

Donald L. Scantlebury, Chairperson of Panel 1 then announced that a number of prepared questions would be posed to each panel member. Following the responses of the panelists to these questions, discussion would be opened to the audience.

Before beginning the questions and answers, Mr. Scantlebury reiterated two key points which were contained in Comptroller General Staats' remarks on December 13 (see P.12):

1. It is more beneficial to prevent fraud through front-end controls than to attempt to catch a thief or abuser after the fact.
2. Auditors have not devoted enough effort in the past to fraud and abuse matters.

Mr. Scantlebury then began the question/answer period. (Since the following questions and answers deal largely with internal controls, it might be helpful, for those who may not be familiar with accounting theory, to reprint the following textbook definition of internal control:

"Internal control comprises the plan of organization and all of the coordinate methods and measures adopted within an entity to safeguard its assets, check the accuracy and reliability of its accounting data, promote

operational efficiency, and encourage adherence to prescribed managerial policies.")

Question 1:
What is wrong with existing accounting controls? Is Government as far along as the private sector in this area?

Answers:
- (Martin Ives, First Deputy Comptroller, New York City): The Federal Government does well, especially in internal auditing—however, it emphasizes delivery systems over controls and perhaps might do well to have more CPA attest audits in the financial area.
- (Robert J. Freeman, Professor of Accounting, University of Alabama): The focus has been on internal auditing—professional auditing/accounting associations have lagged behind in emphasizing need for better internal controls.
- (James Harmeyer, President, Institute of Internal Auditors): We need to define internal controls. The Institute of Internal Auditors has started a crash project to do this and hopes to publish results by this spring.
- (Mr. Scantlebury): Controls are better in the private sector. Many Government audits don't pay attention to financial controls. Improvement is needed here.

Question 2:
Do we need new internal controls in the computer age?

Answers:
- (Professor Freeman): No—computer systems may be complicated, but a better understanding of the systems would make internal controls more workable.
- (Mr. Ives): Audit needs to recruit persons with understanding of computers. This would help audit to better understand computer systems.
- (Mr. Scantlebury): Philosophy of internal controls remains unchanged. They need, however, to be adapted to complicated computer systems.

Question 3:
What about collusion? Can anything be done by management to prevent two or more employees from conspiring to defraud?

Answers:
- (Professor Freeman): With computers we don't need two or more perpetrators—one person can pull off a theft.
- (Mr. Harmeyer): There is no easy approach to this problem. Two possible solutions include 1) rotation of personnel in sensitive areas such as procurement, and 2) team purchasing (which, in effect, allows for a peer review of actions).
- (Mr. Scantlebury and Mr. Ives): Mechanisms might be established to detect aberrant patterns which might indicate abuse in certain areas. Auditors cannot avoid the responsibility of detecting fraud or abuse.

Question 4:
What can be done to tighten existing internal control systems?

Answers:
- (Mr. Ives): We might hire specialists, e.g. engineers, who can help with evaluations by physical observation of end products.
- (Professor Freeman): In the past, management would only react to a crisis situation and after a number of crises we wound up with a patchwork internal control system. We need to change this, start over and develop new well-thought-out systems.
- (Mr. Scantlebury): We need to work more work more closely with management systems experts.

Question 5:
As auditors, do we need to perform more surprise audit tests?

Answers:
- (Mr. Harmeyer): As internal auditors—yes. As external—no. Because of adversary relationship between external audit and client this would not be healthy. (Mr. Scantlebury added that GAO requires notification of the auditee 10 days prior to start of audits.)

Question 6:
What can audit do to get its internal control recommendations accepted by management's responsibility in this area?

Answers:
- (Mr. Ives): Prime responsibility for good controls is management's. "We need tough managers who worry."
- (Mr. Harmeyer): Management should be sure to supply necessary resources. In the private sector the Foreign Corrupt Practices Act requires, in part, that management ensure controls are in place to protect against bribes of foreign officials and such. Strict penalties are imposed for failures in this area. Perhaps the Federal Government needs similar law re management controls?

Question 7:
What can be done to make management more receptive to audit's recommendations?

Answers:
- (Mr. Ives): A good personal working relationship with management helps. Other aids: some auditors are legislative auditors who can influence other arms of government (such as GAO). Other auditors may have a vote on budget matters. This provides plenty of clout.
- (Professor Freeman): Recommendations should be "clearly the right thing to do" and material in relation to total operations. Also, timely audit reports are important.
- (Mr. Scantlebury): It may help to use horror stories (sensationalism) to make a point.

Summary of Additional Questions, Answers, and Comments

Comments: Art Gordon, an auditor with the State of New York, noted in New York comparative analysis and physical observation are used as audit techniques, That is, by observation and using good common sense, an auditor can detect potential abuses of government programs.

Q. Tom Tulley, of the Office of Program Integrity in New York, asked Mr. Ives, "What to do you do to encourage management in New York City to establish internal audit groups?"

A. Other than through Mr. Ives' office, which he considers the City's internal audit group, there is little or no review of this type at the various Departments. There is a danger that certain units within a State or local government may want too many auditors, but overall the use of this review mechanism is encouraged.

Q. Bill Wilkerson, of the HEW Audit Agency, asked what role program complexity played in the occurence of fraud and abuse.

A. Mr. Ives warned that we shouldn't be overawed by complex programs. They are often not that difficult to attack, if taken one piece at a time. This approach requires a familiarity with and understanding of programs.

A. Mr. Harmeyer added that although internal control systems were generally more adequate in the private sector, the Federal and State Government auditing groups are the ones who are developing sophisticated new audit techniques. They've had to be innovative, he said, in order to attack the complex problems they face.

In concluding the discussion, Mr. Scantlebury noted two points which, in his view, were quite clear:

1. There is a need for more emphasis on auditing international controls. Particularly, auditors need to think more about fraud and abuse, and its prevention, when performing audits.
2. Managers should be made more accountable for maintaining sound internal control systems and practices, an important aspect of responsible management.

I. THE ROLE OF AUDITING AND ACCOUNTABILITY—PANEL B· "THE AUDITOR'S RESPONSIBILITY FOR THE DETECTION OF FRAUD"

Moderator

Edward W. Stepnick
Assistant Inspector General for Auditing
OIG/HEW

Chairperson

Frank Greathouse
Director of Audits
State of Tennessee

Panelists

William Klenk
Comptroller
City of Philadelphia

Donald R. Ziegler
Chairman, Subcommittee on Perpetration and
Detection of Fraud
American Institute of Certified Public
Accountants

Edward W. Stepnick
Assistant Inspector General for Auditing
OIG/HEW

Staff Reporters

Ray Lazorchak
OIG/HEW
HEW Audit Agency

REMARKS

Frank L. Greathouse, *Director of Audits State of Tennessee*

In order to properly understand the position of accountants and auditors as they face their responsibility for the detection of fraud, one must take a look into history to discern how the accounting profession has faced the problem historically. It is necessary that we look at the practice of public accounting in order to determine where, perhaps, we as government accountants and auditors should presently be. Early on, the public accountant, as he audited commercial enterprises in the private sector, was aware that the unlimited publicity that misleading financial statements might contain was viewed as a potential cause of widespread reliance and loss. At some early point in time, a determination was made as to whether public accountants were public only in the sense that their services were offered to anyone who chose to employ them, that is, whether the 'Public' in public accounting was akin to the 'Public' in public stenographer, the contra being that the public in public accounting meant that the accountant and the auditor had an overriding responsibility to the general public welfare.

Even in the 1920's, accountants and auditors were solely responsible to those who paid their fees. They have since then sold their wares to publicly held corporations, not only on the basis of being available to the public for hire, but also on the basis of being responsible to the public investors in the audited companies.

Virtually every pronouncement on the subject from the accounting profession either expressly states the public responsibility of accountants or takes it for granted. Let us examine the very first sentence of the American Institute of Certified Public Accountants' code of ethics, and I quote: "A distinguishing mark of a professional is his acceptance of responsibility to the public." On that same page is this reference, and I quote: "The ethical code of the American Institute emphasizes the profession's responsibility to the public, a responsibility that has grown as the number of investors has grown, as the relationship between corporate members and stockholders has become more impersonal, and as government increasingly relies on accounting information." The remainder of the quote reads in a similar vein.

The preface to the 1953 restatement of accounting research bulletin also refers to the "increasing interest by the public in financial reporting".

John Cary, in his recent historical study of the accounting profession, provides more details to this same effect, that accountants and auditors believe and advertise that they have a duty to the public. Today, as all of us here know, the public accounting profession is once again reexamining its position in relationship not only to the discovery of, but also to the disclosure of, fraud.

Over the years, the public accountant/auditor has grown to rely upon the fairness of the presentation as the prevailing factor to which the audit report is addressed. Whether or not fraud is discovered in the process of audit has been an issue which was not considered significant as related to the fairness of presentation. Questions have arisen as to whether or not the auditor had a responsibility to disclose fraud where the client had no duty to disclose. The profession considered it inappropriate to require any higher duty from the auditor than the client had.

Even when the accountant is aware of facts, the American courts so far uniformly have held that no duty is required of accountants to police their clients beyond their duties in connection with audited or "associated with" financial statements which they have reason to believe will reach the investing public.

The bases for court decisions have not included any suggestion that the auditor's ethical duty to maintain client confidences is relevant. Perhaps, this is as it should be. The general opinion, however, seems to be that fraud should be fairly clear. The precise status of an accountant's ethical code may differ from that for attorney's although in some states ethical rules of conduct for public accountants have been enacted into law.

The problem is that we accountants and auditors in the public sector have an overriding responsibility for the detection of fraud that is above and beyond that of the public accountant practicing in the private sector. We have a responsibility to detect fraud and to disclose fraud. What is that responsibility? How do we live up to that responsibility? And what can we do if we have detected fraud or abuse and disclose the same only to have the products of our endeavor buried in a bureaucratic pile of manure? Apparently, in the public sector, the auditor has in most cases the authority to audit governmental organizations in the depth that is necessary to detect abuse, fraud, irregularities, and lack of program performance. It is certain that the profession's standards, as established by both the American Institute of Certified Public Accountants and the General Accounting Office in the "yellow book," would demand that the auditor use his competence in carrying out his duties, not only to report on the financial condition and operations, but also to detect abuse and even fraud. This by no means would indicate that every time an audit is performed, even where the standards are adhered to and adequate audit procedures are followed, fraud may be detected. However, where fraud or program abuse is detected, the auditor has the responsibility of seeing that full disclosure is made, *not only to the head of that organization, but also* to the legislative body and to the general public.

When, in the sequence of events, the audit findings concerning fraud and abuse or lack of program integrity are not followed up by the head of the organization or the proper authorities, then the auditor has the responsibility of reporting to the judicial authorities or the legislature directly. To do otherwise would be an abnegation of the auditor's responsibility.

A question often arises as to where audit ceases and investigation begins. It is apparent that when the auditor discovers a crime has been committed, a fraud exists, or that when abuse is flagrant, he must immediately advise those persons who have the authority to investigate and build a case for prosecution. This in no way would indicate that audit should stop pending the results of investigation.

How tired I get and how sick I am of those investigators advising auditors to cease auditing for fear that their prosecution will be screwed up. In fact, most of the time the shoe fits the other foot—investigation screws up a case which has been perfectly developed through properly

documented evidentiary matter produced by auditors. Certainly, the auditor should proceed, with the advice of counsel and most certainly, the auditor should not wash his hands of the audit.

Historically, those programs which have been eminently successful, which have adequately used funds provided by the taxpayers, and which have accomplished the process for which the legislative body intended, have been those programs which were properly fiscally managed and against which audits were prepared in a timely, expeditious, adequate manner. Audit is a tool and, used properly, is the most effective tool to prevent fraud and program abuse.

REMARKS

Edward W. Stepnick, Assistant Inspector General for Auditing, OIG/HEW

In 1975 I was among several HEW representatives asked to testify before the House Intergovernmental Relations and Human Resources Subcommittee on HEW procedures and resources for prevention and detection of fraud and program abuse. These hearings laid the groundwork for later consideration and enactment by the Congress of Inspector General Legislation for HEW, later followed as you know by similar legislation for most of the major federal civil departments and agencies.

At the 1975 hearing I was asked by the chairman whether the primary role of the HEW audit agency—an internal audit organization within HEW—was in the field of economy and efficiency and whether its activities with respect to prevention and detection of fraud and program abuse were secondary. I think it would be useful for me to briefly compare the answer I gave then with what I might be saying today based on the last two years experience of auditing in an inspector general environment.

In 1975 I said that the definition of audit encompasses financial accountability, economy and efficiency in the use of resources, and where it is feasible to do so, getting information on the effectiveness of program results. This part of my response was based, of course, on the official definition of audit by the Comptroller General and OMB, and would still stand today.

I went on to more directly answer the question by saying that audits—aimed at one or more of the elements of financial accountability, economy/ efficiency, and program results—relate to fraud and abuse in four aspects—

The first—a system of regularly performed audits *deters* fraud and program abuse by subjecting would-be offenders to possible discovery.

Two—audits sometimes *detect* improprieties and other practices which are deemed to be fraudulent.

Three—audits result in better internal controls and administrative procedures which may either *prevent* fraud or make it more difficult to go undetected.

And four—audits *assist* investigators and law enforcement officials in their criminal fraud investigations.

In summing up, I tended to agree with the chairman that fraud and abuse was a secondary concern, or perhaps a by-product, of normal audit activities.

I have often wondered, if I had put the auditor's concern about fraud more up-front, whether we would have more *auditor* generals in today's environment. But I must confess that, at the time, I was not particularly anxious for the audit function to bear more than its proper share of responsibility for HEW's past sins in this area. But what is that "proper share"? Is it more than "secondary" or "by-product" aspects of normal audits? For the internal auditor in government today, the answer must be "yes."

While not every audit can be "fraud-oriented" to the same degree, every internal audit organization in government must devise special techniques for (1) *assessing* the relative risks of its agencies' programs to fraud and abuse and (2) *searching* for fraud and abuse in the most vulnerable areas. It is time for the auditor to play a more active role in anti-fraud activities, to work with others in extending the "state-of-the-art" of fraud detection, and to recognize that as a result of taking on this new "product line," the value of the total audit effort will be significantly enhanced.

During fiscal year 1978 the HEW audit agency utilized over 200 staff-years—about one-fourth of its total direct audit effort—on developing and applying specialized techniques for fraud and abuse in the health care and public assistance programs, and in assisting investigators and prosecutors develop criminal cases. The largest of these efforts—project integrity in the medicaid program and project match in public assistance —were conducted as special projects separate from our normal audits, although the computer-screening techniques that were used to search for fraud had been developed and tested during earlier regular audit assignments.

When one considers the billions of federal dollars and the millions of people and organizations who receive them, it is an inescapable conclusion that computer-assisted techniques must be a major part of any positive search for wide-scale fraud and abuse. Any audit organization playing an active role in the search must possess or have access to computer skills. We have found that research, development, and testing of new computer applications in our regional offices is challenging and satisfying work, and a good change of pace for our field audit staffs. I expect that many of the techniques, after playing their part in special anti-fraud initiatives, will eventually join the auditor's arsenal of normal audit procedures and management's accounting or administrative systems. In short, the "special" things we are doing today will become institutionalized and commonplace tomorrow.

In general, auditing in an inspector general environment has significantly influenced our attitude, priorities, and methodology. We no longer regard our contribution to anti-fraud activities as secondary—or simply a by-product of normal audits—but rather as a major active product to respectfully line up along side our other work.

While every individual auditor does not at this time have the responsibility to detect fraud in every audit assignment, our organization as a whole has accepted the responsibility to devise and apply specialized techniques that will eventually help him do so.

REMARKS

Donald R. Zeigler, *Chairman, Subcommittee on Perpetration and Detection of Fraud, American Institute of Certified Public Accountants*

In my presentation today I would first like to briefly discuss the history of the objectives of auditing and to outline how the changing of these objectives affected the auditor's perception of his responsibility for the detection of errors and irregularities—otherwise known as fraud. I would then like to discuss briefly the activities and objectives of the committee which I am presently chairing, which was formed by the American Institute of Certified Public Accountants to study methods by which frauds have been perpetrated and means by which they have been detected. Because of the charge of my committee, my remarks today will be directed primarily to the auditor's responsibility to detect material management fraud in connection with his *ordinary examination* of financial statements, rather than to fraud and abuse related to government agencies and government programs—although my remarks may touch somewhat on the subject.

The question as to whether an independent auditor should be held responsible if his ordinary examination of financial statements fails to detect a material fraud concealed in those statements cannot be answered unequivocally; but that does not prevent it from being asked. An article several years ago in *Dun's Review*, for example, asked:

> *"Who is to blame for corporate fraud? That is, who should foot the bill when stockholders suffer a loss because a company's inven-tory is stolen, or its assets turn out to be phony or its profits turn into mysterious losses? Right now, nobody knows for sure."*

That there should be any doubt about the answers sometimes puzzles financial writers and many of their readers. The same article stated:

> *"To many sophisticated business executives as well as ordinary stockholders, the idea that auditors could not be responsible seems incredible. What else are auditors for, they ask, if not to verify the accuracy of a company's books? So it may shock them to learn that the auditor's responsibility for uncovering inadequacies in the books at Equity Funding—or at Home Stake Production Co., U.S. Financial, National Student Marketing and the host of other well-publicized debacles —is far from decided."*

If an audit then is not meant to uncover major fraud, its usefulness to those who rely on audited financial statements is considerably reduced. The problem is the distinction between "meant to uncover" and the actual uncovering. Some fraud should be detected in *any ordinary examination*. Other frauds, however, would be so difficult to detect that assumption of responsibility for their detection would be an impossible burden for independent auditors to bear. Between these two extremes are a number of gradations that make up the large "gray" area within which most

frauds would fall. Obviously, it is this "gray" area that is of most concern to the independent auditor.

While the objectives of auditing prior to the 1900's are of some historical interest, they are not relevant enough to the current interest in the responsibility for the detection of fraud to warrant detailed consideration. From its distant origins, auditing has always been considered as an independent check on stewardship; that is—an objective review of the activities of individuals entrusted with scarce resources or important responsibilities.

The auditor's concern with detecting fraud was clearly expressed by a leading auditing textbook in the early 1900's in which the object of an audit was said to be threefold: the detection of fraud; the detection of technical errors; and the detection of errors of principle. Audits at that time were focused on the examination of the cash records with the primary purpose of the examination being to give a sort of clearance to the treasurer or cashier, or whoever was acting in a position of trust in respect to the funds of the concern, so that the owners might be assured in that point.

Over the next three decades, the importance of the detection of fraud as an audit objective decreased steadily. The objective of the ordinary examination changed from being primarily concerned with providing "clearance to the treasurer" to being concerned with the fair presentation of financial statements in conformity with generally accepted accounting principles.

The decrease in emphasis on the importance of detecting fraud is illustrated in the descriptions of audit objectives in the successive editions of Montgomery's auditing and in the professional standards. In the early editions (1912-1923), Montgomery indicated that in the early days of auditing the detection or prevention of fraud and the detection and prevention of errors were the chief object of an audit. Subsequent editions gave less and less emphasis to the detection of fraud until in the later editions it is described as a "responsibility not assumed" and that "if an auditor were to attempt to discover defalcations and similar irregularities, he would have to extend his work to a point where its cost would be prohibitive."

Some of the more important reasons for the de-emphasis of attempting to detect fraud in an ordinary examination were:

1. As absentee ownership of corporations expanded, the need for a stewardship check on employees became less significant than an objective review of management stewardship reports—the financial statements.
2. The rapid growth in the size and complexity of business enterprises necessitated changing an audit to an examination of selected items rather than an examination of all transactions in a period. Accordingly, the likelihood of detecting defalcations and similar irregularities was reduced.
3. As the significance of an adequate internal accounting control system became generally recognized, good internal accounting controls were relied upon for the prevention and detection of defalcations and similar irregularities and clerical errors.
4. As the growing complexity of business transactions made the appropriate selection of accounting principles more difficult, they became a more likely source of material misstatement of financial statements, thus requiring increased attention by the independent auditor.
5. The developments in the areas of new accounting principles, uncertainties and the expanding requirements of regulatory and other agencies such as the SEC and New York Stock Exchange made the evaluation of the adequacy of disclosure an important objective for auditors.
6. In recognition of the difficulty or impossibility of detecting frauds involving collusion, forgery, and unrecorded transactions, the auditors started to emphasize the inability of an audit to provide absolute assurance that material frauds would be detected.

These factors, among others, led the AICPA to adopt the position on the auditor's responsibility for the detection of fraud set forth in the codification of statements on auditing procedure published in 1951, which stated:

"The ordinary examination incident to the issuance of an opinion respecting financial statements is not designed and cannot be relied upon to disclose defalcations and other similar irregularities, although their discovery frequently results."

The codification goes on to say:

". . . If an auditor were to attempt to discover defalcations and similar irregularities he would have to extend his work to a point where its costs would be prohibitive. It is generally recognized that good internal con-trol and surety bonds provide protection much more cheaply. . . ."

Needless to say, the position taken was strongly criticized by auditors and others for attempting to go too far in relieving the independent auditor of the responsibility for the detection of fraud. In recognition that the position taken in the codification was not an appropriate explanation of the auditor's responsibility for detecting fraud, the AICPA issued Statement on Auditing Procedures No. 30 in 1960 which was entitled "Responsibilities and Functions of the Independent Auditor in the Examination of Financial Statements." This statement was incorporated in Statement on Auditing Standards No. 1, along with all other statements on auditing procedure in November 1972.

Statement on Auditing Standards No. 1, section 110.05 states that the auditor's responsibility is as follows:

"The responsibility of the independent auditor for failure to detect fraud (which responsibility differs as to clients and others) arises only when such failure clearly results from non-compliance with generally accepted auditing standards."

In other words the SAS indicates that independent auditors are responsible for the detection of fraud that would normally be uncovered by an examination performed in accordance with generally accepted auditing standards. Obviously, however, some frauds were specifically excluded from that responsibility by the SAS which further states:

"The subsequent discovery that fraud existed during the period covered by the independent auditor's examination does not of itself indicate negligence on his part. He is not an insurer or guarantor; if his examination was made with due professional skill and care in accordance with generally accepted auditing standards, he has fulfilled all of the obligations implicit in his undertaking."

Notwithstanding these nice sounding words, the independent auditor, particularly in today's environment, is extremely concerned with the possibility that fraud might exist. This is because of his concern that the financial statements might be materially misstated as a result of fraud. The auditor is not concerned with fraud as such, but with the potential material misstatement of the financial statements.

In light of the notorious and highly publicized cases in recent years and the increased litigation against accountants, the profession has been under increased pressures to accept more and more responsibility for the detection of errors and irregularities. I was a member of the auditing standards executive committee of the AICPA from 1973 to early 1977. During that time, the following statements on auditing standards dealing with the auditor's responsibility for the detection of fraud and other irregularities were issued:

1. SAS 6—related party transactions.
2. SAS 16—the independent auditor's responsibility for the detection of errors or irregularities.
3. SAS 17—illegal acts by clients.

SAS No. 16 superseded SAS No. 1 insofar as SAS 1 dealt with the auditor's responsibility for the detection of fraud. I recall with frustration the long months and late hours of deliberations and the wide diversity of positions taken by various members of the committee in an effort to agree on exactly what is the auditor's responsibility for the detection of errors and irregularities. The biggest concern and the big debate involved the use of the word "search" in paragraph 5 of SAS 16, which states:

". . . Consequently, under generally accepted auditing standards the independent auditor has the responsibility, within the inherent limitations of the auditing process, to plan his examination to search for errors or irregularities that would have a material effect on the financial statements, and to exercise due skill and care in the conduct of that examination."

". . . an independent auditor's standard report implicitly indicates his belief that the financial statements taken as a whole are not materially misstated as a result of errors or irregularities."

This is the first time in professional literature that it acknowledges that the auditor has a responsibility in an ordinary examination *to search* for errors and irregularities which may have a material effect on the financial statements. It was not an easy acknowledgment to incorporate in the literature and involved the entire board of directors of the AICPA before the statement on auditing standards became effective. What finally tipped the scale, I believe, was the fact that both the courts and the regulatory agencies such as the Securities and Exchange Commission were, in fact, holding the independent auditor to that level of responsibility.

In issuing SAS 16 we finally acknowledged

that when the auditor expresses an opinion on the financial statements of an enterprise that they present fairly financial position and results of operation in conformity with generally accepted accounting principles, he is implicitly representing that the financial statements are free of material errors and irregularities that would be detected in an ordinary examination performed in accordance with generally accepted auditing standards. With this in mind, SAS 16 does not really impose a new level of responsibility, but only acknowledges in writing what the auditor presently perceives and has accepted his responsibilities to be.

SAS 16 goes on to explain that even the most extensive examination cannot provide absolute assurance that no fraud exists if the fraud is accomplished by management's override of internal controls, collusion, forgery, or unrecorded transactions. It reminds the reader that the auditor is not an insurer or guarantor and concludes that "if his examination was made in accordance with generally accepted auditing standards, he has fulfilled his professional responsibility."

While AUDSEC was issuing statements on auditing standards Nos. 6, 16, and 17, the Commission on Auditor's Responsibilities, chaired by Manny Cohen, was established by the AICPA to develop conclusions and recommendations regarding the appropriate responsibilities of independent auditors. The final report which was issued in January 1978, as you probably know, makes a number of recommendations with respect to the entire audit process. Section 4 of the report presents the commission's recommendations with respect to the need for "clarifying responsibility for the detection of fraud". This section discusses, to some extent, certain of the matters I've already covered today as to the changing responsibilities of the auditor over the years for the detection of fraud.

The report suggests that "an audit should be designed to provide reasonable assurance that the financial statements are not affected by material fraud and also to provide reasonable assurance on the accountability of management for material amounts of corporate assets." The report goes on to state that "an audit of financial statements should be expected to detect those frauds that the exercise of professional skill and care would normally uncover". It concludes, however, that "an auditor cannot be expected to detect all frauds. He cannot detect certain types of fraud, such as collusion between management and other parties whom he has no reason to suspect of duplicity".

The Cohen Commission report presents a number of recommendations on a standard of care for fraud detection. It is careful to point out that these recommendations are illustrative only, rather than all inclusive, and further states that many are not original. They include:

1. Establish an effective client investigation program.
2. Take immediate steps if serious doubts arise about management's integrity.
3. Observe conditions suggesting pre-dispositions to management fraud.
4. Maintain an understanding of a client's business and industry.
5. Extend the study and evaluation of internal control.
6. Develop and disseminate information on frauds and methods of detecting fraud.
7. Be aware of possible deficiencies in individual audit techniques and steps.
8. Understand the limitations of incomplete audits.

It was in response to the Cohen Commission's recommendation to develop and disseminate information on frauds and methods of detecting frauds that prompted the AICPA to establish the standing committee of which I am chairman that is charged with the responsibility to study and publish analyses of methods of perpetration and means by which various types of fraud have been detected and to study, with the prior approval of the board of directors, specific instances of alleged audit failures and to publish the results of such studies insofar as they indicate the need for new or revised auditing standards.

The Committee has been in existence for about one year now, during which time we've been attempting to organize our thoughts and develop a plan of action. We've been attempting to accumulate as much data as possible in the form of educational and training materials, newspaper or journal articles, comprehensive case studies and other information relating to management fraud. This has not been an easy task. We have been hampered by both a lack of manpower and the hesitancy of CPA firms and others to make detailed information available to us, other than that which is generally in the public record.

There are nine members of the committee including myself; six of whom are presently practicing independent auditors. Three are from big eight firms, two from other larger firms and one from a small firm. The remaining three members of the committee include two from the academic world (one a lawyer) and a representative from industry. At present our staff assistance is limited to one part-time manager from the auditing standards division of the AICPA. Recognizing that our project requires full-time support, the Auditing Standards Division of AICPA has agreed to make one of its auditing fellowships available to the committee. We are presently looking to fill that position. Also, we are hoping that a number of the CPA firms will make staff available to our committee on an ad hoc basis to work on special projects as they develop and the need arises.

As I mentioned previously we have been experiencing considerable difficulty in obtaining information from the most likely sources in light of today's litigious environment. In an effort to get the cooperation and information needed to do an effective job, we are trying to build an impenetrable wall around the committee and the information and files accumulated by it so that the various regulatory agencies, the Ethics Committee of the AICPA and the Public Oversight Board will not attempt to use any of this material against those that have furnished it. We also hope, of course, that the Ethics Committee of the AICPA will agree that information given to us by the various independent auditing firms will not be a violation of the ethics rules relating to the confidentiality of client information. We have had several meetings with counsel for a number of the firms and counsel for the institute in an effort to solve these problems and are hopeful that we are nearing their resolution.

In an effort to establish closer relationships with the many groups interested in our project, the various members of the committee have been assigned liaison responsibilities with such groups as the Institute of Internal Auditors, counsel for the various CPA firms, The Financial Executives Institute, various governmental agencies, and the fifty state societies of CPA's. I'm extremely optimistic that the efforts just outlined will enable us to build a data bank of information that will become the foundation for the dissemination of meaningful guidance to the profession so that it might improve its batting average in the detection of the fraud.

The Computer Services Executive Committee of the AICPA has established an EDP fraud review task force to analyze the circumstances relating to particular occurrences of EDP fraud and to perform EDP auditing case studies. We anticipate that the EDP task force on fraud will work closely with us in the development of suggestions to the auditor for the detection of fraud from an EDP point of view and to assist us in analyzing the technical EDP aspects of frauds being studied, whenever there has been a significant computer involvement in the perpetration or cover-up of the fraud.

We are not quite sure at this time what the end product of our efforts may be, although we expect that our study of past and present fraud cases will enable us to identify a number of categories or patterns of fraud which could result in our publishing a book on types of frauds that have been perpetrated and means by which they were detected, or perhaps prepare a critique indicating why they were not detected. It might also include specific case studies as illustrations. The eventual publication of the results of our studies could take many months and even years. With this in mind, we are considering a number of interim projects, such as—

1. Preparing a digest of all the important facts and circumstances set forth in accounting series releases issued by the Securities and Exchange Commission as they relate to alleged management fraud. We believe it will be extremely helpful for the profession to have in layman's language a one volume digest of ASR's dealing with management fraud.
2. We are considering accumulating and publishing a comprehensive listing of "danger signals" or "red flags" to alert the profession to possible fraud in connection with upcoming 1978 examinations.
3. We are considering the possibility of publishing a "fraud of the month" case study in the Journal of Accountancy or similar publications to continually remind the independent auditor that frauds, in fact, do occur and to remind them that they should be alert to situations conducive to fraud.
4. We expect to develop a continuing education program on fraud for use by each of the fifty state societies next summer. We expect that the program would be directed toward the smaller practitioner, rather than the larger firms. We anticipate that the members of the standing committee on fraud will either participate in or conduct these continuing education programs at the State level. We are convinced that an effective program directed toward the smaller practitioner will go a long way toward improving the profession's performance in this critical area.

As you can see from the brief description I've given you of the activities to date of the AICPA's

standing committee on fraud, we have a long way to go and a lot of work to do if we are to accomplish our overall objective of determining whether there is a need for new or revised auditing standards with respect to the detection of material management fraud.

I would like to leave you with one final thought and that is we need all of the information, cooperation and assistance we can get. If any of you are willing to supply the Fraud Committee with educational or training materials, articles or disguised descriptions of cases you may have encountered, please forward them to the Standing Committee on Perpetration and Detection of Fraud in care of George Zuber of the AICPA at 1211 Avenue of the Americas, New York, New York 10036 or to me. I'll take this opportunity to thank you in advance for any information you may forward us.

Summary of Discussion

The session considered two major issues: first, the role of internal auditors (city, State and Federal) in the detection and reporting of fraud and abuse situations; and, second, the independent public accountants' perceptions of their responsibility for the detection of fraud.

In considering the first issue, discussion centered around the question whether the primary role of Government internal audit units is economy and efficiency and whether prevention and detection of fraud and program abuse are of secondary importance. Are the auditor's anti-fraud efforts more than "secondary" or "by-products" aspects of normal audits?

The consensus of public sector auditors was that Government internal audit organizations have an overriding responsibility for detection and disclosure of fraud that is above and beyond that of the public accountant practicing in the private sector. Moreover, it was agreed that such effort is more than a "secondary" or "by-product" aspect of normal audits; rather, it is a major active product of audits. It was noted that auditors should play a more active role in anti-fraud activities, work with others in extending the "state-of-the-art" of fraud detection, and recognize that as a result of taking on this new "product line" the value of the total audit effort will be significantly enhanced.

While not every audit can be "fraud-oriented" to the same degree, every Government internal audit organization must devise special techniques for 1) *assessing* the relative risks of its State, city, or Federal agencies' programs to fraud and abuse; and 2) searching for fraud and abuse in the most vulnerable areas. Where fraud or program abuse is detected, the auditor has the responsibility of seeing that full disclosure is made, not only to the head of that organization, but also to the appropriate Federal, State and city officials, legislative bodies, and the general public.

The panel members concurred that audit is potentially the most effective tool to deter, detect, and prevent fraudulent practices.

As to the second major issue, Donald R. Ziegler, Chairman of the subcommittee on Perpetration and Detection of Fraud, American Institute of Certified Public Accountants (AICPA), discussed the history of auditing objectives and outlined how changes in these objectives have affected the auditor's perception of responsibility for the detection of fraud. (See prepared remarks on P. 117)

Mr. Ziegler noted that today's independent auditor is extremely concerned with the possible existence of fraud, since financial statements might be materially and fraudulently misstated. The auditor is not concerned with fraud as such, but with the potential material misstatement of the financial statements.

In light of several notorious and highly publicized cases in recent years, and the increased incidence of litigation against accountants, the profession has received significant pressure to accept more and more responsibility for the detection of errors and irregularities.

Therefore, the AICPA formed a Committee to study and publish analyses of methods by which frauds have been perpetrated and means by which they have been detected. The Committee also publishes the results of their studies insofar as they indicate a need for new or revised "auditing standards."

The Committee's efforts are directed primarily at the auditor's responsibility to detect material management fraud in connection with the *ordinary examination* of financial statements, and not to fraud and abuse related to Government agencies and Government programs.

The Committee has been in existence for about one year, and during that time it has been organizing and developing a plan of action.

After outlining the activities of the Committee, Mr. Ziegler concluded that there is much to be done to accomplish the objective of determining the need for new or revised auditing standards with respect to the detection of material management fraud. Mr. Ziegler concluded his remarks by soliciting any information, cooperation and assistance in the form of educational or training materials, and articles or disguised description of cases. Such information may be forwarded to the Committee on Perpetration and Detection of Fraud, in care of George Zuber of the AICPA, at 1211 Avenue of the Americas, New York, New York 10036.

II. THE ROLE OF INVESTIGATION AND PROSECUTION—PANEL A- "THE PROSECUTOR AND INVESTIGATOR—THEIR COMPLEMENTARY ROLES IN THE PREVENTION, DETECTION, AND PROSECUTION OF PROGRAM FRAUD"

Moderator

Lawrence Lippe
Assistant Inspector General for Investigations
OIG/HEW

Chairperson

Philip Heymann
Assistant Attorney General, Criminal Division
U. S. Department of Justice

Panelists

Dale Tooley
District Attorney
City and County of Denver, Colorado

Joseph Henehan
Chief, White Collar Crime Unit
Criminal Investigative Unit
Federal Bureau of Investigation
U. S. Department of Justice

Stanley N. Lupkin
Commissioner, Department of Investigations
New York City

Staff Reporter

Buford M. Mosely
Special Agent in Charge
Atlanta Office
OIG/HEW

Summary of Discussion

Lawrence Lippe, Assistant Inspector General for Investigations, U. S. Department of Health, Education, and Welfare, opened the session by describing the historical growth of HEW's "war" on economic crime and fraud. He outlined the Inspector General concept at both Federal and the State level, and discussed the establishment of the State Medicaid Fraud Control Units.

Philip Heymann, Assistant Attorney General, Criminal Division, U. S. Department of Justice, and the Chairperson of the panel, stated that the principal guideline for effective and efficient prevention, detection and prosecution of fraud is the *coordination of all resources*. Mr. Heymann out-

lined the detection and prosecution phases as: auditors following paper trails and making third party verifications; investigators directing auditors as to what signals to look for in the records; investigators pursuing leads disclosed by audit activity; early investigative case review with prosecuting attorneys to explain cases and to utilize grand juries. Mr. Heymann warned that premature administrative action could destroy prosecutive potential. He also counseled that the "case agent" (which could be the principal investigator or auditor) must be involved with the prosecutors at the trial.

Dale Tooley, District Attorney, Denver, Colorado, emphasized early and regular communication between the auditor, investigator and prose-

cutor. Mr. Tooley stated that cases with strong jury appeal should be given priority and that "technical" violations should *not* be charged as felonys. He advised that many matters involving program "problems" are not crimes, and criminal investigative resources should *not* dwell on such matters. However, cases which are not appropriate for criminal prosecution should nevertheless be used as a basis for correcting system or program problems. He noted that a professionally run investigation can, in itself, be a deterrent to fraud.

Stanley N. Lupkin, Commissioner, Department of Investigations, New York City, New York, urged that, in designing and legislating programs, all protective measures be in place at the inception. These measures include: required record maintenance; access by auditors and investigators; accountability to appropriate local, State and Federal officials; sanctions for failure to comply; and audit and investigative capabilities as a part of program operations.

Joseph Henehan, Chief, White Collar Crime Unit, Criminal Investigative Division, Federal Bureau of Investigation, noted that approximately 1,300 Special Agents, including 750 accounting trained agents, are assigned to economic fraud cases. Mr. Henehan explained that, in order to best utilize resources, all matters

are discussed initially with an Assistant U. S. Attorney to secure a prosecutive opinion. He stated that the FBI is working and will work with the new Inspector General's offices on joint investigations. Mr. Henehan agreed that the challenge of program fraud requires a team effort, and noted that the U. S. Attorney's office decides how a case is to be developed. He also stated that the Racketeer Influenced and Corrupt Organizations (RICO) statute (18 U.S.C. 1961-68) will be used in situations which merit its application. Mr. Henehan concluded his remarks by noting that although the FBI's thrust is criminal prosecution, information developed on program systems failures will be brought to the attention of the appropriate agencies.

Mr. Heymann concluded the panel discussion by explaining that "high impact" cases were usually categorized by high-dollar volume, the uniqueness of the scheme, the high-level position of the subject, and/or the vulnerability of the victims. He also noted that, due to the limited spaces at the FBI Academy, local prosecutors will not routinely receive white collar crime training, but that FBI "road show" training will fill some needs. Finally, he pointed out that the National District Attorneys Association can assist in filling some of the training needs of local prosecutors.

II. THE ROLE OF INVESTIGATION AND PROSECUTION: PANEL B. "THE FEDERAL, STATE, AND LOCAL PROSECUTOR—THEIR COMPLEMENTARY ROLES IN THE PREVENTION, DETECTION, AND PROSECUTION OF PROGRAM FRAUD"

Moderator

Lawrence Lippe
Assistant Inspector General for Investigations
OIG/HEW

Chairperson

John J. Degnan
Attorney General
State of New Jersey

Panelists

Russell T. Baker, Jr.
U. S. Attorney
Maryland District

Marjorie W. Parker
Deputy Attorney General
Chief, Medi-Cal Fraud Control Unit
California Department of Justice

John K. Van de Kamp
District Attorney
County of Los Angeles, California

Mark M. Richard
Chief, Fraud Section
Criminal Division
U. S. Department of Justice

Staff Reporter

Joseph A. Roche
Special Agent in Charge
Baltimore Office
OIG/HEW

REMARKS

John K. Van de Kamp, *District Attorney, County of Los Angeles, California*

This conference which provides a national focus on welfare fraud and the need to protect the taxpayer's dollar comes at a most appropriate time.

As a prosecutor from California—the state that started the taxpayer's revolt—I can assure you that people are watching very closely how their tax dollars are spent. And, no function of government is under greater scrutiny today than the welfare system.

In the short time alloted for formal remarks, I will concentrate on what we consider to be the prime welfare fraud problem—multiple aid and conspiracy frauds.

The cases involving this type of fraud which come to our office for investigation and prosecution involve losses of hundreds of thousands of dollars in each case. And, because of the scope of the losses, they are the most visible examples to the taxpayers of how their tax dollars are being ripped off.

Let me cite a few examples from our own case files:

Case No. 1: A case still under investigation involves the loss of at least $400,000. Out-of-state fictitious birth certificates and California driver's licenses in different names were used to establish at least 58 fictitious identities and at least 58 fraudulent welfare cases were opened.

Case No. 2: Two weeks ago, our office convicted a person who became nicknamed the "Queen of Welfare." She was accused of bilking the county out of $239,587. The defendant received aid for more than 70 children. Only four (her own) really existed. She used false birth certificates to establish the existence of the children. When our office moved in with a search warrant, we discovered an expensive copying machine which was apparently used for the production of false documents in her $170,000 house.

Case No. 3: One suspect and several associates submitted phony California birth certificates to welfare offices in Los Angeles and Ventura counties to establish the existence of minor children. Estimated amount of fraudulent payment $140,000.

The common thread running through these typical cases is the use of false documents to establish fictitious identities to obtain welfare payments.

How do we cope with this problem?

First of all, a computerized fingerprint comparison system would greatly reduce the possibility of individuals entering the welfare system more than once.

The technology exists to develop a computer-based system that stores fingerprints and provides a continued cross-check to insure that duplicates do not get into the system. This will require the fingerprinting of every welfare applicant. The potential which this system holds for halting multiple aid fraud clearly indicates that its feasibility must be explored at the federal, state and local levels.

Basically, once a welfare applicant was fingerprinted and that fingerprint was coded into the computer, any future application bearing that fingerprint would trigger the computer to produce the prior application. People who go from welfare office to welfare office using false documents to open cases would be easily spotted.

A second priority, should be the development of a national computer system linking local welfare offices with the Social Security Administration. I understand that such a system is in the initial stages and it should be given top priority. It would insure the validation of social security numbers and provide a check on people who are seeking welfare in more than one jurisdiction.

Coupled with a fingerprint system, this computer check on social security numbers would go far in stopping multiple aid frauds.

A corollary of this social security check which can be implemented now by local welfare departments is a system to automatically reject invalid social security numbers which may be used in welfare applications.

Welfare department computers can be programmed to reject social security numbers which are higher than those currently issued by the Social Security Administration.

In our office's investigations, we have discovered that such fraudulent social security numbers are frequently used in multiple aid fraud cases.

Another system which must be developed involves document verification. One of the keys to multiple aid fraud cases has been the requirement that easily forged documents, such as family bibles, baptismal certificates or photocopies of photocopies of birth certificates, must be accepted by welfare departments to verify birth.

The most accurate form of birth verification is through a registered or certified birth certificate. Welfare departments should automatically obtain these documents to verify birth and to verify any other documents presented to the department in a case application.

Los Angeles County currently has a new birth record verification program underway.

Once again, a computer system which would automatically make such checks when applications are filed would greatly enhance this effort to detect the use of false documents.

In our Los Angeles investigations of welfare fraud, we have discovered another pattern which may help catch welfare cheats. Frequently, welfare cheaters give the same telephone number when they open multiple cases.

The computerized storage and comparison of applicant phone numbers would catch people who are using the same phone number for multiwelfare applications. When such an application was received, the computer would provide immediate notification that a comparison must be made between cases.

This telephone comparison should be coupled with an address match system. In Los Angeles, the address match system has proved to be one of the most effective tools in locating multiple frauds.

These steps will go far toward halting multiple aid frauds and taking the profit out of welfare cheating. Threat of quick discovery and prosecution is the best way to convince cheats that cheating doesn't pay.

Finally, I would briefly like to address another problem which is akin to multiple aid and which

ranks high in the amount of money lost. That is, fraudulent applications for loans to replace allegedly stolen checks.

We have uncovered highly organized operations involving applications for emergency loans on the basis that welfare warrants had been lost or stolen in the postal system.

One such operation which is still under investigation involves an estimated loss of at least $200,000. A single district office loss was at least $80,000.

Such losses could be greatly diminished, if welfare recipients are required to have a bank account in which the check will be directly deposited by the welfare agency or the checks will only be available at the welfare office for pick up by the recipient.

I understand that such a system has saved Philadelphia about $8 million annually.

These are a few ideas for improving the investigation and prosecution of welfare fraud. I am anxious to hear the experience of other jurisdictions in these areas and your comments on these proposals.

I am sure that our panel today will be rewarding for us all—and ultimately rewarding for the taxpayers, whose money we are trying to save.

Summary of Discussion

A major commitment to fight the war on white collar crime needs implementation at all levels of government. That is the principal reason for the Secretary's Conference and the issue addressed by this panel. It is basic that delivery of health services and other benefits to the taxpayers be made at the least possible cost while providing quality of care and efficiency in operation.

The burden is on the law enforcement community to ensure cost-effective programs. Frequently, law enforcement officers become involved only when scandalous activity erupts; however, it is incumbent upon Federal, State and local government to prepare today for the prevention and detection of fraud in government programs tomorrow. Program administrators and audit workers need to recognize the potential for fraud and be more vigilant in their routine duties.

Cooperative efforts at all levels in law enforcement agencies can prevent duplication, thus conserving taxpayers' money. The degree of productivity, however, is dependent upon established relationships. Joint investigations not only increase productivity, but also promote greater efficiency.

To develop true cooperative relationships, participants need to overcome negative attitudes commonly seen in "turf battles." There is a need, however, to recognize legal restrictions or constraints which may be imposed upon law enforcement officials, and which may be misinterpreted as refusal to cooperate. Therefore, the law enforcement community must not only be sensitive to and tolerant of each other, but also a clear understanding of realities must be developed. For example, some information cannot be shared legally. The human factor is always present—people deal with people who establish rapport, trust, confidence and recognize mutual objectives.

The searching question—do we *really* know how much fraud and abuse exists? Agencies' impressively low percentages of fraud/abuse are not complete and accurate—as demonstrated when sensational cases come to public attention. Public confidence in the integrity of money-paying or service-providing is paramount today.

Wrongful payment of benefits is a common occurrence resulting from use of false/fraudulent Social Security Numbers (SSN) and various personal identification documents. National identification (fingerprinting) of all program applicants has been proposed as a means of insuring against improper disbursement of multiple benefits. Although this proposal is controversial and may be construed by some as demeaning, it is less intrusive than some existing welfare inquiries relating to eligibility. Another proposal would involve a national computer system linking fingerprint classifications and Social Security data for identification, verification/elimination.

The Department of Justice sponsors joint training of investigators and recognizes the need for the law enforcement community to have continuing dialogue and to establish priorities. Joint investigation can resolve jurisdictional problems in many cases. Moreover, it reduces severe competition between agencies and increases the competency of the investigative team.

III. COMPUTER TECHNOLOGY AS A TOOL FOR FRAUD COMMISSION AS WELL AS AN INSTRUMENT 6815/ FOR FRAUD AND ABUSE CONTROL

Overview Panel

Moderator

Thomas S. McFee
Assistant Secretary for Personnel Administration
HEW

Chairperson

Dr. Ruth M. Davis
Deputy Under Secretary for Research and
Advanced Technology
U.S. Department of Defense

Panelists

Donn Parker
Senior Management Systems Consultant
SRI International

Peter S. Browne
President
Computer Resource Controls

Clark Weissman
Chief Technologist and Deputy Manager
Research and Development Division
System Development Corporation

Staff Reporter

Jim Cox
Management Analyst
SSA/HEW

REMARKS 6815/

Dr. Ruth M. Davis, *Deputy Under Secretary for Research and Advanced Technology, U.S. Department of Defense*

It is an honor to be here to preside over this Workshop which has such distinguished panel members. I have been fortunate enough to know each of them for many years and my admiration for them has grown steadily as their contributions to computer usage and the health of computers have multiplied.

I deem it inappropriate to publicly announce my pleasure at being involved with a tool for fraud commission—even if we later recognize that we are speaking of the computer as such an instrument. Such a statement would surely call to mind a presumed hidden desire of us all to be law-breakers, albeit as honorable a set of law-breakers as our early Boston tea party ancestors and our Western cowboy heroes.

Nevertheless, this Workshop with its intentionally ambivalent title does purposely suggest to us that a device—in this case, a computer—can be an instrument for good as well as for evil. And, what is so challenging about computers is that they can be both simultaneously while being disarmingly responsive.

The single understanding that is so important to reach is that reliable computer systems are the only resources available to us for responsible and responsive large funds disbursement and record-keeping operations. The key words here

are "reliable", responsible, responsive and large. These adjectives, of course, apply to most of HEW's financial assistance, welfare, and health care programs. There is no agency in the government, and I would surmise that there is no agency in the country, which surpasses HEW in motivation and need for championing computer technology as the single most important technology on which its usefulness depends.

As natural corollaries then:

- DHEW should not allow itself to be an unwilling captive of a hostile arrogant technology.
- DHEW should take its place as a singularly important, demanding, and knowledgeable customer for reliable, responsible and responsive computer system.
- DHEW should champion the cause of innovation in the computer and software industries in areas of security and reliability.
- DHEW should be a demanding consumer through setting-up criteria and standards for its aceeptance from the marketplace vendor of computer products and service, and
- DHEW should be the leader in government for defining, preventing, detecting and correcting fraud and abuse involving the use of accomplice computer systems.

What do all these seemingly arbitrary dictates mean to responsible management in DHEW. First and foremost there needs to be an explicit policy statement that computer system management is an integral function of responsible management in DHEW fund disbursement and funds record-keeping organizations. Secondly, this policy statement should recognize the high risk activities of DHEW: namely, funds disbursing and record-keeping activities such as Social Security, Student Financial Assistance Programs, Welfare Programs, Social Services Programs, Health Care Financing Programs, etc. Unwillingness to recognize high risk activities inevitably has led to diffusion of management attention which, in essence, equates to inattention.

Following explicit policy manifestations of management attention comes the difficult task of dealing in an organizational context with complex, dynamic and unforgiving technologies— those of computer hardware and software. As I wrote in the Foreward to "Computer Control and Audit":

"The computer has been described as a dominant advance of the 20th century. Cer- *tainly it is a primary reason for the accelerating evolution of business methods. Applications are no longer computerized simply to gain the benefit of the speed and reliability of automated equipment but to use a new approach in performing applications.*

The advent of electronic funds transfer systems, online data bases, and networks of interconnected computers provides management with new challenges which have created new problems. For one thing, the traditional methods used to control organizations in a manual environment are not effective in a computerized business environment. New control techniques are needed to be responsive to and complement the characteristics of the computer.

These changes are reflected in the problems auditors have in evaluating the reliability of computerized applications. Without established internal control mechanisms, auditors are turning to external measures to control computerized applications. This is because data processing personnel have not spent enough time evaluating computer-generated exposures and risks to their organizations or developing adequate internal control systems for monitoring computer functions. Weaknesses are particularly evident where manual and computerized portions of an application interface."

In high risk organizations there must be unrelenting attention to the reliability of computer systems. Management doctrine must contain the precept that it is a management responsibility to know:

1. When a computer system is *not* performing its *intended* functions

and

2. When a computer system *is* performing a function which was *not* intended.

This balanced equation for computer reliability needs to be applied not only when the computer system begins to perform a new task but throughout the life cycle of the computer system operation. It is here that computer audit becomes a prerequisite to computer reliability.

We do not find this Computer Reliability Equation in widespread use today. We find "band-aid" solutions and "quick-fix" approaches to specific risk problems as they occur. Until we come to grips with the risks inherent with computer systems and with the application of the above cited Computer Reliability Equation the computer will lose out in its continuing credibility gap.

There are those who with sincerity point out

that dealing with computers in terms of risks involved may provide a one-sided negative indicator of computer worth.

I do not think this to be the case. Rather, I think that looking at the risks associated with computers is a very beneficial way of discussing the problems of computers. The beneficial aspects are two-fold: first of all, it appears to be a healthy counter-measure to 25 years of selling computers based on a somewhat naive approach that any use of computers is an improvement to existing ways of doing functions. Secondly, looking in a very pragmatic way at what risks are involved in using computers, should enable us to highlight whatever are the benefits of computers. We should be able to compare the relative utility of computers to other alternatives and the risks associated with performing functions using computers with the risks associated with performing the same functions by other means.

It is in the context then of attempting to pursue a realistic approach to computers and to highlight the relative benefits and disadvantages of computers that discussions of risks and risk-taking with computer systems become very attractive.

There is also something very appealing about the concept of risks. Through its use, we can delineate the various responsibilities of the several groups in our country that are concerned with computers and computer use. For example, commonly found fears of the public can most easily be presented by public representatives and advocates if they can be translated into the kinds of risks that the public fears from computer systems. If fears cannot be translated into something as legitimate as risks, then they remain amorphous and free-floating anxieties to which it is very difficult for responsible managers and for responsible scientists to respond.

Secondly, the concept of risk allows one to describe vulnerabilities of computer systems and the dangers associated with their use. Then, again translating these into risks, one can ascribe safeguards that can be used to combat or to avoid vulnerabilities or dangers. Another most important factor in discussing problems of computer systems in terms of risks is that one can associate risks with costs. The cost of alleviating the risks of computer systems through the use of safeguards can be compared with the cost to the public or to individuals if the risks cannot be eliminated through applying safeguards to computer systems.

Again, most importantly, it is going to be extremely essential to come up with acceptable levels of risks in using computer systems for the performance of particular functions. The

idea of deciding on acceptable levels of risks although new to the computer professional is in no way new to scientists or to the public. It is indeed comfortable to most people in other fields of science, economics, and law to talk in terms of risks. Furthermore, it appears to be a very useful way to bridge the present communications gap between computer science and management if one can use a terminology which is comfortable to all concerned.

I would highlight then as summary key points in our planning to reduce computer risks to acceptable levels that:

1. Computer risks can be dealt with realistically by drawing upon such resources as computer technology, auditing, good management practice and legal and regulatory knowledge.
2. Fraud, abuse and error are common manifestations of possible unacceptable levels of risk.
3. High risk organizations include large funds disbursing and funds record-keeping activities.
4. Management policy in high risk organizations requiring the use of computers must identify computer management as a most important integral component of the management function.
5. Large funds disbursing and record-keeping activities are dependent upon computer systems for reliable, responsible and responsive operation, and
6. DHEW is perhaps the single, largest high-risk funds disbursing and record-keeping activity in the country.

I am looking forward, as I know you are, to hearing our eminent speakers relate to us their ideas and experiences. Let us turn now to them.

Summary of Discussion

Moderator Thomas S. McFee, HEW Assistant Secretary for Personnel Administration, summarized the conference theme and expanded on the role of computers as a tool used both to commit and deter fraud. He noted the effects of Proposition 13 which has placed added responsibilities on agencies. There is a need to "get tough" and to demonstrate ability to manage computers which are vital to large fund disbursements. HEW fund disbursements now exceed those of the Department of Defense. Mr. McFee then introduced the Overview Panel Chairperson, Dr. Ruth M. Davis, Deputy Under

Secretary of Defense for Research and Advanced Technology.

Dr. Davis began her remarks (text on p. 129) by noting that computers have the capability for both the commission and prevention of fraud.

In utilizing computers, it is extremely important to recognize that *reliable* computer systems are the *only* resources available for *responsible* and *responsive large* funds disbursement and recordkeeping. Both DOD and HEW depend on these resources.

Dr. Davis observed that DOD differs from HEW in that it disburses funds to thousands of companies upon which legal requirements can be placed. HEW can place few legal requirements, however, on the millions of individuals it services. HEW, therefore, assumes greater responsibility and assumes more risks.

Hence, with its unequaled computer dependence and the resulting inherent risks, HEW has an obligation to:

- Not allow itself to be an unwilling captive of a hostile arrogant technology;
- Take its place as a singularly important, demanding, and knowledgeable customer for reliable, responsible, and responsive computer system;
- Champion the cause of innovation in the computer and software industries in areas of security and reliability;
- Be a demanding consumer through establishment of criteria and standards for computer products and service; and
- Be the leader in government for defining, preventing, detecting, and correcting fraud and abuse involving the use of accomplice computer systems.

Dr. Davis urged that HEW formally recognize that management of computer systems is integral to the overall management of HEW programs. In addition, it should be recognized that HEW funds-disbursing and recordkeeping operations are high-risk activities.

Dr. Davis stated that computers have accelerated changes in business methods, leaving users with inadequate controls over their operations. Since data processing personnel have not filled this gap with data useful for auditing, auditors are turning to external controls on computerized applications.

In high-risk organizations, there must be unrelenting attention to the reliability of computer systems. Management doctrine must contain the precept that it is a management responsibility to know:

1) When a computer system is *not* perform-

ing its intended functions, and

2) When a computer system *is* performing a function which was *not* intended.

Dr. Davis noted that few computer users have an understanding of these two issues. Rather, they apply "band-aid" solutions to risk problems as they occur. Until this situation is changed and the inherent risks in computer systems are recognized, the credibility gap associated with computers will continue.

Dr. Davis concluded her remarks by stating that, contrary to some opinion, addressing the risk issue will have a beneficial effect, by providing a useful way of discussing computer problems. This approach will counter a 25-year-old assumption that use of a computer is always an improvement. Also, computer usage and associated risks will be more effectively compared with other methods of doing business.

Other benefits resulting from a risk evaluation approach include:

- Clear articulation of public fears regarding risks associated with computers which will assist in the development of responses.
- Development of safeguards to combat vulnerabilities or dangers.
- Comparison of safeguard costs with the cost of potential harm resulting from an absence of safeguards.
- Development of better communications between computer science and management, through use of mutually understandable terminology.

Donn Parker, Senior Management Systems Consultant, SRI International, has identified, studied, and written about hundreds of computer fraud cases. He noted that losses due to fraud are outnumbered by losses due to errors and omissions by five to one, and that these are two different problems requiring different approaches. The solutions to fraud and error, though, should be integrated and implemented jointly. Even though fraud results in less loss, concentration on fraud safeguards can also prevent much loss due to error and omission. Safeguards only against errors and omissions, however, do not significantly reduce fraud.

Mr. Parker observed that there are currently no valid estimates of losses from computer crime, although it is clear that such cases are surfacing at an increasing rate. This increase is due not only to increased computer usage, but also to the lag of supporting technology behind hardware advances. Computer technology is a "moving target" which is not being controlled. Computer audit capability and computer fraud insurance

have not kept pace with advances in hardware. Similarly, the law and prosecution of computer crimes are behind the times, as evidenced by the need to use wire and mail fraud statutes to prosecute and convict. In Mr. Parker's view, Senate Bill 1766 is a step in the right direction, although he does not agree with all of its penalty provisions.

Despite the lack of appropriate support for today's computer technology, the use of computers for large fund disbursements is unavoidable. With proper controls, however, automated service is ultimately safer for those being served, since computerized operations require fewer inherently error-prone human decisions.

Mr. Parker concluded his remarks with the following points:

- We can theorize about computer fraud only for so long.
- At some point, we must learn from available data about who is doing what to us.
- We cannot afford to be merely reactive to computer crime.

Peter S. Browne, President, Computer Resource Controls, described the state-of-the-art in computerized fraud detection and prevention as immature adolescence, or even chaos. At present, there are few accepted tools and little widespread knowledge in this immature field. There are some bright spots, however, including the administrative systems of IBM, the Chase Manhattan Bank, and the GAO.

In Mr. Browne's view, the many ills include:

- Inadequate audit capability.
- Inconsistent practices (reinforcing the strongest link).
- An excess of privileged computer access.
- The "squeaky-wheel" syndrome.
- The fighting of the wrong security fires.
- Security personnel having other, sometimes conflicting, duties.
- An excess of emotion.
- A reliance on ignorance ("No one can cheat us because it is too complex.")

Mr. Browne then listed essential requirements

for use of the computer as an audit tool:

- The collection of information from a variety of sources.
- The review and analysis of the data.
- The use or application of the data for detection.

Mr. Browne concluded his remarks by indicating that more detailed methodologies would be presented in succeeding workshop presentations and panels.

Clark Weissman, Chief Technologist and Deputy Manager, Research and Development Division, System Development Corporation, stated his emphatic belief that while the technology to deter computer fraud exists, it is not applied. In Mr. Weissman's view, fraud is even encouraged by careless computer technology, as evidenced by:

- The complexity of scale of projects.
- Unclear security requirements.
- The omnipotence of operating and data management systems.
- Adhoc design of security.
- Flawed implementation.
- Inadequate operating practices.

Mr. Weissman then listed several steps toward fraud prevention:

1) Top management statement of security objectives.
2) Identification or assignment of security responsibility.
3) Assessment of assets and risks.
4) Segmentation of threats and countermeasures.
5) Development of a technology-intensive security plan.
6) Commitment of sufficient resources to implement plan.

The session concluded with a detailed explanation of methodology, including:

- Segmentation of security requirements by function.
- Enforcement techniques.
- Opportunities to install security during a system's life cycle.

III. COMPUTER TECHNOLOGY—PANEL A—
"COMPUTER CRIMES: CASE HISTORIES AND
PROPOSED LEGISLATION"

Moderator

Thomas S. McFee
Assistant Secretary for Personnel Administration
HEW

Chairperson

Donn Parker
Senior Management Systems Consultant
SRI International

Panelists

Robert P. Abbott
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REMARKS

Donn B. Parker—SRI International
Susan H. Nycum—Chickering & Gregory

This paper is a summary of the nature of computer crime based on our research over the past eight years and an analysis of proposed computer crime legislation.

Computer Abuse

We use the term computer abuse for all intentional, computer-related acts in which perpetrators made or could have made gain or victims suffered or could have suffered loss. Crimes in which the perpetrator is criminally convicted represent only one type of computer abuse. This definition includes a broad spectrum of acts including those in which the alleged perpetrator was not convicted, but a loss was proved even though the perpetrator was only fired or reprimanded. This spectrum also includes cases that arise from management disputes in which civil cases may or may not be litigated. Many of the cases have come

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* *The preparation of the parts of this report dealing with computer abuse (not the parts addressing Federal legislation) was supported, in part, by the National Science Foundation Grant MCS76-01242. However, any views or conclusions in this report should not be interpreted as representing the official position or policy of the National Science Foundation, Chickering & Gregory, or SRI International.*

from the Federal government and the banking industry world-wide.

The primary purpose of our study of computer abuse is to learn an organization is vulnerable in its use of computers, then develop controls and safeguards that can ensure safety and security in computer use. The legal aspects and inadequacy of the law have also been studied.

The methodology for the computer abuse study entails the collection of reported cases of computer abuse, field investigation of selected cases, analyses of the collected data to determine types of vulnerabilities of computers, the identification of potential perpetrators, the unauthorized methods used, the types of losses, inadequacy of criminal laws, and failures in control and prevention.

The Nature of Computer Abuse

The conditions that give rise to computer abuse today are a rapidly advancing use of computer technology and applications and lagging supportive functions that could make the technology safer to use. These supportive functions include having mature and knowledgeable management, an informed public, a knowledgeable justice system, and adequate laws. Knowledge of the nature of computer abuse will enhance the understanding of this problem.

Four types of computer abuse have been identified in the collection and study of 640 cases: vandalism against computer hardware and facilities or against the data and computer programs stored in them; theft of information or property (hardware and programs); financial fraud or theft; and unauthorized sale, use, or denial of use of services. Cases include international and business espionage and sabotage, whitecollar crime, organized crime, and employee and consumer misbehavior. The abuses go by the familiar names of fraud, theft, larceny, extortion, embezzlement, sabotage, and espionage. However, new circumstances associated with automation have created a new kind of crime. Occupations of the perpetrators, environments, modi operandi, time scale, geographic constraints, and forms of assets are all new. This is causing different problems and challenges for potential victims, law enforcement agencies, prosecutors, the judiciary, and legislators.

We have not determined whether financial fraud and embezzlement are increasing. The methods of fraud and embezzlement are changing as the activities in which they exist are automated. It is also clear that crime involving computers is increasing.

This conclusion is based on analyses of 640 cases. About seventy-five percent of the cases have been verified. The remainder have not been investigated and include reports for which sufficient data such as the name of the victim or prosecutor have not been reported. Sources of case information include newspapers and other public media, law enforcement agency reports, and questionnaires prepared as part of the study and distributed to victims.

Computer-abuse losses are probably less than losses associated with natural disasters such as fire and are often the result of poorly designed systems, errors and omissions in computer programming, and faulty data input. We have been fighting these types of computer problems for 30 years, and solutions are well known although not sufficiently applied. Nevertheless, computer abuse is a new problem and has emerged only recently as computers proliferated into sensitive functions in society. New approaches to prevention and control are needed to protect against intentional acts of computer abuse. There are still types of abuses that defy solution.

These control needs can be better understood by considering the nature of computer abuses. One or more of the following four roles of computers apply.

(1) A computer can be the *object* of an abusive act. In four cases, computers have allegedly been shot with guns. The computer as an object of abuse exists in twenty-eight percent of the sample cases, although in many of the cases other roles may also have existed.

(2) The computer can be either the basis for a unique *environment* in which an act occurs or the source for unique forms of assets. For example, computer programs, unique products of computer technology, represent entirely new types of assets subject to loss. About sixty-one percent of the sample cases concerned the unique nature of computers although many may have the following two roles (3 and 4) present as well.

(3) A computer can be the *instrument* of an act. For example, in one reported case, a computer was used by an embezzler to simulate the operations of his company to plan and regulate his embez-

zlement. Only three percent of the sample included this type of role exclusively.

(4) A computer can be used as a *symbol* to intimidate or deceive. Dating services have falsely advertised their use of "giant computers" in matching people for dates. Only nine percent of the sample cases included this role exclusively.

New types of acts may be discovered that have not been anticipated, especially with the rapid advancement of the technology. For example, electronic funds transfer systems and violations of the Privacy Act of 1974 are likely to generate new kinds of frauds and other violations of law. As another example, most organizations that use computers consider most computer programs developed for their own use and crucial to their business activities as being safe from theft. Nobody else could profitably use the same program. However, taking and withholding the victim's own programs as a means of extortion has been frequently overlooked. The computer abuse study revealed this problem. In one verified case, a programmer completed a set of programs and confiscated all copies of them, including the documentation, in an attempt to extort $100,000 from his employer for their safe return.

Mr. Robert Bullock, Director of the Illinois Bureau of Investigation, reported in October 1976 that bankers in Chicago have stated that organized crime is engaged in unauthorized activity in banks through coercion of EDP technologists who have loan-shark and gambling debts. These technologists are forced to perform unauthorized acts in banking computer systems. This is just one of an increasing number of incidents of organized crime taking advantage of computer technology for illegal purposes.

Early in this research, we found that terms such as "computer crime" and "antisocial use of computers" were too restrictive. The purposes of the research might otherwise be diverted to purely social or legal issues, thus limiting the effort to address the problem in a multidisciplinary fashion in computer technology, sociology, and law.

Arguments have been made that such cases as the $2-billion Equity Funding Insurance fraud discovered in Los Angeles in 1973 should not be included in computer abuse because that fraud was a major crime committed by top management, and computers were not the focus of the planning and perpetration of the fraud.

However, computers facilitated the large volume of fraudulent acts in producing and maintaining 64,000 fake insurance policies, and computers played a role in the deception of the external auditors. A significant amount of knowledge is being gained from studying this case that contributes to safer ways of using computers. Therefore, it is included in the data base, but excluded from loss totals (since the large loss distorts the rest of the data). Any case that contributes information that will make computers safer to use is added to the data base.

Size of the Problem

The amount of computer abuse is not known. Our study has identified only a piece of the top of the iceberg of computer abuse. Only a few of the study cases were discovered by auditors. However, the data base is probably biased because cases discovered by auditors tend to be kept confidential and, therefore, would be less likely to be reported for the data base. Most of the cases were discovered accidentally because the perpetrator made a mistake, or circumstances beyond his control revealed the crime. If the sample data base is representative of all cases in this regard, it can be assumed that only a small number of computer abuse cases that have occurred are being discovered and even fewer publicly reported. According to a number of certified public accountants interviewd, most known cases have been discovered only accidentally; many more are treated confidentially and not reported.

The lower limit to the extent indicated by reported computer abuse can be assessed by considering the number of cases relative to the number of computers in use. Assuming that 100,000 computers were in use in 1965 and 200,000 computers in 1975 (worldwide), then there was a reported case per 10,000 computers in 1965 and perhaps as many as five cases per 10,000 computers in 1975 (assuming 100 cases will ultimately be reported for 1975). A rate of one case per year for each 2,000 computers seems unreasonably low perhaps indicating that only a few of the known cases are reported, or perhaps that only a few of the computers are in vulnerable situations.

Resources devoted to searching for and recording cases have been uniformly applied since 1970. However, a widening public awareness of the project has increased the number of unsolicited contributions of information about cases and has increased the number of cases

privately reported. At the very least, the existence of the problem is demonstrated by the amount of collected data that is contributing to the knowledge about the obviously growing problem.

It is clear from the study that proven losses of over $330-million have occurred over the past 15 years (not counting the $2-billion Equity Funding Insurance fraud). This is insignificant compared with estimates of losses from white-collar crime of all types. The U.S. Chamber of Commerce estimated annual white-collar crime losses to be not less than $40 billion (U.S. Chamber of Commerce, 1974). This estimate includes $100-million from computer-related crime (only 1/400th of all white-collar crime).

Losses per incident of computer abuse provide further insight. The losses per incident seem to be far higher with computer abuse than with other white-collar crime. The average loss per case of bank fraud and embezzlement of all types reported by the Controller of the Currency in 1971 was less than $100,000 (based on cases over $10,000). In another study from the computer abuse file of 42 computer-related bank frauds and embezzlements in the period of 1962 to 1975, the average loss per case is $430,000 (total $18-million, range $200 to $6.8-million). The average loss over all reported computer abuse cases in which dollar losses are stated (144 cases not incuding the Equity Funding Insurance case) is $450,000 per case. All banks represent only twenty percent of the computer abuse cases in the SRI study.

Larger losses in computer-related cases could be explained in several ways. There might be bias in the sample, because cases with larger losses might be reported in the public media more than those with smaller losses. White-collar crime losses may be larger when they entail computers because the assets are more concentrated. Once a system is compromised, it is as easy to steal large amounts as small amounts (the automation of theft), and the danger of detection and greater efforts needed forces the perpetrators to look for a larger return on their investment in crime.

Perpetrators

A profile of perpetrators based on extensive interviewing of 24 people engaged in computer-abuse acts provides some insight into the type of people to be cautious of. The perpetrators tend to be young—18 to 30 years old. However, a few of the embezzlers are older. The perpetrators are highly motivated, intelligent, and

personable, making them among the most desirable employees from a hiring point of view. Many are overqualified for their positions. None of the perpetrators entered their jobs with a plan of perpetrating computer abuse, and most of them had been in their jobs for several years with no record of difficulties before they perpetrated the crime. These characteristics and other indications about the typical whitecollar criminal indicate that these people are not professional criminals; instead, they are people who have encountered problems or have identified goals on a short-term basis and have discovered that a violation of their positions of trust could result in solving their problems or assist them in reaching their goals.

Usually these people rationalize that they either are not harming other people in their acts or are harming only a justified few people to achieve their goals. They rationalize that their attacks are aimed at large organizations that can afford to suffer losses. This would probably be particularly true of bank employees who see their employer as a bottomless pit of financial resources, quite removed from assets directly owned by people. Resentment of management was the primary motive stated in only three of the 24 cases investigated. However, most of the perpetrators indicated that job dissatisfaction was a contributing motive.

Little sophistication is found in the methods of attacks on computers. The few cases that are more sophisticated seem to be the ones that get more public exposure and, therefore, are more likely to be in my study case file. The more sophisticated methods for compromising computers also tend to occur among the reported cases that have been perpetrated among students in educational environments (31 cases). These tend to be malicious mischief rather than acts that result in serious loss, but they are the most technically sophisticated. There is some concern that students in data processing environments in universities have come to look on the computer as a game-playing device and do not treat it with the professional respect that a powerful tool deserves. These students may leave universities and go to their occupations carrying this game-playing concept with them, and this could result in an increasing number of computer abuse cases.

The high incidence of collusion in computer abuse—compared with that in general whitecollar crime—leads to the conjecture that when a crime is committed in a technical EDP environment, more skill and access are required than are possessed by any one perpetrator.

Better security measures and auditing practices would discourage collusion and therefore be of great benefit in reducing computer abuse. An alternative conjecture on collusion is that the high incidence of collusion in the reported cases is the result of collusion being easier to detect and more likely to be publicly reported. Lone perpetrators would be more likely to be successful, and thus, their acts would not be reported and included in the data base. In contradiction to this latter conjecture, auditors claim collusion is more difficult to detect.

A study of computer abuse cases, by noting the occupations of the perpetrators and the methods they used, indicates that most perpetrators have performed their unauthorized acts within their own work environments using their own specialized capabilities. This indicates that the most likely potential perpetrators are workers in positions of trust. This indicates that the more effective types of controls and safeguards are journaling, monitoring, separation of responsibilities, and dual controls over the work activities of the employees.

The most common vulnerability in cases studied is in the manual handling of data in human-readable form before it enters the computer. The vulnerability of the computers to computer program changes and acts during processing inside computers is of only sixth-level importance by frequency of reported cases. Only one case of data communications wire tapping has been discovered in the SRI study. The logical conclusion is that manual data handling is far more attractive for fraud than the complex, technical environment of the computer or data communications circuits. However, when the more technical acts are perpetrated, the losses tend to be much larger in each case.

Computer Security

The value of computer-related crime legislation can be appreciated by understanding the high positions of trust that computer technologists occupy. Such position is attributable in part to the lack of sufficient safeguard in computer usage. Although advanced computer security is reducing the potential crime threats among large numbers of people who lack sufficient computer skills and knowledge, it is putting far greater trust into the hands and minds of the few who have sufficient skills and knowledge to compromise systems.

The design of commercially available computers is not yet technically secure from these

highly skilled people, and sufficient security is not expected for at least eight to ten years. Safe in their realization that they cannot be prevented nor detected if they are careful enough, these technologists can do anything they please in sensitive business systems. Most of the 640 known cases of computer abuse have been discovered only accidentally because of perpetrator errors.

This is not meant to imply that the computer manufacturers are at fault. In general, they are making significant efforts to improve security in their products—even beyond what their customers are willing to use or pay for. Progress in research to design and develop provably secure computer systems in the national defense environment is accelerating. Significant effort, motivation and time will be required to transfer this technology to other sectors. A more important problem today, however, is the insecure physical environments in which users place computer systems and the lack of operational, administrative, and personnel security. This makes significant crime legislation all the more important.

The Future

The future of computer abuse can be anticipated on the basis of known experience. Massive fraud, organized crime activity, physical and mental harm to people, violation of personal and corporate privacy, tapping of data communications, violation of intellectual property, terrorism attacks, computer output hoaxes, time-accelerated fraud, and geographically independent fraud must be anticipated to produce adequate legislation.

- Massive Fraud. High incidence, low-loss fraud such as credit card fraud is of minor concern, because it can be closely tracked and adequately controlled with known, powerful detection methods in computers. However, we have few solutions to the sophisticated, highly automated fraud that happens infrequently, but that has high loss in the $10-million to billions range. Study of the few large cases such as Equity Funding ($2-billion), the alleged Cenco Instruments fraud ($40-million), and the recent alleged Fisco Insurance fraud reveals that similar conditions in the use of computers exist in many other businesses, government agencies, and industries. Therefore, even more massive frauds are bound

to happen as we concentrate more assets in computer systems and networks.

- Organized Crime. Only a few, unpatterned computer-related crimes have occurred that involved organized Mafia type criminals. However, there are some clues of their increasing interest in computers. For example, the knowledge that increasing assets are stored in computers where highly technical crime can go relatively undetected and the increased opportunity for career criminals to gain data processing capabilities through training programs now offered in many major prisons make this a likely new problem area.
- Human Losses. Increasing use of computers to control processes where human life and well-being are at stake make murder and injury of people through computers a possibility. Computers are used to schedule surface and air traffic, landing and navigation of aircraft, monitoring patients in intensive-care wards, and controlling industrial processes and military weapons. These are a few of the applications that are hazards to human life and safety.
- Terrorism. A number of computers have been physically attacked and destroyed in the United States in antiwar and anti-establishment demonstrations. Eleven computer centers have been attacked with automatic weapons, Molotov cocktails, and plastic explosives by terrorists in Italy in the past 18 months. The FBI has been warning of increasing international terrorism in this country and computers can be anticipated as likely targets. Businesses and government agencies are becoming so dependent on continuous availability of EDP services that a few days can make the difference between survival or total loss and unrecoverability.
- Loss of Privacy. Unauthorized modification, destruction, disclosure, or use of personal or corporate information for criminal purposes will increase as more of this type of information is stored, processed, and disseminated in computer systems and networks. Increasing legislative action is indicative of already anticipated future problems.
- Data Communication Tapping. There is only one known but unverified case of wire tapping a data communication cir-

cuit. However, as security increases at the computer and terminal ends of the data circuits, the communications parts of systems and networks become the weakest links and attractive targets. The rapid development and increasing use of cost-effective encryption devices may preclude this potential problem, but it merely produces another problem of vulnerabilities in poor encryption key administration.
- Computer Output Hoaxes. Con and swindle artists are finding that computer printouts are useful in presenting an aura of legitimacy to their images by implying they represent substantial businesses that have computers. They also can use the content of printouts for deception or intimidation relying on the image of accuracy and integrity of computer output.

It is important to anticipate future crime problems in legislative considerations to ensure effectiveness of the law in future rapid changes and new uses of the technology. We have applied analysis of the anticipated future crime areas described above to test the likely effectiveness of legislation to deter computer-related crime.

Legislation

We have worked for eight years with the hope that computer-related crime would receive the serious attention now represented by the interest of the U.S. Senate in the bill, S1766, proposing the Federal Computer Systems Protection Act of 1977 introduced by Senator Ribicoff and others. We support this bill as a concept identifying a need in criminal law today and as a focus for legislative study and consideration. Whether the omnibus approach of this bill is appropriate or alternatively, specific changes in Title 18, the results will be beneficial to the safe use of computer technology in business and government.

Bill S1766 is a sound beginning toward meeting the criminal law needs in the difficult and complex technology of the computer environment. It should be expected that presenting this bill for review to computer technologists, potential and past victims of computer crime in business and government, and the justice community will result in modification to make it technically sound, relatively independent of future technical change, comprehensive, complete, and consistent to meet the recognized and anticipated problems as we know them.

Problems of State Law

Acts of theft of and damage to computer programs may or may not be a crime in the various states. The laws vary widely and the presence of a crime turns on whether the program is characterized as property within the meaning of the statute. Some states such as California and Texas already have case law interpreting computer programs as such property, the value of which is measured by the value of the program rather than the medium on which it resides. Other states such as Virginia, Maryland, and until the passage of its Computer Crime Act last year, Florida, hold to a common law tangibility test of what constitutes personal property. These laws do not readily encompass computer programs whether or not such programs are stored in a computer. It is important to note here that if the perpetrator who was convicted of wire fraud, a federal crime, for stealing a computer program by use of interstate telephone facilities, had perpetrated his act totally in the state of Maryland so that federal jurisdiction did not attach and the wire fraud statute was inapplicable, he might have been held to have committed no crime.

Similarly, alteration or destruction of computer programs may or may not be sanctioned by state malicious mischief statutes. Particularly troublesome is the law of New York which requires damage to tangible or physical property. Unfortunately, it is quite possible, and it has been done in New York, to obliterate or alter software without injuring the media on which it resides. Unauthorized use of services may or may not be a crime in the several states.

Problems of Federal Law

At the federal level, acts of theft of government property are a crime and the statute (18 U.S.C. 641) is broad enough to cover both computer programs and services. Acts of destruction or damage to government property are a crime and the relevant statute (18 U.S.C. 1361) has also been construed broadly and should include injury to software. In addition, the federal crime of wire fraud and mail fraud are existing and useful sanctions for perpetrations of fraud involving the media.

Notably absent, however, are existing sanctions in the federal or state jurisdictions against unauthorized transference of electrical impulses. Also absent are clear sanctions against unauthorized use of debit cards, or other instruments similar to but not defined as credit cards. These "loop-holes" in the law are particularly troublesome with respect to electronic funds transfer systems that consist largely of transferences of electronic impulses and which may be initiated by the use of non-credit card but card-like devices and be initiated or consummated outside the traditional bank structure, e.g., at merchant point-of-sale terminals or at automated teller machines.

Our conclusion from computer abuse research is that legislation that would specifically make certain activities a crime is very necessary at the state level and very desirable at the federal level. The state laws that require that injury be to a tangible or that gain result from the taking of a tangible may preclude or render very difficult the applicability of such available sanctions to frauds involving computer programs, computerized data or misappropriation of computer time. Indeed, with respect to theft of computer time, the argument has been made that computer time has no value if it isn't being used and that a perpetrator who uses time when no one else wants that time takes nothing of value and therefore commits no crime. This argument has proved unpersuasive in two recent federal prosecutions; it is not clear how the issue would be resolved in a given state jurisdiction.

Most unauthorized activity studied is sanctioned by existing federal statutes, when federal jurisdiction can be obtained. However, what is theoretically possible and what occurs in practice are frequently disparate, particularly when a sophisticated level of technical expertise as well as imaginative reasoning is required to perceive the applicability of a particular federal sanction to a technologically new and complex set of facts. We should like to emphasize from the experience of our study that the problem is no less acute to the defense bar and even to the perpetrator who may be truly unaware that his act was unlawful.

In our opinion, computer crime legislation should be uniform because of the multi-state and interstate character of computer operations, particularly computer networks. As a practical matter, because of the difficulty in achieving real uniformity among 50 state laws, and we cite here the experience with the Uniform Commrcial Code, a federal law may be essential. Further, we feel that one body of interpretative judicial decisions is a distinct advantage to all parties involved in prosecution where the facts and the concepts are so technologically dependent.

Definitions in the Senate Bill

Insufficient effort has been expended for an in-depth analysis of the definitions in the bill. Nevertheless, examples of some problems and the suggested corrections provide an indication of what must be done. The name of the proposed article #1028, Computer Fraud, is incorrect. The bill covers theft, extortion, sabotage, vandalism, and burglary as well as fraud. Computer-Related Crimes might be a more appropriate title.

The goal for wording of the definitions should be to make them general, simple, and as independent of current and changing technology as possible. They should also exclude subject matter that the bill is not meant to cover. For example, current wording of the definition of computer would include a growing number of devices containing micro-processors such as automated traffic lights, microwave ovens, hobby computers, wrist watches, television and radio sets, digital sound systems, and automobiles. At the same time, the definition would exclude important nonelectronic computers, such as fluidic computers and in the future computers based on the behavior of molecular, atomic, and subatomic particles. In addition, the term "software" should not be used because it is a jargon word that has several different meanings and implies that it represents programs that are different from another new term, "firmware". The suggested definitions below preclude the need for these terms. They should not be considered final until suggestions from other technologists have been carefully considered.

(1) "Computer" means an internally-programmed, general-purpose, digital device that automatically processes data.
(2) "Computer system" means a set of connected devices including a computer and possibly other devices such as data input and output and storage devices, data communication circuits, and operating system computer programs that make the system capable of performing special-purpose, data processing tasks for which it is specified.
(3) "Computer network" means a set of two or more computer systems that automatically transmit data over communication circuits connecting them.
(4) "Computer program" means an ordered set of data that are coded instructions or statements that when executed by a computer cause the computer to process data.
(5) "Property" includes, but is not limited to, financial instruments, data, computer programs, documentation associated with data and computer systems and programs, all in machine- or human-readable form, and any other tangible or intangible item of value.
(6) "Services" includes, but is not limited to, providing a computer system to perform tasks.
(7) Eliminate "software" as a term not needed.

Impact

The impact of this legislation must be considered if it is to result in appropriate law. One effect from passage of this bill would be to make serious felony crimes of many pervasive practices among computer personnel. It is common practice for programmers, computer operators, and other computer users to make unauthorized use of computers for such activities as game playing, printing Snoopy calendars, calculating bowling scores, and maintaining church mailing lists. Under the proposed law, these practices would no longer be ethical issues, winked at or ignored by management, but federal crimes punishable by up to 15 years in prison and $50,000 fine. Moreover, high school and university students are encouraged to attack campus computer systems and attempt to compromise them as an educational exercise; thus, future felons would be in training under this proposed law.

Many computer programmers still believe in the tradition created early in computer history that the author of a computer program has rights to trade, give away, or make personal use of the program even though his employer's resources were used in its development. Further, many computer technologists believe they are members of a technological elite with special rights to access, use, and compromise any computer system.

These concepts and practices ingrained in the computer field will have to be drastically and quickly changed to ensure that the proposed law will start its life with respect and in an absence of gross and pervasive violation. For the first time in the history of computers, this legislation will force organizations that use computers to specify to their data processing employees exactly what activ-

ities are authorized and not authorized in their work and to enforce adherence to these specifications. This will require a period of time for intensive exposure of the concepts in this bill in trade literature, professional society and trade association meetings, discussions, and debates to swing practice in line with proposed law. Otherwise, we make potential criminals of a large minority of otherwise honest and dedicated computer personnel.

The current penalty proposed of 15 years in prison and $50,000 fine is certainly commensurate with the seriousness of the crimes of the Equity Funding perpetrators. But this penalty would also attach to the maker of an illicit computer-produced Snoopy calendar, or the employee who balances his checkbook using a company computer program and computer time. It can apply equally to the theft of a ten dollar pocket calculator as to the theft of a multi-thousand dollar minicomputer.

Second, certain actions which are covered by this bill are already a crime under existing federal legislation. Moreover, the penalties are considerably less under existing federal law. For example, infringement of a copyright by unauthorized copying of a copyrighted computer program or computerized data currently subjects the perpetrator to a $10,000 fine and/or one-year imprisonment pursuant to the Copyright Act (17 U.S.C. 506). Similarly, the unauthorized knowing and willful requesting or obtaining of personal information from a federal agency system of records by false pretenses makes the perpetrator quilty of a misdemeanor and subjects him to a $5,000 fine under the provisions of the Privacy Act of 1974 (5 U.S.C. 552a(i) (1).) It is suggested that these and other disparaties be identified and resolved.

With respect to further drafting questions, we are critical of the use of the term "approach" as used to define "access". This word is not in general use with respect to computers or computer systems and gives no additional meaning to the term "access" in this context. More importantly, the present draft should be limited in applicability by the addition of words such as "for the purpose of causing injury thereby". There are occasions at the present state of rapid development of computing when a person may make an unauthorized intentional change to a computer or computer system with no intent or expectation of harm resulting, but instead to accomplish a positive result. These acts should not be crimes.

In another dimension, it must also be real-ized that this bill, with its current definitions and even the proposed definitions, would extend to unauthorized use of many government-supplied programmable pocket calculators or digital wrist watches and clocks as well as to giant multimillion dollar computers. It would be difficult, if not impossible, to produce definitions that would differentiate these devices in light of rapidly changing technology. Ultimately, a large share of the whole universe of machines and processes will be encompassed by the definitions of this bill.

As we understand the purpose of the bill, it is to encompass in an omnibus measure all of the generally recognized forms of computer-related abuse. In preparation for this testimony, we reexamined representative case histories from the computer abuse study case file to ascertain how S1766 would apply to such cases.

The category of abuses related to obliteration, alteration or theft of computer programs stored in machine-readable form or human-readable form but not "in" a computer does not appear to be sanctioned by the bill. Furthermore, existing state law may not apply, so that a real void may remain unless the bill is changed to include these acts.

The category of abuses related to unauthorized disclosure of computerized data or computer programs for other than fraud purposes does not appear to be sanctioned by the bill. (If the data is personal data, existing privacy or credit reporting laws may apply.) The Senate may wish to exclude privacy consideration from the bill. However, significant occurrences of computer abuse are violations of privacy, and if the statute is silent as to these activities, it should be so by design rather than oversight.

If data or programs are trade secrets, state sanctions may or may not be applicable and federal sanctions will probably apply only when the secret is owned by the federal government or in its custody (18 U.S.C. 1905). In all cases, the criminality of an act may turn on the relationship of the perpetrator to the victim, e.g., 18 U.S.C. 1905 requires that the discloser be a federal employee.

In a related area, where information (data or programs) is taken but not used, no sanctions of this bill appear to apply.

The category of abuses concerning denial of use of a computer, such as when an authorized user uses most or all of the resources of a computer in order to keep other users away as an harassment or form of sabotage, does not ap-pear to be sanctioned by the bill. This coverage is particularly important when such denial of use results in loss of vital services such as transportation, energy and health care.

The category of abuses that entail threats to computer facilities when the threat is never carried out could not be prosecuted under the proposed law. Similarly, acts of extortion predicated on threats of misuse of computer systems that are not consumated are not within the purview of this bill.

The category of abuse involving computers where such computer does not exist or was improperly installed, as for example a dating bureau being sued for failure to use a computer in its services as advertised, is not covered by the bill. The proposed statute only applies when a scheme to defraud actually uses a computer. The statute could not be used to prosecute when the scheme entails the failure to use a computer.

Civil rights and discrimination cases in which, for example, a computer program is used to screen out minorities, do not appear to be covered by this bill.

Our review of reported abuses prompts the query as to how pervasive the coverage of the bill is intended to be. As the foregoing points out, certain acts which are acts of current computer abuse are not covered by the bill or existing law, yet some acts covered by the bill are also sanctioned by existing law and finally some acts not covered by the bill are covered elsewhere in the existing law. If the intent is to "plug loopholes" in existing law, certain amendments should be considered. If the intent is to be broadly encompassing, certain amendments should be considered.

Finally, it is hoped that interest and progress in this criminal legislation will not lead too rapidly to the development of licensing or certifying of computer systems or the personnel who work directly with them. Although the ultimate benefits to society are obvious, the technology, accepted practices, and job requirements are too new, undefined, and changing too rapidly to have enough standards or generally accepted good practices against which to certify or qualify for licensing. Nonetheless, this bill will provide significant impetus in accelerating the needed maturing of the computer field for this to happen.

Summary of Discussion

Discussion topics included recent cases of computer crime; investigation of computer crimes; proposed legislation and problems associated with these subjects. Each panelist made a presentation followed by a brief period of open discussion.

Robert P. Abbott, President, EDP Audit Controls, Inc., addressed the problem of computer systems penetrations and offered the following observations:

- Computers are vulnerable. While working with Livermore Laboratories, Mr. Abbott investigated and proved methods of penetrating systems at the Department of Defense. He never failed to penetrate, even after technical staff had an opportunity to increase the system's security to the maximum of their capabilities.
- An expert can accomplish an undetected penetration through careful timing. An unannounced and unaccounted for termination of services can result in a penetration being masked. Causing a computer to operate at less than full speed can have serious impact on the timeliness of operations. A penetrator who uses these techniques can usually go undetected, since it is very difficult to determine the cause of the termination or slow speed.
- Statutory provisions are currently inadequate or non-existent for computer-related crimes. The Ribicoff Bill (S 1766) is a step in the right direction (if enacted), but it does not apply to the States.

William A. Bayse, Deputy Assistant Director, Technical Services Division, Federal Bureau of Investigation, addressed three basic problems in the area of investigation of computer crimes:

1) Analytical examination of computer-related crimes.
2) Current and possible future computer crime technology.
3) Legislation and law enforcement aspects.

Mr. Bayse estimated that the FBI has a statistical data base consisting of 600-700 computer crime cases. There is a need to analyze these data and to use the results of the analysis to help formulate legislation that would serve as a powerful prosecution tool and as the source for prosecution guidelines. He indicated a need for statutory provisions containing measurable deterrents to various types of computer crimes.

Mr. Bayse noted that there are "pivotal points" in computer crime discoveries; they occur when

managers weigh the loss in public image against the loss of dollars, and decide whether or not to engage an investigator.

Mr. Bayse cited a publication by Charlie Lex, "The Waves of Change," which points out that by 1980, over 85 percent of all computer systems will have at least one remote terminal on-line; by 1985 there will be 240,000 computer sites (80,000 more than estimated for 1980); and by 1985 there will be over 500,000 general purpose computers and 8-10 million terminals. Mr. Bayse suggested that some form of matrix will be needed to determine the effects of the future scale of computer technology on the incidence of computer-related crimes.

Mr. Bayse also recommended Lance Hoffman's book on Computer Security. This volume encompasses problems associated with threats in networks, terminals, automated offices, telephone services, and word processing. It also addresses the complexity of investigation and prosecution of computer crimes.

As a closing note, Mr. Bayse said that there is a need for additional investigators at local, State and Federal levels; and a need to resolve the jurisdictional boundaries associated with computer crimes.

August Bequai, an Attorney at Law in Washington, observed that the Ribicoff Bill (S 1766) is a small step toward, but a long shot from what prosecutors need. Currently, it is almost impossible to prosecute a computer-related crime. Few understand these crimes, and defense lawyers frequently settle the cases by clouding the issues (the accused is a good person), or by plea bargaining. Mr. Bequai also explained that regulatory agencies, and not the FBI, currently handle most computer crime cases. In Mr. Bequai's opinion, the chances of convictions under the Ribicoff Bill (if passed) are not good: "Chances are that S 1766 offenders can get around the Bill, and if convicted will usually get probation."

Donn Parker, the session Chairperson, cited three significant problems with computer crimes legislation:

1) Managers usually resolve computer crimes through administrative actions and not by criminal prosecution, and this practice may continue.

2) The definition of a "computer system" is not clear for purposes of criminal prosecution.

3) What will be the impact of computer crime laws, once they are enacted?

Summary of Questions and Answers

Q. Frank Riley: Who gets blamed for a crime when several offices are involved in changing a system to cause losses?

A. Mr. Bequai: If the company is a publicly held company, the courts have taken the position that computer security is a highly specialized field and that the computer manager is responsible if he or she should have been aware of the crime. The law is already clear that it's not whether you actually knew of the crime, but whether you should have known. If you should have known, then you are a negligent manager. However, these cases usually will not go to criminal court.

A. Mr. Abbott: Policies do not usually exist in companys, corporations, and other entities. Statements of awareness should be given to employees. Policies should be established. Procedures need to be written.

A. Mr. Parker: Managers must establish what is authorized and what is not.

Q. Michael Kreuger, UCLA, asked about the role of encryption as a defensive measure.

A. Mr. Parker: Encryption safeguards provide one form of security, but open new vulnerabilities associated with safeguarding the encryption keys.

III. COMPUTER TECHNOLOGY—PANEL B— "THE ROLE OF COMPUTER TECHNOLOGY IN FRAUD DETECTION"

Moderator

Bryan B. Mitchell
Assistant Inspector General
for Health Care and Systems
Review
HEW

Chairperson

Peter S. Browne
President
Computer Resource Controls, Inc.

Panelists

Robert H. Courtney
IBM Corporation

Joseph L. Boyd
Assistant Director
Financial and General Management
Studies Division
U.S. General Accounting Office

Jerry Hammett
Deputy Director
Ohio Department of
Administrative Services

Staff Reporter

James G. Cox
Management Analyst
SSA/HEW

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REMARKS

Peter S. Browne, President, Computer Resource Controls, Inc.

BACKGROUND

We live in an era of dynamic technical, economic and social change. A dominant factor in causing the change has been computer technology. Through the power of this technology we have put men on the moon, we can transfer monetary funds instantaneously, we are playing exciting new video games, are automating the supermarket, and are building even more elaborate and effective social programs.

The benefits of this change do not come without costs, however. The need for a conference on fraud, waste and abuse serves as a grim reminder of those costs. Computer and communications technology has provided an environment of complex systems, operated with insufficient personnel and management resources, and with little concern for controls. In such an environment, fraud and embezzlement flourish. There are numerous, well-publicized cases where the computer has been used as a tool for committing or covering up a fraud. In addition, such an environment is conducive to waste and mismanagement. As a result, computer security and EDP auditing are now very current and important subjects.

On the other hand, commercial and governmental organizations are just beginning to use the power of the computer as a positive tool on the never-ending battle against white-collar crime. Also, the audit profession and security professionals are now becoming interested and knowledgable in computer system controls.

There are two areas of focus for consideration.

The first question to answer is how is the computer actually used? For years, the audit profession has been looking at files, records, changes, controls and security in and around an ADP environment. Some of the results have been spectacular; some of the failures equally horrifying. The investigative use of computers has been growing quietly. It is quite common to see computer applications like HEW's Project Match, or some of the state welfare or medical service computerized searches for fraud. In the case where crimes are committed through the manipulation of computer systems, usually the only clues are found through reviewing the audit data provided by the system accounting data. This data has been invaluable in conducting investigations.

The second question is what can computer technology do for the auditor, investigator or program manager. It is important to know both the capabilities and limitations of this (somewhat) new tool. That computer analysis of transactions, data records and output is rarely seen, is a factor of education and management, not of technology. However, the technologists have not given as much help in this area as they could. This subject will be explored in more detail in this paper.

THE ROLE OF COMPUTER TECHNOLOGY

Current Practices

The situation in late 1978 in regard to the use of computers for detecting fraud can be best described as immature adolescence. For a number of years, many large companies and agencies have indeed implemented an EDP audit function. Judging by the volume of current trade literature, the function is not always well supported or well stocked with people deeply knowledgeable in computer technology. A recent study conducted for the Institute of Internal Auditors[1] pointed out numerous deficiencies in the state of the art. A comprehensive survey revealed many organizations are not adequately auditing in the EDP environment and that few current EDP audit tools and techniques are adequate. Some twenty-eight of these techniques were described in detail; many of them relate to second generation, batch processing concepts totally irrelevant in a situation where computer systems are linked via communications, data is distributed to small computers or intelligent terminals, and data is shared among many diverse users.

A more recent survey by EDPACS[2] has resulted in a deeper insight into actual practices.

Most commercial organizations use generalized audit programs (software) to check the validity and relationships between data; most government auditors do not. Public accountants do not generally use an integrated test facility or special purpose audit software. Even though this survey shows increased use of audit practices in a computer environment, it is the experience of the author that such practices are too often inconsistently implemented and usually insufficient.

Some successes have been reported of the use of computers in detecting fraud by social service recipients. A computerized search for fraud and errors by New York City medical practitioners revealed over $31 million in overbillings. A computer audit alerted Los Angeles officials to a single welfare fraud of $289,000. HEW's Project Match related computerized files of District of Columbia employees with the Aid to Families with Dependent Children data base. Fifteen persons were indicted.

But even among those organizations and agencies that are aware of the risks and that have a program to deal with fraud and waste, experience has shown that implementation generally suffers because of insufficient attention or application of resources.

- Recent Office of Management and Budget and General Accounting Office surveys have shown that ADP auditing is insufficient in most federal agencies.
- Any study that evaluates ADP security or management controls can find numerous discrepancies in procedures, physical security, organizational responsibilities and technical controls.
- Resources are spent emotionally or incompletely. GAO was able to bypass a $500,000 physical security system by removing hinges in a door.

Technology

In order to use the computer as an audit tool, three things have to be done. Data and information must be collected, analyzed and then utilized as a detection tool.

In terms of collection, the greater the amount of information, the better. Suffice to say, all transactions in which personal or financial rec-

[1] *Institute of Internal Auditors*, Systems Auditability and Control Study, *Researched by Stanford Research Institute, 1977.*

[2] *Perry, William E. and Donald L. Adams*, Use of Computer Audit Practices, *EDPACS, Automation Training Center, Inc., Reston, VA, November 1978.*

ords are added, changed or deleted must have a complete log record written. This means that:

- Date and time;
- Transaction type;
- Nature of changes/additions/deletions; and
- Who was responsible for the change

need to be collected and retained in a tamper-proof file. The critical issue becomes who will review this data.

In terms of today's computer systems, audit data is available from a number of sources, to include:

- Computer system accounting records provided by the manufacturer.
- System accounting records provided by the communications processor, transaction processor or data base management system.
- Accounting records provided by the individual computer application.
- Audit records designed specifically for logging audit, access and control information.
- Control records designed for data integrity and backup purposes.

Data can be analyzed either manually or by automatic means. Whichever, the analysis must take into account the volume, frequency and amount of non-relevant or spurious (for audit use) material. Normative guide-lines must be established for each review in order that "red herrings" or false violations be minimized. In addition, statistical data can be generated from the analysis in order to provide increasingly valid normative guidelines. The following diagram shows this process.
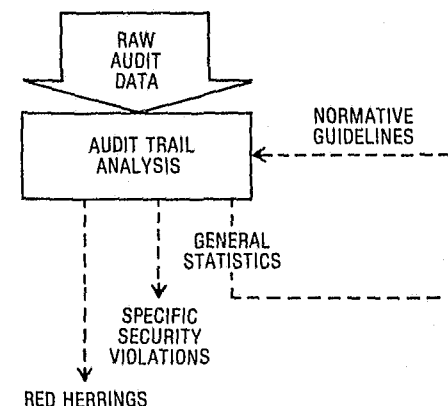
The more traditional audit tools can be used to detect variances between input records and output, as well as to verify transactions. Generalized or specifically written software can be applied on an application by application basis to determine variances, unusual transactions, suspensed items and other anomalies. Comparison of data records from two or more sources, such as used in Project Match, is another valid technique.

Even a good analysis will not be useful or cost-effective unless it can be used to detect fraud and deal with the very real problem of too much data and not enough people to look at it. *One* way to help is by collecting all the relevant data in one place, and separating it from the normal accounting records. This is especially true when the "footprints" are in many places within a single or distributed set of computer systems. The *second* approach is to develop a unique, case-by-case abnormality pattern analysis to allow the author to deal with exception information only, rather than wade through a mass of detailed, uninspiring records, usually in an incomprehensible format. A *third* approach is to allow the detection capability to be very selective—to only look at a small population of transactions or individuals, or to review only selective times, places or amounts.

REQUIREMENTS

Given the need and the existence of adequate tools for auditing computer activities or using the computer to audit other activities, what needs to be done? How can the promise of reducing waste and fraud be translated into concrete action? Is it even technically feasible?

The answers to these questions require organizational commitment, budget funds and technical understanding. Agencies cannot expect to instigate these important control mechanisms without changing their approach to managing complex systems.

There are two main thrusts of action. One deals with the technology of detection and the other its management.

Technical Requirements

Manufacturers and system designers need to make audit and detection tools available, useable and cost-effective. With the wealth of data available in the contemporary computer's billing or accounting system, it would seem quite easy to utilize this data for more than charge-back to

system users. However, very few systems of this nature are used by the auditor. Part of the reason is due to the fact that collecting and logging data requires considerable system overhead. Another reason is that many designers and users have not appreciated what good audit data can mean to them in terms of management.

Therefore, systems designers must understand the technical requirements and provide mechanisms to:

- Log the right data, to include detailed records of data change or access to systems resources.
- Put the data in a convenient place, so that it may be used by more than one person or group for purposes of review and control.
- Protect the audit data from tampering, so that malicious or playful internal personnel cannot easily "turn off" the log, destroy the data or change it to camouflage intent.
- Instrument applications systems to detect anomalies in events, transactions, data or processes.
- Provide mechanisms to instrument systems on a selective basis or be able to turn the audit trails on or off. Thus, samples may be taken, or 100% auditing allowed.

All of these technical needs can be satisfied in the design phase of any system. The problems occur when older, poorly designed systems are to be retrofitted.

Management Requirements

The second set of problems relates to the need for administration and education. Given the availability of technical tools and skilled people to use them, there are some needs still to be met. Too often Agencies do not have people who understand the security, privacy, data integrity and management problems in dealing with computer systems. Thus, the problem is one of education. A short course in computer science is insufficient to brief managers on system complexity and possible loop-holes. Thus, there is a crucial need to place highly skilled, technically trained personnel in positions where they can work closely with auditors, security personnel and users of ADP services. These technicians would then be able to advise on audit trails, on needed controls, and can then use the computer as an investigative device.

The second management problem is lack of awareness, leading to application of insufficient control resources. It must be recognized that to properly audit takes time and painstaking attention to detail. In nearly every case, the payoff can be very high, but resources must be committed first. A few more examples of large savings in program costs through the application of computer-assisted detection or a computer system control audit will certainly help this problem of awareness.

The third management issue is how to allocate resources for management control purposes. All such efforts must consider the trade-offs of cost, potential savings and levels of risk. Thus, there is a need to explicitly consider risks. One tool for doing this is a formal risk analysis of computer applications, where the loss potentials are clearly analyzed and the propensity for damage determined.

Conclusion

This paper has presented an overall view of some major considerations in detection of fraud and waste. It has focused on ADP technology as well as management, and has attempted to look at the following questions:

- What are the problems?
- How has the computer been used for detection?
- How can it be used?
- How can the problem be managed?

In short, we have defined an overall strategy or approach. What is needed now is a concerted effort by federal, state and local government agencies to come to terms with the issues, and the need to organize resources to deal with the very real problems of complexity and inconsistent control.

Summary of Discussion

Moderator Bryan Mitchell, Assistant HEW Inspector General for Health Care and Systems Review, introduced the session panelists and noted that the technology and tools are quickly becoming available to detect and deter computer fraud. Analyses of transactions and data base usage are not only feasible, but being usefully performed in many installations. He observed that the panelists would describe a few of these successes. Mr. Mitchell concluded by stating that the tools are available and the time is ripe for installing more extensive controls on the machines upon which we are so dependent.

The panel Chairperson, Peter Browne, President, Computer Resource Controls, Inc. (Prepared text on p. 145), expanded on several points discussed during the Overview Panel and raised the problem presented by the excess of data over the number of persons available to detect fraud. Three approaches to this problem were suggested:

- Separation of relevant data, or "footprints," from accounting records into one location for manipulation.
- Use of a unique case-by-case abnormality pattern for analysis of exceptions.
- Selective review of a small population of transactions or individuals, or selective review of times, places, or amounts.

Mr. Browne noted that the session panelists had broad experience in computer fraud detection methods and would provide examples of detection techniques and some interesting case histories.

Jerry Hammett, Deputy Director of the Ohio Department of Administrative Services, noted his concurrence with the remarks of previous panelists on the current state of activity in computer security. Even the limited technology that is available is not being used extensively. He noted that most of the problems can be considered people problems, rather than technology problems.

Mr. Hammett commented that one set of tools which are underutilized are system transaction log data. The state of Ohio has made extensive use of these data to analyze computer activity, with considerable success. Through manipulation of these data, manageable outputs are presented for routine security checks.

In Mr. Hammett's view, the development of this system and other controls has made it clear that:

- The system designer must work closely with auditors.
- Raw data have little value.
- Data must be manipulated and formatted to be useful to those responsible for routine security oversight.

Joseph L. Boyd, Assistant Director, Financial and General Management Studies Division, U.S. General Accounting Office (GAO), discussed two areas: GAO involvement in computer auditing and a newly established Task Force on Fraud, which he chairs. Mr. Boyd noted that the GAO policy on computer auditing has evolved over a 10-year period and is stated in a GAO guide. The policy makes reliability assessment an auditor responsibility, and acknowledges the risks inherent in computer usage.

Mr. Boyd also described a technical assistance group in GAO which is actively involved in evaluating agency usage of computers, including controls, security, and reliability. He remarked that the skills needed for computer auditing cannot be purchased, but must be developed.

At GAO, the needed computer audit expertise was developed by:

- Selecting in-house personnel with financial background.
- Training them in computer and reliability assessment.
- Having them work while learning.

The GAO Task Force on Fraud will concentrate on two areas: controls and prevention. An examination will be made of the adequacy of management controls. In addition, the Task Force will assess and followup on auditor's reports. Little consideration will be given to fraud investigation and prosecution per se. The Task Force will be working with the newly established Executive Branch Inspector General offices.

Robert H. Courtney, IBM Corporation, noted that losses due to fraud and abuse are tiny compared to those due to errors and omissions (Dishonesty will never be a match for ignorance). This fact must be recognized before security safeguards can be taken. It is usually not possible to justify the cost of safeguards against fraud and abuse alone; detection of errors and omissions must also be considered.

In Mr. Courtney's view, detection and prevention of computer crime are almost synonymous. Well-publicized detection is the best prevention, since people have a great fear of being caught. Punishment is not a great deterrent.

Mr. Courtney urged that computer security safeguards not be installed unless their cost is justified. Consideration of the amount of potential loss and the probability of such loss are vital in the justification. Too many security safeguards are taken intuitively (locks, guards) and for the sake of appearance. In some instances, a $10 problem many be of greater significance than a $150 million problem because of its frequency.

In this connection, Mr. Courtney described the case of a bank which lost millions from an unauthorized transaction sent by telecommunications lines. The bank lost additional money and time investigating what it thought to be a wiretap problem. It was finally discovered that a key operator had entered the transaction because her fiance had asked her to send a coded message to a friend on his birthday. The key operator had been wined, dined, and given a promise of marriage for the sole purpose of having her make an

unauthorized computer transaction.

Mr. Courtney concluded his remarks by noting that raw computer output can only be useful for fraud detection if it is drastically summarized and analyzed. As an example, he cited an incident which occurred on IBM's internal administrative system which has 22,000 users. Users are scrupulously identified and are held accountable for their transactions. Analysis of a summary of terminal transactions disclosed a mere 12 percent above-average rate by one employee. An ensuing inves-

tigation of this apparently innocuous situation uncovered a fraudulent scheme, and resulted in prosecution, conviction, and imposition of a prison term on the perpetrator.

In summary, the message emerging from this panel was that the technology is available to extract the data needed to detect and prevent fraud. It is time that systems were designed so that we can mine the gold that is available in the data base.

III. COMPUTER TECHNOLOGY—PANEL C— "THE ROLE OF COMPUTER TECHNOLOGY IN FRAUD PREVENTION"

Moderator

L. David Taylor
Deputy Assistant Secretary for Management
Analysis and Systems
ASMB/HEW

Chairperson

Clark Weissman
Chief Technologist and Deputy Manager
Research and Development Division
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Panelists

Dr. Dennis K. Branstad
Institute for Computer Sciences and Technology
National Bureau of Standards
U. S. Department of Commerce

Daniel B. Magraw
Assistant Commissioner
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John T. Panagacos
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William Grant
ADP Systems Security Officer
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REMARKS

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Clark Weissman, Deputy Manager and Chief Technologist, Research and Development Division, System Development Corporation

Introduction

It is the thesis of this paper that "computer technology is the mechanism for security policy enforcement." We live in a technologically complex society which is vulnerable to abuse. One of the major technological advances of this society is the digital computer; thus, the computer becomes both an object of and a tool for fraud. However, the computer also represents the best mechanism for its own protection. The challenge to employing this protection is to find a balance among the three interdependent computer secur-

ity issues: (1) security policy to be obeyed by the computer system (2) computer enforcement mechanisms of hardware, software, facilities and procedures, and (3) assurance and confidence that the enforcement mechanisms are correctly and exclusively obeying the chosen policy.

1.1 Computer Systems are Flawed, Complex Clockwork Mechanisms

Careless and ignorant use of computer technology may encourage fraud. Today we find an

increasingly educated technical population capable of exploiting weaknesses and imperfections in computer systems. The small size of the criminal element among this technical population can increase their payoff by the leverage that the computer affords for fraud. This threat obtains because of the sheer complexity of the "clockwork mechanism" that is a modern computer system. Such systems are the end product of over six years of development, involving hundreds of manyears of labor, and incorporating hundreds of thousands of software instructions and computer circuits. The architecture of such systems gives omnipotent authority for good or evil to the computer's operating system and data management software; principal components which are flawed in their implementation. Flaws result from unstated, unclear, imprecise security requirements. Flaws result from ad hoc security design, partial controls, distributed management responsibility, and little or no verification of the correctness of the implementation, the enforcement mechanism, or the security policy. Flaws also result from inadequate operating practices which leave the internal computer software, data bases, and hardware configuration exposed to tampering.

Steps can be taken to prevent fraud by use of, or toward computer systems. It is the balance of those technological steps that this paper addresses. However, the right conditions for technological solutions must be created by higher levels of management. It is important for top management to clearly state the security objectives to be entrusted to the computer, and assign authority and responsibility to a member of top management. In performing the duties of fraud prevention, the identified security manager must assess the assets and the risks of concern. He must segregate the threats and potential countermeasures according to people or technology control. A strategy for countermeasure emplacement must be prepared as part of a technology-intensive security plan, and sufficient resources must be committed to the timely implementation of such a security plan.

1.2 Policy, Mechanism, Assurance; Triad of Good Security Planning

Figure 1 shows the cornerstone of a good security plan. The structure of that plan is based on the mutually supporting triad of security policy, enforcement mechanism, and assurance of the trustworthiness of the system to handle sensitive data. Technologically, the security policy must be translated into a set of specific and precise system requirements which describe *what* must be done. The enforcement mechanisms consist of the computer hardware, software, communications, facility, people, and procedural interfaces that determine *how* the policy is carried out. These enforcement mechanisms are "organic," and grow through a series of life cycle phases, from original concept development to operation. At each stage in the life cycle, appropriate *evidence* must be gathered, studied, and approved to assure that the system is trustworthy and accreditable to properly operate in an environment containing the set of anticipated threats. It must be emphasized that accreditation take place throughout the life cycle of the system development, not just at the last operational stages. This is paramount, since attacks against the enforcement mechanisms are the most serious methods for frauds against computer systems, and the institutions they service.
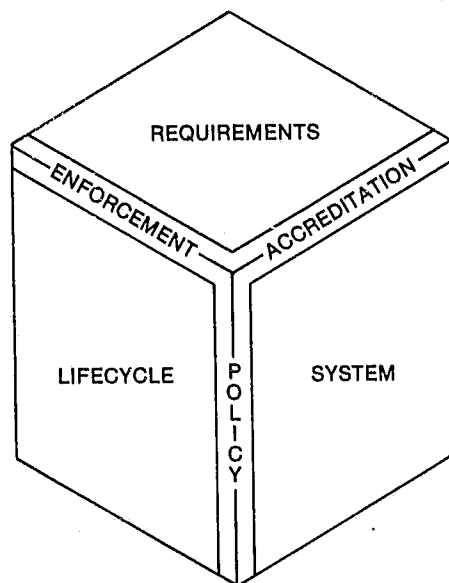
Figure 1: Cornerstone of A Security Plan

2. Computer Security Requirements

Computer security requirements are derived from the protection policy. Broadly speaking, these requirements might address *safety*, where the protection policy addresses the threat of accidents or system failure. The requirements may satisfy a protection policy of *privacy*, in which the system is intended to eliminate unauthorized disclosures to legitimate users who are data "browsing" beyond their authorized limits. Finally, the requirements may address a *security* threat, in which the system is protecting itself against attack by an individual, or an organized conspiracy. Requirements which satisfy a security threat represent the most stringent technical requirements. They demand that the protection mechanisms be self-protecting, and always invoked, even from the most sophisticated attacks as will be described later. This requires that the system be developed in a formal, "well-made" technology. Anything less will lack the trustworthiness required.

Carefully considered computer security requirements can eliminate computer fraud. To achieve this, it must be recognized that fraud will occur at the weakest link. Hence, balanced system-wide countermeasures are required. The general theme of these countermeasure requirements are as follows: Data and software sharing should be minimized and then sharing only via trusted resources. All users (i.e., *subjects*) must be identified by on-line authentication. All terminals, messages, files or software assets (i.e., *objects*) must be authenticated by computer-checked codes. On-line privileges exercised by subjects must be authorized by management, and the computer must check all such authorizations and deny subject access to unauthorized objects. All accesses to objects must be logged for scrutiny at a later time by the object owner. Access and change of system software master copies or of the hardware configuration must be authorized and controlled by machine room procedures. Lastly, all exceptions to the above are suspect.

A balanced enforcement mechanism requires an integrated set of such computer security requirements. These requirements can be segmented by information system function. A generic set of such segmented requirements are discussed below.

2.1 Security Requirements for Data Capture and Display

All subjects and objects must carry an identification and must be labeled both internally and on output. This basic requirement of security is absent in most information systems. All subject-to-object transactions must be authorized and authenticated at the time of access to validate the authenticity of the computerized transaction. Finally, there must exist physical access control to all input/output equipment and terminals to forestall unauthorized modification of the data capture and display devices.

2.2 Security Requirements for Data Transmission

The best data transmission security can be obtained with encryption technology, such as the National Bureau of Standards Data Encryption Standard. In planning for future systems, a message-based transmission system appears optimal. Such a system would segregate traffic-control, and text fields in each message. Encryption of selected data fields, or even the total message is possible. Error and tampering-detection protocols are required to uncover accidental or intentional message modification. Although *link encryption* (i.e., encryption of text flowing between two specifically connected points) is a simple and well understood requirement, it has weaknesses; for example, clear text is exposure at the communications nodes. End-to-end encryption, a newer technique, is a requirement offering a considerably higher degree of protection, and for large networks, at competitive overall cost compared to link encryption. Encryption is only as secure as the safety with which the encryption keys are managed. Frequent key changing is an important security requirement. However, manual key changing is both expensive and subject to abuse. Automated encryption key management is the preferred security requirement.

2.3 Security Requirement for Data Storage and Retrieval

The data management software (e.g., the management information system) is the principal vehicle for data storage and retrieval. As with all application software, the data management system is dependent for its security on the operating system software. However, the data management system can provide additional security as extensions and refinements to that offered by the operating system. The data management system can provide finer data granularity, possibly to the item level, over that available to the operating system. The data management system must provide data security labeling of all sensitive data under its control. Access control and access logging can be provided by both the

operating system and the data management system. They must coordinate with one another. Lastly, the data management system should satisfy requirements for "reasonableness" enforcement; that is, the data management system can perform checks on the semantic legality of data, on threshold limits, and on the frequency or timeliness of information. Such checks are powerful countermeasures to fraud and a quality control measure for error and accident detection.

2.4 Security Requirements for Data Processing and Control

The security policy must segregate data according to "sensitivity." A requirement for the data processing element, is access control to that sensitive data. A corollary requirement is that mixing data of multiple sensitivities must be performed by a *trusted* system. In the absence of such a trusted system, the computer must be dedicated in its use to a single type of sensitive data. The computer should never be used concurrently for program development and operations. Current technology for trusted systems dpends on an access and audit control mechanism (ACM). The ACM must also provide protection for itself if high degrees of trust are to be expected.

A requirement exists for a data base of security information necessary for the operating system and data management systems to function correctly. This data base would contain user identities, passwords, access authorizations, etc., and a requirement exists for a data management system to handle the security data base. An information system security officer (ISSO) is required as the interface between the off-line procedural controls and the on-line ACM controls. Lastly, there must exist a variety of applications level security countermeasures to support the system-level security protocols for user authentication and message protection, as described above.

2.5 Security Requirements for Facility and Operations

A fundamental security requirement is a physical perimeter to protect all computer and communications equipment. Requirements must exist for trusted personnel and procedures to support the computer operation. Foremost among these requirements is the need for, and job description of, the ISSO. The ISSO is responsible for the creation, update, and management of the security data base.

Requirements for hardware and software configuration control ensures responsibility for changes in the physical hardware configuration of computer and communications equipments, and for all software and data base modifications. Finally, there needs to exist a review procedure of all transaction audit logs, structured by security object. The "owner" of the object is responsible for reviewing those logs.

3. Computer Security Enforcement System

Computer security policy is enforced by the total information system, which is composed of the hardware, operating system, network, data base management and application software, user, and facilities. Vulnerabilities in each of these system elements have been demonstrated in current systems. The foremost class of vulnerabilities are those which enable users to make unauthorized modifications to the enforcement mechanisms. Such corruption of the information systems control mechanisms can then be employed to subvert sensitive application's data. Modern computer technology has derived information system architectures which improve our confidence that the system can protect itself. Assurance that the information system countermeasures are trustworthy obtains from both the system architecture and the implementation methods for realizing that architecture. We will dwell in this section on an overview of architecturally sound approaches for security enforcement mechanisms. Security assurance of the implementation will be discussed in the next section.

Figure 2 presents an overview of current research and development approaches to secure enforcement mechanisms for Department of Defense (DoD) applications. These mechanisms are broadly categorized into one of two classes; dedicating a computer to a given level of sensitive information, or sharing a machine concurrently among users with data of mixed sensitivities. The shared machine approach has been called the "multi-level" security approach. Characteristics for each of these architectural enforcement alternatives is briefly described below.

3.1 Periods Processing

Periods processing is the term used for processing a given type of sensitive information on a computer, exclusively, for a limited period of time. All other applications and data uses are prohibited during that given time period. Processing of other sensitive data requires a shutdown of the computer, and a careful sanitization of all memory and printer devices. This transition is called a "color change." It is labor intensive, slow (in order of 30 to 60 minutes) to effect, breaks operational continuity, and often under utilizes computer resources, since the machine cannot be shared. However, it is current practice, offers little security or technical risk, and has no run-time overhead.

3.2 Automated Periods Processing

The objective of this solution is to reduce the manual efforts and attendant time lost in color change between processing of data of different sensitivities. Two approaches have been designed for effecting this automatic switch over; the Job Stream Separator (JSS) and the Cryto Switch. Both schemes involve the use of an auxiliary mini computer to effect and control the color change operation. The auxiliary computer is a shared mechanism between the two time periods and, hence, requires considerable trustworthiness. It is a simpler mechanism than the larger computer it controls and is within the technological state of the art. DoD development of these approaches is currently in progress.

3.3 Secure Distributed Processing

The architectural strategy is to use a computer network to tie together a collection of computers, each of which is dedicated to the processing of a different level of sensitive data. Users could then view the network as a multi-level, or mixed-data sensitive "supra-computer." Access control functions within the network restrict users to operation on only those dedicated computers to which they have authorized access rights. The fundamental technology to make secure distributed processing possible is that of End-to-End Encryption (i.e., E^3). End-to-end encryption guarantees that message text remains enciphered regardless of the communications path from
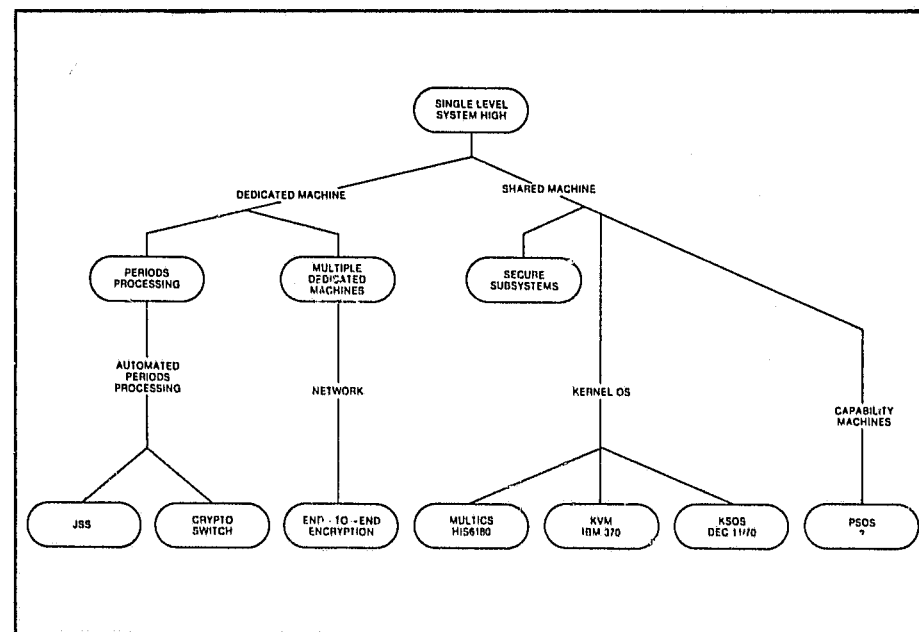

Figure 2: Architecturally Trusted Approaches for Security Enforcement Mechanisms

originator to recipient; e.g., from user terminal to host computer. With the adoption by the National Bureau of Standards of the Data Encryption Standard (NBS-DES) last year, major strides toward realizing E³ technology, is now close at hand. Operational studies have shown that E³ technology is a cost-effective technology for safe transmission of sensitive data, for access control to dedicated computer resources, and for authentication of users and computer hosts. Various trusted devices and processors are needed to make secure distributed processing a reality. These devices include smart encryption boxes, secure terminal handlers, and network front ends. This technology is moving very rapidly and various devices are already in being.

3.4 Secure Subsystems

Given an untrusted operating system, this approach employs the use of a trusted transaction data management system (i.e., TDMS) in concert with facility and procedural constraints which limit the population of users to the TDMS. This solution combines trusted software and trusted procedures, and is an expedient until development of completely trusted operating systems are more widely available. Secure subsystems development for the Department of Defense in limited transaction applications is currently under development.

3.5 Security Kernel Based Operating Systems

Vulnerabilities have been demonstrated to exist in current operating systems. Furthermore, flaw-by-flaw repair of such systems have also been demonstrated to be untrustworthy because, introducing the repair often creates additional flaws, and because repair does not affect yet undetected flaws. The best architectural strategy for future secure operating systems is based on a security kernel. The security kernel enforces the security policy on every subject access to a security object. The kernel is always invoked, self-protecting, and a trusted mechanism. The bulk of the operating system, that is, the non-kernel software, need not be trusted, making the attainment of a kernel-based operating system well within the state of the art. By next year, at least three different kernel-based operating systems on commercially available equipment, will be existent. These include the MULTICS systems on the Honeywell 6180, KVM on the IBM 370, and KSOS on the DEC 11/70.

3.6 Capability Based Security

More advanced security architectures will be based on computers different than those now existent. Such hardware will support software hierarchy and capability "tags" on all computer objects, distinguishing their permissible uses. Burroughs computers and those of the Plessey Corporation typify such structures. The Department of Defense Provably Secure Operating System, i.e., PSOS, is a design that will explore the use of capability machines for secure, trusted, multi-level security enforcement.

4. Security Accreditation

Selection among the options for employing protection or enforcement mechanisms increases with the lead time before the solution must be emplaced for secure operation. As noted earlier, information systems have a life cycle, from conception, requirements definition, development, and operation, that can span more than five years. A security plan that reaches forward five years can improve the trustworthiness of the countermeasure solutions by increasing the number of options from which the solution is chosen.

Words like "trustworthiness," "certification," "accreditation," must be given substance. In Department of Defense applications, certification is a technical process that examines risks, expected losses that might obtain from a given set of threats, and the effectiveness of the enforcement mechanism to counter those threats. The security policy defines which threats are relevant for the given environment. These technical assessments generate a set of "evidence" documents which may include risk assessment tradeoffs, security architectures, program debugging and testing, and formal proofs of correctness.

Accreditation is a management judgment that the evidence is credible, and sufficient to support the contention, that the enforcement mechanism counters the known threats. The mechanism is then deemed trustworthy and approved to operate in the specified manner. Accreditation involves technology for generating credible evidence, and the adequacy of the technical measures employed. It also involves establishing policy regarding acceptable levels of risk. In non-DoD government activities, such as those of HEW, a most serious weakness exists in the absence of sound, technical security policy. For example, no grading system exists for identifying differences in data sensitivity or types of confidentiality of information. By contrast, the Department
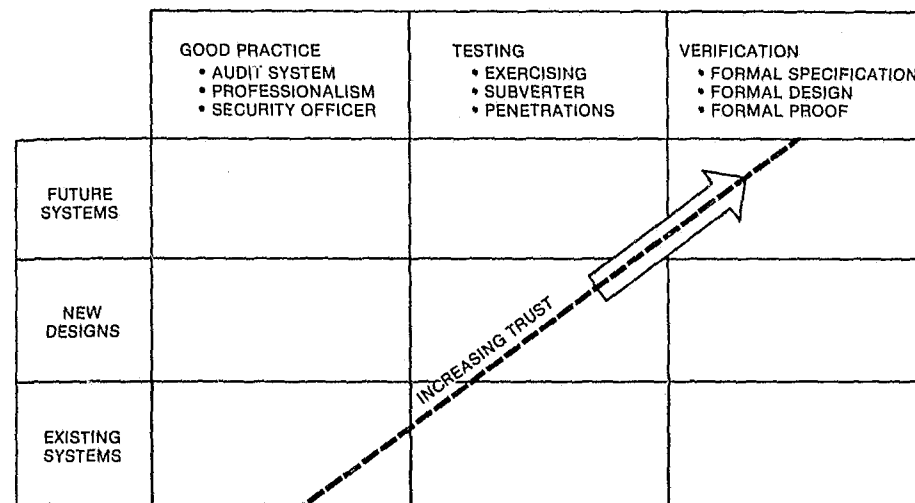

Figure 3: System Accreditation: Confidence that Security Policy is Acceptably Enforced

of Defense classification system is the bulwork of all trustworthy security enforcement mechanisms.

Figure 3 shows that technical confidence increases with improved methods for generating technical evidence. Today's existing systems essentially employ good practice in system construction. New designs are now employing improved security testing and penetrations analysis. Designs are in progress for future systems utilizing more formal methods of specification and proof by formal verification.
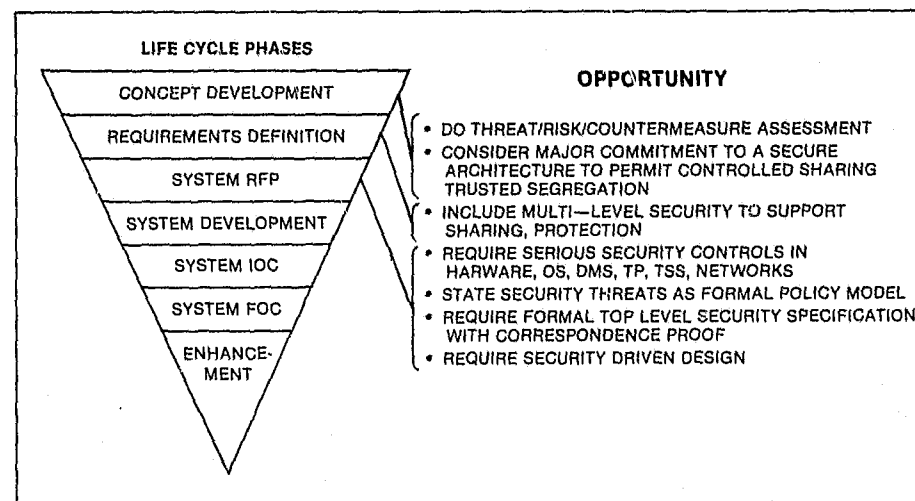

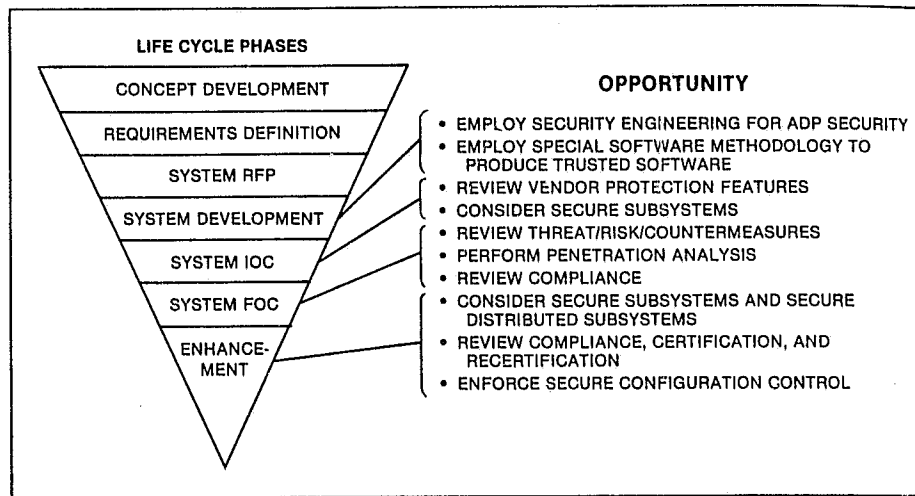*Figure 4: System Life Cycle Opportunities*

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LIFE CYCLE PHASES

CONCEPT DEVELOPMENT                            OPPORTUNITY

REQUIREMENTS DEFINITION          • EMPLOY SECURITY ENGINEERING FOR ADP SECURITY
                                 • EMPLOY SPECIAL SOFTWARE METHODOLOGY TO
   SYSTEM RFP                       PRODUCE TRUSTED SOFTWARE
                                 • REVIEW VENDOR PROTECTION FEATURES
 SYSTEM DEVELOPMENT              • CONSIDER SECURE SUBSYSTEMS
                                 • REVIEW THREAT/RISK/COUNTERMEASURES
   SYSTEM IOC                    • PERFORM PENETRATION ANALYSIS
                                 • REVIEW COMPLIANCE
   SYSTEM FOC                    • CONSIDER SECURE SUBSYSTEMS AND SECURE
                                    DISTRIBUTED SUBSYSTEMS
   ENHANCE-                      • REVIEW COMPLIANCE, CERTIFICATION, AND
     MENT                           RECERTIFICATION
                                 • ENFORCE SECURE CONFIGURATION CONTROL
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Figure 5: System Life Cycle Opportunities
(Continued)

5. Caveat Emptor

Without a market a product will never be realized. If users do not demand good security, they must live with what they get! The key problem is articulating what you want to the technical community. In Figures 4 and 5, we show opportunities for the buyer to demand security at different phases in the system life cycle. The generic life cycle phases are concept development, requirements definition, system request for purchase (RFP), system development, system initial operating capability (IOC), system final operation capability (FOC), and enhancement. The opportunities available to the procurement agency begin in the early concept phases to perform the risk and threat analysis, move through serious requirements for security, employ competent enforcement architectures, and utilize development techniques which permit the generation of good certification evidence.

Caveat Emptor; "Let the buyer beware." The benefit of our democratic, competitive society is that the users get the systems they deserve!

Summary of Discussion

L. David Taylor, HEW Deputy Assistant Secretary for Management Analysis and Systems, briefly introduced the subject, referred to some of the discussion during the overview panel session and provided a resume of the panelists' backgrounds. He emphasized that it is particularly important to incorporate fraud controls at the systems design stage in order to prevent more costly corrections at a later stage. Mr. Taylor referred to Dr. Ruth Davis' challenge to HEW to be a more demanding customer for computer reliability and security by establishing criteria and standards for acceptance.

The Panel's Chairperson, Clark Weissman, Deputy Manager and Chief Technologist, Research and Development Division, System Development Corporation, limited his remarks to a reference to his earlier talk during the overview panel session. He noted that his presentation would be made available as part of the report of these meetings (See P. 151).

Dr. Dennis K. Branstad, Institute for Computer Sciences and Technology, National Bureau of Standards, noted that there are many euphemisms used to avoid calling people poor; instead, they are referred to as "economically deprived" or "economically disadvantaged." There is a similar tendency to call fraud by other names. Dr. Branstad stated that "computer fraud" is a bad term. People commit fraud, not computers. There should be a strong commitment to fight fraud, since fraud controls must be used to be effective. There are tools available today to prevent and detect fraud, but they need to be used.

Daniel B. Magraw, Assistant Commissioner, Bureau of Management, Minnesota Department of Administration, urged HEW to take a stronger role in the design of State welfare computer systems by imposing computer security standards on the States. In Mr. Magraw's view, it is unconscionable for the Federal Government to continue to permit the States' control over this vital area.

Mr. Magraw also noted that systems users must solve their own security problems because it is the user who is at risk, and not computer personnel. Users must ask for readily available techniques, not for "blue sky" technology which is still under development. He suggested that users insist on answers to the following questions:

1) Is there a layman's description of what the computer does and does not do to preserve security?
2) Is there visible proof that security features perform as claimed—are they doing what they should?
3) Is there a follow-up system to insure that information about fraud, abuse, errors or omissions is acted upon—when something is found, is appropriate follow-up action taken?
4) Is there a security manual and are the procedures being followed? Do audits verify this fact?
5) Is there a security budget, and is it used for this purpose?

John T. Panagacos, Research Consultant with the Equitable Life Assurance Society of the United States, observed that impedients to absolute computer security must be recognized. These impedients include legal and social issues that bear on privacy and the right of individuals to due process of law. Mr. Panagacos recounted that his attempts to establish absolute computer security for his company ended in the preparation of a policy statement on individual legal and social rights, including very important customer rights.

Mr. Panagacos then stressed the importance of establishing priorities in the building of systems. In government, in particular, there are often constraints resulting from the passage of legislation without adequate time or funds for effective implementation, i.e., the Supplemental Security Income Program. He pointed out that when these constraints develop, security and systems documentation are frequently ignored.

Mr. Panagacos concluded his remarks by observing that good fraud controls exist,

through current technology, which could be 90 percent effective.

Summary of Questions, Answers, and Comments

Q. With the time/money constraints, what can be done to get the job done?

A. Dr. Branstad: President Carter has stated a commitment to eliminating fraud and abuse. Now there is hope that Federal managers will allow enough time to incorporate better design and audit tools into the systems and will not allow programs to become operational until they are ready. Technology has improved so that programming and other aspects of system development can be speeded up, but it is important that implementation be delayed until adequate testing has been done, and the system is verified and certified as being secure. We cannot afford to have fraud, abuse, errors and omissions because of premature implementation.

A. Mr. Taylor: Most HEW systems security requirements are not costly. When security requires money, usually a high risk is involved. It still costs more to go back and fix an existing system than to include the proper tools in the first place.

A. Mr. Weissman: Systems have a life of roughly six years. It is cost-effective to build security features in the system in the first phase of the six years, and not wait until the end of the system's life. Good design anticipates the problems while incomplete design leaves the system with gaps which make it vulnerable to fraud.

Q. How do fraud and abuse controls apply to errors and omissions?

A. Mr. Weissman: There is a key principle that good systems design attempts to explore all problems in advance. A well-made, well-designed system is responsive to all types of errors, including dumb input. A secure system is efficient and cost-effective, because testing and implementation goes better. There is also a containment of errors—mistakes do not propagate additional errors.

A. Dr. Branstad: Checks for reasonability should be built into systems, and are excellent tools to prevent errors such as paying for seven hysterectomies for one woman. The necessary checks are simple to build into an application program.

Q. Is prevention less susceptible to social/ legal issues than detection? (Asked by Mr. Weissman of Mr. Panagacos.)

A. Mr. Panagacos: Perhaps. In the prevention area, due process is not easy to deal with.

Q. What is the ideal percentage of the total cost of a system that should go into security?

A. Mr. Weissman: I can only make an estimate of costs if we know what the system must protect. In the absence of a policy statement, we don't know what systems security means. Priorities result from policy, e.g., are medical data more or less sensitive than legal data? What is the data security policy?

A. Dr. Branstad: Controls can represent three percent to ten percent of the budget for a project. However, some controls are purposely kept minimal so as not to drive away business. Banks do not require customers to use more than six digits as an identifier to authorize transactions, even though 16 digits might be required to insure the security of the system.

A. Mr. Magraw: Policy is the important thing. Policy must be established by the user. If you leave security in the hands of computer personnel, it won't be done. Security must be adequately budgeted and there must be an independent, outside audit of results.

Q. Of the number of security breaches, what number are not reported?

A. Mr. Weissman: Most of the banking type appear not to be reported. Steps are taken to prevent these from happening again. There is an iceberg of undetected, and not just unreported, security breaches. Vulnerabilities do exist in most systems.

A. Mr. Panagacos: Although some security breaches are hidden, bonding companies do provide fraud statistics. My own company vigorously prosecutes anyone committing fraud.

Q. Duplicates were mentioned as a problem in using Social Security Numbers as a universal identifier. Is there a more useful identifier?

A. Mr. Panagacos: A Federal Commission on Privacy recommended against the use of universal identifiers. The Social Security Number may be duplicative, or some persons may not have a number. Social Security Numbers were considered to lack the controls necessary for an accurate universal identifier.

Q. Are detection or prevention controls better?

A. Dr. Branstad: One is before the fact, and the other is after the fact. By using systems standards and properly designing the system, we hope to prevent fraud, abuse, or error. If tools are available for either prevention or detection, they should be used. It is difficult to separate prevention from detection.

A. Mr. Weissman: With reference to detection versus prevention, we may have to rethink what fraud means in terms of timing. Some of the techniques for detecting fraud that have been around for a long time, e.g., double entry bookkeeping, auditing techniques, etc., are directed at long-time or slowly occurring frauds. We now have to think of fraud prevention in terms of transactions happening in microseconds. New approaches are needed.

Closing Comment: Mr. Taylor thanked the panelists and summarized the session by restating the recurring themes mentioned during the discussion. He noted that it is clear that technology now exists substantially to prevent fraud, abuse, and error. It is particularly important to incorporate system security features at the design stage. We have the tools, but need to go beyond talking about them and get started using them.

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IV. GRANTS AND CONTRACTS ADMINISTRATION WORKSHOP

Moderator

E. T. Rhodes
Deputy Assistant Secretary for Grants and Procurement
ASMB/HEW

Speaker

Lester A. Fettig
Administrator for Federal Procurement Policy
Office of Management and Budget
Executive Office of the President

Panelists

Charles Miller
Deputy Assistant Secretary for Health Operations
PHS/HEW

George R. Houston, Jr.
Vice President for Financial Affairs and Treasurer
Georgetown University

John B. Reiss, Ph.D.
Assistant Commissioner
Department of Health
State of New Jersey

Daniel Paul, CPA
City Auditor
City of Baltimore

Willis Holding, Jr.
Former State Purchasing Officer
State of North Carolina

Staff Reporter

Richard Sullivan
Policy Specialist
Policy Division
Office of Grant and Contract Financial Management
ASMB/HEW

Summary of Discussion

E. T. Rhodes, Deputy Assistant Secretary for Grants and Procurement, HEW, and the Workshop Moderator, opened the session by emphasizing the magnitude and seriousness of fraud, abuse and error:

- The HEW Inspector General identified $5.5 to $6.5 billion lost through fraud, abuse, and error in his 1977 report.
- These losses involve Federal student loan defaulters, Federal employees who improperly receive welfare benefits, and physicians and pharmacists who file improper bills.
- Fraud and abuse account for only 1/6 of the funds lost; the bulk of the losses result from waste and error.

Mr. Rhodes stated that a number of actions have been taken to correct these deficiencies. He stressed the need to be tough in taking corrective actions so that resources to meet unmet needs can be conserved and so that public support for programs which serve poor, disadvantaged, vulnerable, and often powerless citizens, can be maintained.

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Mr. Rhodes observed that the Congress could help deal forcefuly with many of these issues, and pointed out that much of the waste is "legislated waste." In this connection, he noted that legislation is needed to tighten programs and provide needed resources to manage, audit and investigate problem areas. Mr. Rhodes stated that about $4 billion in waste could be eliminated in Fiscal Year 1981, if Congress took appropriate action.

Mr. Rhodes concluded his remarks by stating that the Workshop would focus on the elimination of fraud, abuse and waste in contract and grant programs, and that the panel members would provide Federal, University, State, and local perspectives. He noted that the discussion would include the Model Procurement Code which could be used as a basis for upgrading State and local procurement processes.

Lester A. Fettig, Administrator for Federal Procurement Policy, OMB, Executive Office of the President, noted that the establishment of the Office of Federal Procurement Policy in 1974, symbolized the beginning of a trend toward greater concern with efficient management of Federal programs. The Federal Government expends about $90 billion dollars annually through contracts; and of $130 billion in Federal assistance grants awarded yearly, about $40 billion is used by States, localities, and other institutions to contract for various goods and services.

Mr. Fettig stated that the basic problem in reforming Federal contracting procedures involves the reconstruction of an antiquated system: the basic Federal procurement laws are up to 30 years old, and fostered the development of rigid, narrow, and highly detailed design specifications. Such specifications included one for mousetraps which contained 120,000 words, and one for men's boxer shorts which was 20 pages long! Such specifications have frequently discouraged competition and provided excellent opportunities for fraud and abuse.

Mr. Fettig then detailed the findings of an investigation of the Military Meat Procurement Program, a $1 billion annual purchase. The meat commodity specifications were so detailed that major commercial meat packers would not bid on the contracts. Consequently, about 85 percent of the purchases came from five small specialized companies which were almost totally dependent upon government business. To police the highly detailed specifications, the Army assigned ill-trained, recent recruits as inspectors in the meat packing plants. These inspectors were not only incompetent,

they were also susceptible to bribery and other forms of corruption. As a result of a three-year investigation, several meat company executives and foremen, and a number of former inspectors, were tried, convicted and imprisoned for bribery, fraud and other corrupt actions.

Mr. Fettig noted that he had described this case because it contained some generic characteristics of procurement actions which tend to invite fraud and abuse:

1. Where design specifications are rigid and highly detailed, there is likely to be little or no competition for the contract. Frequently, only one bid will be received.

2. Where there is little or no competition, the purchasing agency must rely heavily on artificial regulatory controls (e.g., inspectors) to assure compliance with design specifications. Unless such artificial controls are very effective, opportunities for fraud and abuse will be present. In addition, use of such artificial controls significantly increases administrative overhead.

Mr. Fettig termed competition as a "disinfectant for fraud and abuse." He noted that, as a result of the Military Meat Procurement investigation, detailed, rigid specifications were converted to standards commonly used by restaurants and other commercial purchasers. Use of commercial standards resulted in the submission of bids by six new companies, including large commercial meat packing concerns. As a consequence of increased competition, the cost of meat procurement declined by 6 percent.

Mr. Fettig then described several major Federal procurement activities which are currently under way:

- *Review of procurement specifications and requirements.*
  Since specifications and requirements are major determinents of competition, a review has been undertaken with the goal of substituting functional or performance specifications in place of rigid, detailed design requirements. Mr. Fettig noted that there are cases, however, in which detailed design requirements are necessary and appropriate. He also noted that advantage can be taken of functional or performance specifications if they are not carefully written.
- *Overt stimulation of competition.*
  Approval for sole source contract awards will be more difficult to obtain. Mr. Fettig

noted that, although the Federal government does have, a need for some exotic goods, which makes a good case for sole source awards, nevertheless there is considerable opportunity for stimulating increased competition through use of formal Requests for Proposals and sealed bids, and through competitive negotiation.
- *Emphasis on cost competition between Federal "in house" and contractor performance.* Mr. Fettig cited this activity as stimulating another form of competition. Competitive pressure from potential outside vendors can result in increased "in-house" productivity and cost savings.
- *Streamlining of the regulatory environment.* Mr. Fettig noted that various Federal Departments, Agencies, and Major Bureaus currently have 851 separate sets of procurement regulations—totalling about 66,000 pages! Many of these regulations are merely duplicative or interpretive of those issued at a higher level. The current regulations will be replaced with Federal Acquisition Regulations—basic regulations which may be supplemented with special instructions, where needed. Unnecessary layers of such instructions will be eliminated.
- *Establishment of an overall Federal Supply System.* Currently there are 45,000 separate Federal specifications for various items which have been issued by different Departments and Agencies (including 5 different specifications for Band-Aids). In addition, there are duplicative purchasing, stocking, and distributing processes and facilities. The goal is to eliminate and consolidate duplicative purchasing, stocking and distributing operations and facilities, where possible.
- *Emphasis on Penalties: Suspensions and Debarments.* Increased emphasis will be placed on clear and strict standards of performance, and the imposition of severe penalties where such standards are not met. Mr. Fettig noted that too often in the past a gentle "wrist slapping" was the only sanction used, and that confusing standards and general mitigating circumstances were used to escape penalties such as suspension or debarment.
- *Enhanced Professionalism and Recognition of the Federal Procurement Workforce.* The Federal Acquisition Institute is providing additional training and career development courses for procurement officials.

- *Procurement Under Grants.* The possibility of "de-Federalizing" procurements by Federal grantees will be investigated. Standards will be developed for the evaluation and certification of indigenous procurement systems, rather than imposing detailed Federal standards and requirements on grantees.

Mr. Fettig concluded his presentation by reiterating the President's goal of assuring competence and efficiency, and noted the importance of improved management in regaining public confidence in Federal programs.

Charles Miller, HEW Deputy Assistant Secretary for Health Operations, described the Department's efforts to improve program performance through grants and contracts. He noted that Secretary Califano had selected grants and contracts administration as a major management matter requiring his personal attention.

In May, 1977, the Secretary announced an initiative designed to correct the following deficiencies:

- Failure to schedule grant and procurement awards (60 percent of awards were made in the last Quarter of Fiscal Year 1977; more than 40 percent were in June—the last month of the fiscal year). This failure significantly undermined good grant contract practices in that there was insufficient time for adequate competition, and grant and contracting offices were severely overloaded.
- Failure to limit non-competitive procurement. In FY 1977, more than 50 percent of DHEW contracts were non-competitive.
- Failure to assure proper monitoring of grant and contract performance.
- Favoritism, conflicts of interest, and other types of subjectivity in the award of grants and contracts.
- Inadequate price and cost analysis.

Mr. Miller then described the Department's Major Initiatives Tracking System (MITS), which measures operating progress of programs and management practices. The MITS is being used to track the progress of the grants and contracts initiatives. In addition, an attempt is being made to relate the Department's employee performance evaluation program to achievements under MITS.

The grants and contracts initiative includes additional training for appropriate staff. A three-year certification program is being undertaken—all grants and contracts officials will be formally certified. In addition, training for key program

managers has also been initiated.

Progress thus far includes:

- In Fiscal Year 1978, fourth quarter grant and contract awards decreased from 6C percent to 39 percent.
- There has been only a one percent increase in competitive contracts—from 48 percent to 49 percent. Mr. Miller noted, however, that a number of statutes designate specific recipients of funds. Moreover, in some programs, the universe is so small that competition is very difficult (e.g., the Indian Health Service, which is restricted to dealing only with tribes on particular reservations). Considerable attention is being given to ways of stimulating further increases in competitive contracts.
- The targets for training and certifying personnel are on schedule.

As to subjectivity in contract and grant awards, Mr. Miller noted that a pilot project is being developed which will involve certification of the absence of conflicts of interest by grant and contract personnel and awardees.

George Houston, Jr., Vice President for Financial Affairs and Treasurer, Georgetown University, noted that, in 1975, he had outlined five external forces affecting higher education:

- *New Legal/social norms:* Social Security, EEO, OSHA, HMO's, ERISA, and Handicapped legislation which reduced the tax-free status of higher education.
- *Accountability:* A fine line exists between reporting or accounting and regulating.
- *Political Economy:* High inflation, coupled with high unemployment; and a falling behind in the purchasing power of faculty salaries.
- *Public Disenchantment:* As tuitions and fees rise, college-bound persons and their parents ask: "Is it worth it?" Some have suggested that a recurring anti-intellectual virus is responsible for public disenchantment. Such disenchantment may make public funding for higher education even more tenuous (e.g., attempts to terminate the College Housing Program).
- *The Federal Government:* By 1975, higher education had enjoyed a fifteen year "honeymoon" with the Federal Government and had become overdependent on government research and training funds. Now there is evidence that the "honeymoon" is over; higher education has begun to drop in priority.

Mr. Houston then described what he termed a "crisis of credibility" between the Federal Government and the university community. Elements of this crisis inlude:

- The lack of a well-articulated and accepted policy on postsecondary education.
- Lack of understanding of the college environment by the Federal Government. The "products" of colleges and universities are not susceptible to precise cost accounting systems. Mr. Houston compared the "products" of an industrial concern with those of universities:

  - While in industry, the timekeeping function is a centralized, full-time job, at a college it is not.
  - Output measurement is relatively easy in industry; in universities it is very difficult—the outcome may not be known for generations.
  - While industry can easily standardize to achieve economy and remain competitive, standardization in the university community interferes with academic freedom.

Mr. Houston noted that higher education institutions are conscious of waste, and have a strong interest in financial integrity. Very few institutions are totally reimbursed for their costs; hence, the university is also hurt by falsification of records.

- Lack of Understanding of the Locus of Control. Mr. Houston suggested that if rules and regulations are to be successful, academic administrators must understand, endorse, and enforce them. In the higher education community, great reliance must be placed on the intellectual integrity of faculty members.
- National preoccupation with scandal. Congressional Committee reports critical of the accounting profession; the GAO study of the quality of DHEW audits; and the "horror stories" within GSA, were cited by Mr. Houston as examples of a preoccupation with scandal in the private and public sectors. He suggested that we shouldn't lose sight of the *accomplishments* of institutions.

Mr. Houston then discussed several points related to auditing versus control:

- Universities are not in an adversary position with the Federal Government on the subject of audit and control. Both want

projects completed successfully at reasonable cost. The University must see that the principal investigator does the research contracted or granted for, that he or she keeps reasonable records; and that necessary reports are filed on a timely and accurate basis. The Government must be responsive and keep the University informed.

- College and University accounting systems have improved in recent years, and these improvements have required major outlays of institution funds for computers, etc.
- The cost of accountability must be compared with the benefits. University priorities will always be research and academic activities, and not strict accounting. In Mr. Houston's view, the solution to current problems does not lie with more auditors or accountants (he noted that at Georgetown, audits have been performed by 6 separate entities); rather, what is needed is improvement in existing auditing or regulations changing the responsibility for audits.

Mr. Houston recommended that direct cost audits and indirect cost audit responsibility be shifted to the independent auditor of each institution. He cited the National Direct Student Loan Program, the College Work Study Program, and an experiment involving Coopers & Lybrand and the University of Pennsylvania as examples.

Such an approach is recommended because it involves a true systems audit; independent auditors are more comprehensive; since independent auditors perform systems audits in connection with the institution's financial statement audit, minimal added cost to the institution is involved; and, such audits would be performed on an annual basis as opposed to the sporadic audits now performed by HEW.

- Another problem is presented by "grey areas" which are not questioned during an initial audit, but are questioned by a subsequent audit. When several years elapse between direct cost audits, the potential for disallowances increases significantly, especially in these "grey areas." Since Government resources will not permit annual audits, Government and universities should make full disclosure when irregularities have occurred or are developing. There must be mutual trust between Federal program officials and university

administrators. Mr. Houston noted that sometimes universities fail in their efforts to enforce Federal regulations because those efforts are undercut by Federal officials.

- Mr. Houston also recommended that universities prosecute fraud to the fullest. He suggested that this approach will serve as a significant deterrent.
- Complexities in reporting requirements often result from the need to apply differing sets of regulations where a project is supported by several Federal funding sources.

Mr. Houston concluded by stating his view that the occurrence of fraud in higher education institutions is infrequent and rare; abuse is more frequent but occasional; and error is more frequent than abuse. In his opinion, most errors are honest or unintentional, and result from changes in Federal attitudes. Mr. Houston urged that identification of individual instances of fraud, abuse, and error not result in the indictment of entire institutions.

Dr. John Reiss, Assistant Commissioner of the New Jersey Department of Health, discussed the role of program incentives in preventing fraud, abuse, and error. He noted that a basic concern should be whether fraud, abuse and error lead to greater government expenditures than would otherwise be the case: "If we are really concerned about the effects of fraud, abuse, and error on the Government budget, we must be concerned about the cost of preventing identifying and correcting them." Dr. Reiss urged that the elimination of fraud, abuse and error be analyzed from a cost-benefit standpoint; it should not cost more to eliminate than it does to have it in the first place.

Dr. Reiss suggested that it is better to identify incentives inherent in the system and make sure they encourage the right results and discourage fraud, abuse, and error, than to establish huge enforcement bureaucracies to deal with the problems the system has generated.

Program criteria, and standards for eligibility, payments, and review can make fraud, abuse, or error more or less easy. The scope of these problems is potentially enormous; it ranges from appropriate eligibility definitions, through identification of appropriate service providers; it ranges from payments to individuals to payments to providers, including institutions, and the administration of programs by all levels of Government. Opportunities for fraud, abuse, or error exist at all of these points.

If the definition of "eligibility" encourages misrepresentation of financial status, it is an in-

centive for fraud. The method of making payment for services may also encourage fraud by enabling providers to maximize payments through various devices. Abuse can be encouraged by not establishing appropriate limitations on services. Error can be reduced by properly designed administrative systems.

Dr. Reiss noted that while controls and enforcement of some kind are necessary (e.g., Medicaid Management Information Systems), such need can be reduced by designing appropriate system incentives.

As an example, Dr. Reiss described long-term care industry problems which resulted from reimbursement of facility cost on an actual historic cost basis. "Historic cost," defined as the last purchase price, made capital manipulation very profitable. Dr. Reiss noted that changing the basis of reimbursement to current appraised value helped resolve the problem.

While Federal regulations insist that historic cost or appraised values, whichever is lower, be used as the basis for reimbursement, if the continued existence of nursing homes is to be encouraged, financial rewards must recognize the "opportunity cost" of the facility. Appraised value is likely to be closer to the "opportunity cost" than is the historic cost of facilities which are still held by the original owner at the initial purchase price.

Dr. Reiss stated that cost reimbursement systems are more likely to be the subject of abuse than are systems which pay for appropriate resource use in the treatment of an admission or a case. Per diem cost reimbursement encourages use of more services and more days. A system which pays for resources necessary for the care of specific patients is more likely to lead to appropriate use of resources and reduce the amount of abuse. Such a system is being developed by New Jersey and HCFA.

Dr. Reiss also suggested that a system which allows providers to share in cost savings is much more likely to stimulate productivity increases than are the penalties inherent in actual cost reimbursement.

Dr. Reiss described some additional examples of inappropriate incentive effects in Section 124.504 of the proposed Hill Burton regulations (on provision of uncompensated services) which had recently been issued by the Public Health Service.

Dr. Reiss concluded by citing two major issues which require public discussion:

1. What is an appropriate allocation of total resources to the health care delivery system? Unless we have an idea how much we want to spend, it is very difficult to determine the proportion of those expenditures which should be spent on cost-effective controls on fraud, abuse and error.

2. Should controls be oriented toward punitive, *ex post* reviews; or, to the creation of positive incentives for appropriate behavior? In Dr. Reiss' view, systems will be much more effective if they encourage what the public desires: penalties should be a measure of last resort, not the primary tools.

Dr. Reiss urged that current system incentives be reviewed, and that changes be made in those which lead to inappropriate behavior.

Daniel Paul, Baltimore City Auditor, described some of the cases of fraud found by his office, and also discussed some problem areas in grant administration.

The first problem Mr. Paul identified pertained to attempts to increase compttetition in hiring consultants in situations where individual consultants have already been hired at the Federal level as sole source providers of services.

Mr. Paul noted that consulting firms which have sole source Federal contracts are frequently unwilling to compete for contracts at the local level.

Another problem arises in the interpretation of grant regulations as to budgets, documentation and reporting. Many local grant administration officials do not have proper background in accounting, etc., to be able to interpret regulations correctly. Mr. Paul suggested that concise summaries of grant requirements be prepared in a general circular form.

Yet another problem is presented by regulations which permit an excessive time period for the completion of reports (e.g., Title I allows one year for completion of necessary accounting reports). Such excessive periods result in procrastination in the preparation of reports and leave inadequate time for a proper audit. Mr. Paul suggested that 120 days would be a more practical time period for requiring reports. He noted, however, that exceptions could be granted where special circumstances warrant.

Grants require audits, yet grant budgets frequently do not include adequate amounts to cover the cost of a proper audit. Mr. Paul urged that adequate funds be included in the grant budget or by the granting agency.

Mr. Paul then described the organization and functions of the Baltimore City Auditor's Office, and discussed a new prequalification procedure for contractors and subcontractors who wish to bid on city contracts. The essence of the procedure involves annual proof of qualification for work to be performed before a contractor is permitted to submit a bid. Mr. Paul cited an example of abuse which led to the development of the prequalification procedure:

- A contract for a recreation area included a subcontract for a fence. The fence was found to be substandard; there had been improper substitution of materials; the fence mesh was of improper size, etc.

Mr. Paul concluded with some examples of his office's findings in education and health programs:

- An audit of food services at the city hospitals revealed that the quantity of food purchased exceeded the amount which could have been consumed by patients and staff. Further investigation resulted in the apprehension and conviction of the Director of Food Services, who had been ordering excess food and selling it to a fencing operation.
- A social services certification officer for the city hospitals obtained a book of receipts. He gave receipts to patients in return for cash, certified to the hospital that the patients were unable to pay, and pocketed the cash. The individual was arrested. Mr. Paul urged that strict controls be maintained over receipts.
- An audit of hospital blood donor program found that a hospital employee was being paid out of blood collection grant funds for blood which had never been collected. An investigation revealed that the grant administrator had paid the employee as a donor, in order to compensate her for extra work effort.
- A hospital cost accounting supervisor was found to be preparing petty cash reimbursement slips and submitting phoney receipts in order to obtain payment for non-existent purchases. The supervisor also forged the signature of an authorizing official. Mr. Paul urged careful scrutiny of petty cash reimbursements.
- An audit of handicaped children's program found a $69,000 overcharge by a cab company which had contracted to provide transportation. A restitution action resulted in recovery of about $55,600 from the company and termination of the contract.

Mr. Paul concluded by recommending that ef-

fective internal controls and a capable audit organization can contribute much to the prevention and detection of losses through fraud, abuse, and error.

Willis Holding, Jr., Former State Purchasing Director for the State of North Carolina, discussed procurement under Federal grants. He noted that there is an apparent lack of familiarity on the part of Federal agencies with the laws and methods of State and local buying.

He asserted that, for the most part, State and local purchasing is characterized by openness, fairness, impartiality, competence, and accountability. It is important to note, however, that all of these elements can be in place without conformity in organization or techniques.

Mr. Holding expressed concern with Mr. Fettig's suggestion regarding certification of State and local procurement systems, and recommended that State and local entities be maintained as laboratories for the development of new and innovative ideas and the testing of such ideas with minimum risk. Disparity, rather than conformity, should be encouraged.

The value of a variety of approaches has been demonstrated by the number of innovations that have arisen in State and local purchasing over the past twenty years. Three significant examinations of State and local purchasing have been made since 1967. These examinations revealed that the general health of State and local purchasing is good, although there is some unevenness.

Mr. Holding noted that it is important to distinguish between purchasing and procurement: purchasing connotes buying, while procurement encompasses acquisition, warehousing and distribution, transfer, disposition, and possibly uitilization. Mr. Holding then described the genesis of the Model State and Local Procurement Code and discussed how the code would further strengthen State and local purchasing.

Among the probable salutary effects of the Model Code, Mr. Holding cited the following:

- reducing undue political or other outside influence on purchasing decisions;
- placing responsibility for procurement policies and procedures in one place;
- defining the fundmentals to be employed in the competitive process;
- specifying extensive documentation;
- requiring cost and price analyses, where appropriate;
- guarding against conflicts of interest;
- providing mechanisms for resolving vendor protests and contractor disputes; and,
- encouraging surveillance against price-

fixing and collusive practices.

Mr. Holding noted that more general benefits will derive from the attention the Model Code will bring to the importance of the procurement function and from the focus on correct principles which will be required of legislative, executive, and administrative leaders.

Another ongoing program for strengthening State and local purchasing consists of a nation-wide series of training seminars being conducted by the National Institute of Governmental Purchasing. These seminars are not only enchancing skills, they are also leading to formal testing and certification of competence.

Mr. Holding asserted that the Model Code, if adopted, will add assurances that procurements under Federal grants are resulting in effective and efficient use of funds. He described problem areas which currently plague procurements under Federal grants:

- Grantor imposed procedures and reporting requirements which range from impractical to impossible.
- Grant procurement provisions are couched

in Federal terms and based on Federal concepts, but State and local purchasing can be more imaginative, innovative, and productive than the Federal system. In this connection, although most Federal purchases are not made under sealed, competitive bidding, this method is the rule and a legal requirement for State and local purchases.

- Failure of Federal grantors to coordinate procurement provisions with the Office of Federal Procurement Policy makes it difficult for State and local purchasing officers to ascertain the correct requirements.

Mr. Holding concluded his remarks by asserting that public funds should be treated alike, once they are in the Treasury. Such funds should receive the same care and stewardship, regardless of source. The Model Code, and the regulations to be developed thereunder, will include safeguards against fraud, and reduce chances for abuse and error. They will help assure the integrity of purchasing procedures and decision making, thereby fostering the proper utilization of Federal grant funds.

V. WORKSHOP—"THE ROLE OF MANAGEMENT SYSTEMS IN CONTROLLING FRAUD, ABUSE, AND ERROR"

Moderator

Frederick M. Bohen
Assistant Secretary for Management and Budget
HEW

Panel A

John T. Dempsey
Director, Department of Social Services
State of Michigan

John F. Briggs
Consultant to the Economic Development Council
of New York City and the New York City
Mayor's Office of Management

Robert Anthony
Walker Professor of Management Control
Howard Business School

Alvin M. Thacker, Jr.
Former Director
Office of Administrative Review
West Virginia Department of Welfare

Barbara Wamsley
Director, Office of Program Integrity
Office of Management Analysis and Systems
HEW

Staff Reporter

Bonnie Fisher
Office of the Assistant Secretary for Management
and Budget
HEW

Summary of Discussion

Moderator Frederick Bohen, HEW Assistant Secretary for Management and Budget, indicated that the purpose of the workshop was "to examine old issues of public management in a new climate," a climate of fiscal austerity. He noted that efficiency is now the central challenge, and accountability is crucial. The issues are not academic ones. The panel members, given their diverse backgrounds and high degree of expertise, were in an excellent position to reflect on the problems and recommend solutions or remedies.

John Dempsey, Director of the Michigan Department of Social Services, was the first speaker. In quoting from Peter Drucker, Mr. Dempsey said: "Good management systems are an alternative to tyranny," From his own experience, Mr. Dempsey observed that they are

also an alternative to anarchy. He then outlined the differences between management in the public sector and management in the private sector. These differences are in: goals; structure; utilization of resources; and, in the continuity of top leadership. The key problems, as Mr. Dempsey sees them, are in the rigidities built into the public sector and the ways top management is chosen. While he acknowledged that public programs were often unfairly criticized for being disproportionately ridden with fraud, abuse, and error, he noted that there is substantial room for improvement. Mr. Dempsey stressed the importance of managing systematically: 1) knowing and understanding the goals of the organization; 2) being aware of the gap between performance and intent; and 3) establishing good management control systems. Such control systems should divide the problems into component parts, define measurable

objectives, set priorities, and monitor the results to measure performance achievements. Accountability, to the public and to the Legislature, is the primary goal. Mr. Dempsey concluded his presentation by discussing the Michigan system within this framework.

Robert Anthony, Walker Professor of Management Control, Harvard Business School, also commented on the issue of the general accountability of management. While Dr. Anthony noted that private corporations are not necessarily better managed than are public agencies, in his view the management systems in most public agencies are antiquated. Where profit-making organizations are able to measure success by dollar profit, nonprofit organizations cannot. Therefore, nonprofit organizations have to work much arder to demonstrate success. Dr. Anthony outlined three technical points which characterize good management systems: 1) they are expense based, enabling good cost/benefit analyses; 2) accounting and budgetary processes are tied together; and 3) they have good output measures, which serve as a substitute for profit in nonprofit or public organizations. The management-by-objective (MBO) approach must be used to educate program planners and operators. Professor Anthony noted that the implementation and success of systems improvements depends, above all, on the active support of top management in the organization. Without such support, no systems changes, no matter how innovative, will be effective.

John F. Briggs, Consultant to the Economic Development Council of New York City and the New York City Mayor's Office of Management, discussed the role of management controls in administering health care systems. He urged that systems be viewed as tools which assist the manager in completing tasks. Mr. Briggs defined management as the art of motivating someone else to do what you want done. The problem is knowing what you want done, and setting goals and performance objectives. He cited the Health and Hospital Corporation of New York City as a case study, and stressed that the objective of management controls needs to be improved management and not the reduction of costs. In connection with reducing fraud and abuse, Mr. Briggs recommended looking at new techniques and ideas, and cautioned that technologically based systems could become the biggest barrier to improved management due to reluctance to lose money invested in them. He concluded his remarks by stating that management needs to have leeway to ex-

periment and perform; where it doesn't perform it should be replaced.

Alvin M. Thacker, Jr., Former Director of the West Virginia Welfare Department's Office of Administrative Review, discussed how States can use data generated by Federally required reporting systems (i.e., Quality Control Systems) to reduce fraud, abuse, and waste in the programs they administer. Referring to Dr. Anthony's comment on the need for a management-by-objectives approach, Mr. Thacker noted that in public agencies the system tended to break down after progress was measured against performance indicators. To eliminate errors, the causes of error must be determined and goals must be set which recognize the constraints of the system. Appropriate corrective action has to be undertaken. Based on his review of Quality Control (QC) data, Mr. Thacker considers it illegitimate to place all blame for fraud, abuse, and error on the client. In actuality, he stated, "less than one-half the errors resulted from wilfull misrepresentation by the client."

In conclusion, Mr. Thacker stressed the need to standardize and simplify Federal requirements of the diverse "welfare" programs. Those Federal changes would, in addition to facilitating the efficient management of programs, also increase the utility of quality control data in reducing fraud, abuse, and waste in the welfare system.

Barbara Wamsley, Director, Office of Program Integrity, HEW/OMAS, described the Department's utilization of the management-by-objectives approach to track performance outcomes and the reduction of fraud, abuse, and errors in programs. Specifically, she outlined the Management Initiatives Tracking System (MITS) and the new fraud, abuse, and waste tracking system (FAW) within the Office of Management Analysis and Systems. Examples of initiatives within each system were provided, in addition to a description of the processes involved. Ms. Wamsley reiterated Dr. Anthony's observation that top management support was an essential precondition of effective organizational change. Ms. Wamsley noted that Secretary Califano has given his full support to both the MITS and FAW initiatives, and these initiatives have been extremely successful in accomplishing their missions. Ms. Wamsley marked, however, that the success of HEW's use of management control systems resulted, in part, from the fact that these systems were flexible and selective, stressing only those issues or areas of major concern to the Secretary.

With regard to the FAW system, Ms. Wamsley acknowledged that the potential had yet to be realized. Ultimate achievement of the $1.1 billion savings goal, through the reduction of fraud, abuse, and waste, will depend upon the cooperation and assistance of States and localities. Ms. Wamsley ended her remarks by requesting and urging that assistance.

Mr. Bohen closed the session by reiterating the need for accountability in public programs. Organizational deficiencies require new ideas and a more effective use of management control systems. Yet, he cautioned, no system is a substitute for the commitment of top-level leadership and the recruitment of good, competent staff.
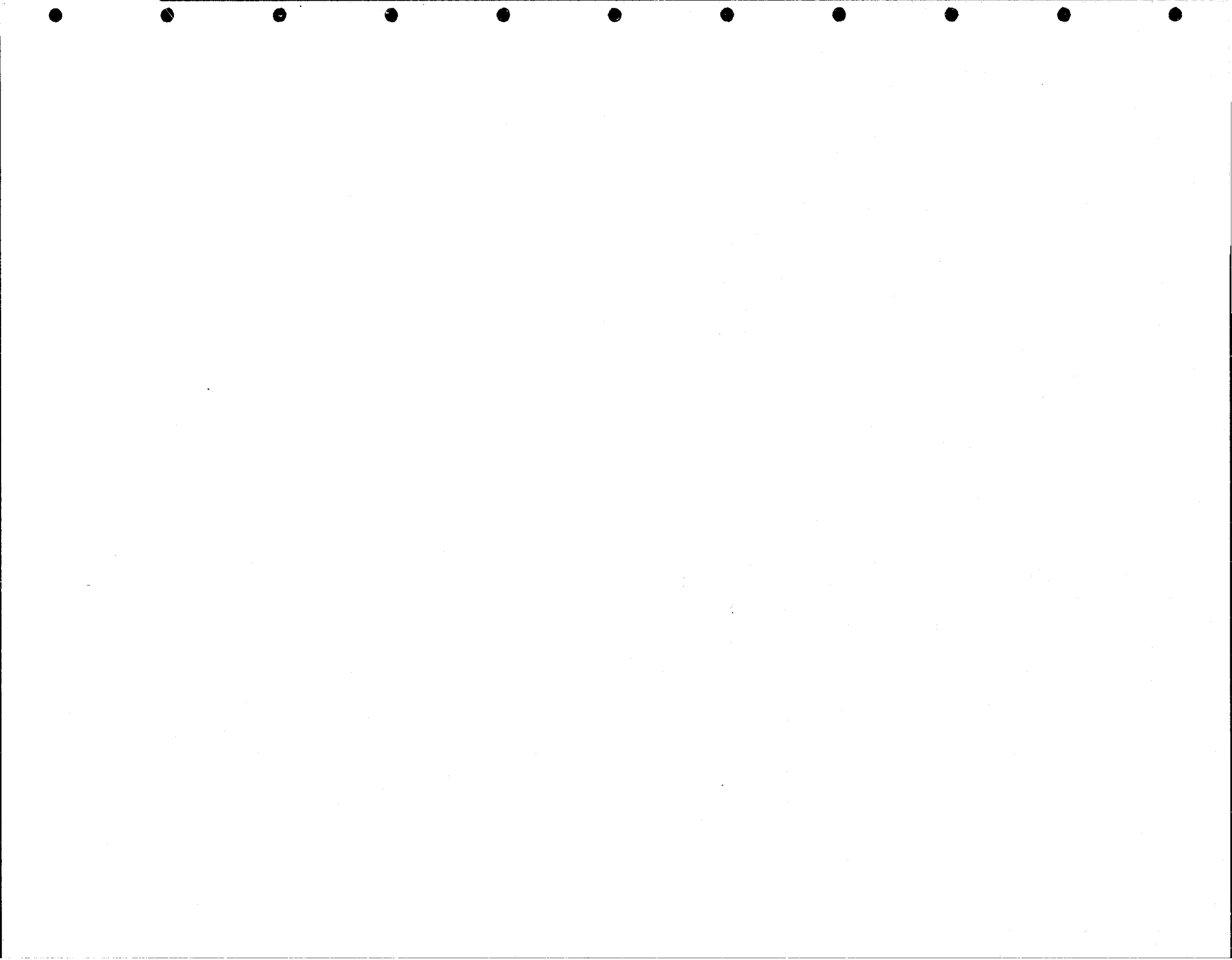
V. WORKSHOP—"THE ROLE OF MANAGEMENT SYSTEMS IN CONTROLLING FRAUD, ABUSE, AND ERROR"

Panel B

Leader

David St. John
Assistant Deputy Under Secretary for
  Intergovernmental Affairs
HEW

Panelists

David Pingree
Assistant Secretary for Administrative Services
Florida Department of Health and
  Rehabilitative Services

Peter Wynn
Deputy Commissioner for Administration
New York State Department of Social Services

Alvin M. Thacker, Jr.
Former Director
Office of Administrative Review
West Virginia Department of Welfare

Staff Reporter

Harry A. Hadd .
Office of the Assistant Secretary for
  Management and Budget
HEW

Summary of Discussion

David St. John, Assistant Deputy Under Secretary for Intergovernmental Affairs, HEW, opened the second panel discussion of the workshop. He introduced two panelists who briefly described management organizations/systems used in their states to control fraud, abuse and error.

David Pingree, Assistant Secretary for Administrative Services, Florida State Department of Health and Rehabilitative Services, outlined how Florida deals with fraud and abuse in a large umbrella organization. He noted that the State had complete administrative responsibility for all programs and for the delivery of services. However, he pointed out that within the umbrella organization, fraud and abuse activities were fragmented among the three major components of the agency: Administrative Services, Program Operations, and Program Plan-

ning. Administrative Services manages the quality control function. This unit works closely with district office personnel and processes all potential cases of fraud or abuse from initiation to the beginning of prosecution. At that point, cases are transferred to the Division of the Auditor General (outside of the agency) for litigation. The Assistant Secretary for Program Planning has no line authority, but conducts quality assurance activities and based on findings (e.g., error reports), assists the Assistant Secretary for Operations in developing corrective action plans to eliminate problem areas. Through close coordination among the three components, aided by active interest from the Secretary of the Department, this approach to handling fraud and abuse has worked well in Florida.

Peter Wynn, Deputy Commissioner for Administration, New York Department of Social Services, briefly described his Department's suc-

cessful efforts to implement a Medicaid management information system in New York City. He also discussed the merits of front-end edit checks versus back-end audits. He noted that his unit's emphasis on back-end audits was probably wrong. However, he observed that it is easier to obtain authorization to hire 50 investigators, accountants, etc., for audit quality control for a Medicaid fraud and abuse audit, than it is to obtain authorization to hire 10 persons to properly train income maintenance intake workers and thereby reduce incorrect payments at the front end. Mr. Wynn noted that the reporting of large-dollar savings through back-end audits tends to highlight these activities to the detriment of front-end efforts.

Summary of Questions, Answers, and Comments

Comment: Philip Laven, HCFA, Office of Integrity, endorsed the need for more emphasis on edit checks and other prepayment actvities. He also said that organizations should not concentrate solely on the dollars recovered but should attempt to find out why money was paid out incorrectly in the first place.

Q. Dr. Karameti, Nassau County, asked Mr. Wynn whether New York City was disqualifying providers who provided poor care, noting that in Nassau County much of the recoupment effort revolved around the question of quality of care.

A. Mr. Wynn replied that New York City was not adequately addressing this problem and had no coherent, careful program to monitor the quality of care. He added that currently the City was disqualifying providers only in the most blatant cases.

Q. Dr. Hayes stated that in Virginia, PSROs were monitoring quality of care. He then asked Mr. Wynn to describe his fraud unit's relationship to New York's Office of Special Prosecutor.

A. Mr. Wynn said that his organization was working closely with the Special Prosecutor. His department concentrated on detection and investigation, and when prosecution appeared appropriate, cases were turned over to the Special Prosecutor. He noted that, prior to the Special Prosecutor, his unit turned cases over to local county prosecutors, and these prosecutors did not always aggressively follow-up on cases. He felt that the advantage of a

Special Prosecutor was that this Office is an available resource ready to prosecute cases.

Comment: Marvin Renglin, Counsel for Nassau County, explained that his fraud unit and Special Prosecutor use a joint team concept. Both units pool their resources (e.g., computers, personnel) and work together in processing cases from the initial detection through prosecution.

In comments on front-end versus back-end activities, Mr. Renglin said that, philosophically, the front end made a good deal of sense but was doomed to failure. He noted that computer edits were effective but if the process held up the payment of claims for too long a period of time, political pressure would force by-passing the edits. He also noted that when institutional providers were operating on the edge of bankruptcy, agencies had to concentrate on reducing the number of days required to process claims and this limited the effectiveness of front-end edit activities. Dr. Hayes said Virginia used sophisticated front-end cross edits to concentrate on physicians and pharmacists and used post-edit detailed audits for institutions.

Mr. Pingree said his department had had to periodically shut off its edits to get payments to providers and noted that this was one reason why back-end audits were so necessary.

Q. Jim Parham, HEW Deputy Assistant Secretary for Human Development Services, inquired if Florida's umbrella organization had led to improved management of social service programs, increased productivity, and better identification of actual costs.

A. Mr. Pingree replied that the Department had better and more accurate data available for the managers to use, that delays in implementing management-by-objectives, workload measurement, and productivity systems had seriously limited the Department's advances in areas that Mr. Parham asked about. Mr. St. John added that Florida had developed a single fee structure and an unduplicated count of clients served by the Department's social service programs, and that these advances had proved beneficial.

Q. Dr. Karameti raised a problem of clients entering Medicaid through the Medicare program.

A. Mr. Parham pointed out that the Health Care Financing Administration (HCFA) was formed to bring these two programs

closer together, and he suggested that Dr. Karameti contact HCFA's Administrator, Leonard D. Schaeffer, and outline the problem in greater detail.

VI. ACCESS TO INFORMATION WORKSHOP
Panel A: "Government Access to Individual Records: Medical, Financial, and Educational"

Chairperson

Alan F. Westin
Professor of Law
Columbia University

Panelists

Richard Neustadt
Assistant Director
Domestic Policy Staff
The White House

Charles F. C. Ruff
Associate Deputy Attorney General
U.S. Department of Justice

Trudy Hayden
Director of Public Information
Office of the Deputy Mayor for Criminal Justice
New York City
(Former Director—American Civil Liberties
   Union Privacy Project)

Staff Reporter

Susan Callahan
Attorney—Advisor
Inspector General Division
OGC/HEW

Summary of Discussion

Dr. Alan F. Westin, Professor of Law, Columbia University, and Chairperson of the Panel, opened the discussion by summarizing the characteristics of individual record information systems. He stated that the two key characteristics of these information systems are that they reveal sensitive personal aspects about individuals, and that there is an expectation by persons whose records are contained in the system that the data collector has a fiduciary duty to protect that information. People will not give accurate information about themselves if they believe that this fiduciary duty will be breached; he termed this phenomenon as "an information strike." In our technological age, there is a tendency to try to collect a wide range of information about an individual. This information gives a picture of a "whole person." Dr. Westin noted that some argue that an information system containing information on a "whole person" assists govern-

ment agencies in treating problems of individuals. However, the definition of personal privacy is that individuals select what they reveal to others; the "whole person" concept is antithetical to this. Rather, the "whole person" concept is, in essence, the basis for an authoritarian society. Dr. Westin concluded by cautioning that the courts should not be relied upon to resist demands for use of information beyond the purposes for which the information was collected.

Charles F. C. Ruff, Associate Deputy U. S. Attorney General, stated that current analysis of the issue of government access to individual records should be focused on creating a rational process for decision-making. It is difficult to define the precise boundary of a person's right to privacy, and the Fourth Amendment provides only the vaguest guidance on this issue. In Mr. Ruff's view, the traditional perception of the right to privacy is flexible. He indicated that the Right to Financial Privacy Act of 1978 may be a model for other areas where decisions are

needed concerning the relationship between individual rights and the needs of government access to records of individuals. He noted that a balance must be struck between these two interests. In reaching this balance, each side should try to avoid attributing evil motives to the opposite side. The rhetoric which has characterized debate on this issue should also be avoided.

Trudy Hayden, Director of Public Information, Office of the New York City Deputy Mayor for Criminal Justice, stated that it may already be too late to discuss individual privacy issues in the traditional manner. While the discussion so far has been based on the assumption that record systems have definable bour 'aries, the advent of computer matching and scanning has caused record systems to lose their traditional boundaries. Using computer techniques, information can be obtained without identifying the name of the persons whose records are being sought. This type of computer search is invisible to those whose records are involved. Ms. Hayden foresees a time when this technique will abolish the traditional boundary between government record systems and private record systems. Although she did not offer any alternatives for accomplishing the results obtained from computer matching, Ms. Hayden noted that this computer technique will eventually be used in every aspect of our life, particularly when electronic fund transfers become operational. She urged that legislators be

more aware of this potential for invasion of privacy when they draft legislation. Finally, Ms. Hayden indicated that the draconian aspects of computer matching and scanning techniques might be reduced if government programs are simplified, thereby reducing the need for extensive files of information on individuals.

Richard Neustadt, Assistant Director of the White House Domestic Policy Staff, observed that people are becoming increasingly apprehensive about the power of recorded data. He also noted that, as a general rule, people are not willing to cripple law enforcement. However, on this issue we can "have our cake and eat it too," by three means: (1) formalizing the process of access to government information files; (2) requiring use of formal legal process to obtain access to these files; and (3) where possible, giving the individual the right to challenge access by a third party. Mr. Neustadt remarked that while, for cost reasons, it might not be possible to institute these procedures for all record systems, the procedures can be implemented for the most important government record systems. He cited the Right to Financial Privacy Act of 1978 and the OMB Proposed Guidelines on Computer Matching Programs, as exemplifying the procedures he believes can be established to protect the rights of individuals without crippling the interests of law enforcement.

VI. ACCESS TO INFORMATION WORKSHOP
Panel B: "Public and Press Access: How Much Freedom of Information"

Chairperson

Eileen Shanahan
Assistant Secretary for Public Affairs
HEW

Panelists

Jack Nelson
Bureau Chief *Los Angeles Times*

Timothy H. Ingram
Staff Director
Subcommittee on Government Information and Individual Rights
Committee on Government Operations
U. S. House of Representatives

Ronald Plesser
Former General Counsel
Privacy Protection Study Commission

Earl J. Silbert
United States Attorney
District of Columbia

Staff Reporter

Judith Bekelman
Executive Assistant to the Assistant Secretary for Public Affairs
HEW

Summary of Discussion

Panelists represented a spectrum of opinion on reconciling the conflict between the press's and the public's right to know about informat'on held by government on the one hand, and government's inclination to protect information about investigations and the privacy rights of individuals involved.

Timothy H. Ingram, Staff Director of the House Subcommittee on Government Information and Individual Rights, cited the conflict between press interest and the need to protect investigative files which often contain the names of informants, unverified allegations, and sometimes false speculation. He noted that while the press often checks the accuracy of "leaked" information with agency officials, there seems to be an assumption that "officially" released investigative information is accurate. Hence, additional verification of such information is seldom requested.

Mr. Ingram concluded that government should do more to assure the accuracy of individual's

records before releasing them to the public. He noted that it might be time for Congressional examination of the accuracy of agency records and that the Subcommittee on Government Information and Individual Rights planned to study the impact of Exemption 7, that provision of the Freedom of Information Act which deals with investigatory records compiled for law enforcement purposes. Finally, he commented that there are no Federal guidelines on release of arrest records, an area in which agencies exercise great discretion.

Ronald Plesser, former General Counsel for the Privacy Protection Study Commission, and currently practicing law in Washington, provided another point of view in citing the Freedom of Information Act as the primary tool for instilling public confidence in government and in guarding against secret government activities. He noted that citizens are better prepared to make decisions about their own lives if government is open. The hard questions, he felt, involve determining which levels of government and related agencies

are covered by the Freedom of Information Act; which materials should be disclosed; and when to exercise the exemptions to disclosing information. Mr. Plesser cited a recent court decision, which permitted a newspaper access to FBI logs on a criminal figure, as evidence that public interest in disclosure of information can be more important than an individual's privacy interest. He noted that the courts have led the way in increased disclosure under the Freedom of Information Act.

Earl J. Silbert, U.S. Attorney for the District of Columbia, raised another issue which results from increasing reliance on the criminal justice process to resolve allegations of fraud and corruption against public officials who violate the public's trust. Conflicts with public and press access to information are built into the criminal process, he said, because of the need to protect the investigative process, the rights of those under investigation, and the identity of witnesses. The criminal justice system, which is necessarily secret, slow, and deliberate, does not meet the public's need to have facts brought to light quickly about abuse of public trust. As a result, the public depends on the news media for infor-

mation which, often based on leaks from criminal investigations, may be inaccurate.

Jack Nelson, Washington Bureau Chief of the *Los Angeles Times*, asserted that if information were not leaked to the press, the public would not have uncovered examples of official lying, such as Watergate and Cointelpro. He suggested that prosecutors assist the press to get accurate information to the public. He also noted that compliance with the Freedom of Information Act varies among government agencies, and many roadblocks such as time delays, travel to copy material, etc., are presented to reporters, Mr. Nelson noted that President Carter, in an interview, had stated that the news media ought to do more to detect fraud and abuse in government, and that the attitude in government should be that those with information will come forward.

In closing the session, Eileen Shanahan, HEW Assistant Secretary for Public Affairs and Chairperson of the Panel, advised government officials at all levels to consider, in advance of a press query, how to deal with questions at any stage of an investigation, in order to respond to the public's right to know.

LUNCHEON SESSION—THURSDAY, DECEMBER 14

Introduction of Secretary Califano

By Thomas D. Morris, *Inspector General, U.S. Department of Health, Education, and Welfare*

Several members of the head table submitted a petition yesterday asking the planning committee, headed by Dan Meltzer, to yield us 90 seconds to thank Secretary Califano for this Conference. I think I speak for most of you, if not all of you, in this room when I say that the past day and a half have indeed been a remarkable experience. Never in my memory have so many significant officials, including the very top of our Federal Government, and officials from the States, come together to talk about a subject which is too often considered mundane, namely better management. The interest which you have shown here today is, first a tribute to the importance of this subject to the public interest (i.e., greater economy and efficiency), and to the interest of our clients (i.e., greater effectiveness). It also is a tribute to the remarkable leadership of Secretary Califano.

To introduce Mr. Califano to this audience would be an empty gesture. You know his background as well as I—his great experience in the Defense Department, then as President Johnson's architect of the Great Society, then as an eminently successful lawyer. But those events do not explain why he has been able to gather about him at HEW so many superb people, such as those you have met here in the past two days, the leaders of HEW. The reason is Mr. Califano's determination and ability to truly manage HEW programs. You may recall that shortly after he came into office, he said, "I'd like to demonstrate to the American people that HEW can be managed. The importance of that is to show that we can make investments in social services and social programs for the most vulnerable in society in an efficient way." And he's made believers of all of us!

So it's with great pleasure that I introduce to you the leader whom we all admire and want to work harder for, Secretary Califano.

REMARKS

Honorable Joseph A. Califano, Jr., *Secretary of Health, Education, and Welfare*

With this luncheon, we reach the end of this Conference. We have, in these two days, taxed not only your intellects—but your ears, your patience and your capacity to sit for long periods. Accordingly, I intend to be brief.

But I do think it is fitting that we have a summing up: that we assess, in Abraham Lincoln's words, "how far we have come and whither we are tending."

What have we achieved in these two days?

Four things I hope.

First, I hope this Conference has succeeded in underscoring the progress we are making nationwide—often dramatic progress—in overcoming fraud, abuse and error.

Many states and localities have done well in the welfare field; to take one example:

- San Francisco County, by vigorously tightening up the management of its welfare program, reduced overpayment and ineligible-payment error rates from 20 percent in early 1979 to 1.3 percent in early 1977.

- Kent County, Michigan slashed welfare-payment errors to 1.6 percent, less than one-fifth the national average—largely by making it easier for workers and clients to find the right answers to frequently-asked question about various programs.

- West Virginia, in the past few years, has pioneered in improving AFDC error rates —and has cut its error rates by more than half, from 10.2 percent in late 1973 to 4.9 percent in late 1977.

Many other states and localities have taken equally impressive steps, in AFDC and other programs. Their successful efforts have been the models for several efforts at the Federal level:

- Project MATCH, for example, HEW's computer-matching program to monitor improper welfare payments has been an impressive success. As of mid-November, we had turned over to the states more than 18,000 cases for investigation. More than 3,800 individuals have already been

found ineligible or overpaid. Project MATCH, which has cost the Federal government only $1 million, will yield $12 million in direct savings to the states and Washington, plus aditional savings in the Food Stamp and Medicaid programs.

- Project INTEGRITY, the computerized search for dishonest Medicaid doctors and druggists, has yielded 25 indictments, 8 convictions, and nearly $3 million in claims for restitution of Government funds, plus other savings.
- Since we began reforming the government's student aid programs, we have dramatically increased the number of defaulters who have begun or completed repayment; the repayment rate for the final quarter of fiscal 1978 was 6 times the rate for the same quarter in 1977. Collections are now running at an annual rate of $25 million—up from $20 million only a month ago. And the backlog of defaulted loans in going down, not up, for the first time in history.
- All told, through these and other efforts in the past two years—reducing error rates, increasing competitive procurements, simplifying paperwork, improving the productivity of people and programs—we have achieved savings conservatively estimated at half a billion dollars.

Last February, we launched a new system for validating information submitted by students seeking Basic Educational Opportunity Grants. This program awards grants for college expenses to students from low and middle-income families; a student's eligibility, and the size of his grant, depend upon his family's income and a variety of related data. This is one of our largest education programs—it spends about $2 billion dollars, and handles 4 million applications, each year. But for years, there was no effective screening system to ensure that these massive sums were being spent only for eligible students.

Today I can anounce a major achievement in our effort to reform that system. Preliminary results from the new system we put in place 10 months ago—are, in my judgment, astounding. They suggest that nearly 500,000 applicants, as of now, were rejected, while many others were approved only for smaller grants. These applicants have until March to prove that they are entitled to participate in the program, or to obtain larger grants. But our best estimates suggest that this new system will reduce costs by $300 to $500 million in this school year. This is a staggering saving—and a saving in addition to

the 500 million dollars we have already saved by other management improvements.

Such achievements as these have significance far deeper than the numbers game of dollars saved or indictments handed down. They mean that we are freeing resources to help the truly needy. They mean that investments in better management pay off handsomely. Above all, they mean that government—local, State and Federal government— can aim for high quality and achieve it; that government *can* work. The real dividends are increased human wellbeing and restored public trust in some very worthwhile programs.

But we cannot rest on our laurels—not even half a billion dollars' worth.

So my second hope as I contemplate the contributions of this Conference, is that it will prove to be a breeding-ground for new initiatives, new techniques, new programs across the nation to sharpen management and guard integrity.

When we were planning this Conference, I admonished my staff at HEW to listen, not just talk. They tell me they have done that; I hope so. For I remember Mr. Justice Brandeis' observation, years ago, that one glory of the American Federal system is that it provides a multitude of State and local laboratories for social and political innovation. We in Washington have become increasingly modest about our ability to impose solutions from above; and we are becoming more open to solutions that originate in the states and cities and counties.

One initiative announced at this Conference is an effort to streamline and simplify application procedures, which the President discussed yesterday. This initiative is a direct response to complaints and suggestions that have come to us from citizens and officials at the State and local levels.

In one city, an average case file contains 700 application documents.

In some places, if you need public assistance, you may fill out 60 separate forms.

This situation truly adds insult to injury—and we intend to improve things: for your sake, for our sake, and for the sake of needy people. Our goal is to devise, if we can, uniform standards of eligibility for programs of public assistance.

Very briefly today—as we prepare to go home from the breeding-ground—I want to announce several other new efforts. They are Federal initiatives—but each responds to ideas we have gathered from State and local officials, from clients and service providers. Each should interest you—and each promises to save the American taxpayer many millions of dollars:

- The Social Security Administration is

launching an important new management initiative, dealing with a large but little-known Federal program—benefits paid by the Social Security system to students who are children of dead or disabled Social Security beneficiaries. Though this provision of the Social Security law is not well-known, it is hardly insignificant: at present, we pay out $1.6 billion a year to more than 900,000 young people. In order to qualify, these young people must be enrolled as full-time students. But because reporting and monitoring systems have been seriously inadequate, the system has been unable to verify whether students who continue to receive benefits are still in school full-time.

We are therefore creating a new system designed to provide accurate, up-to-date information on enrollment status—and to ensure that only students who qualify for benefits receive them.

The potential savings from this initiative, once the system is fully operational, could reach $100 million or more.

This system also highlights the opportunity to improve management through joint efforts by different programs. The Social Security Administration will rely on enrollment information provided by the Office of Education, which collects this information for its own programs. I intend to look for more and more of these kinds of joint ventures, and I hope you will do the same.

- A major problem in the administration of the AFDC program has been that states and localities lack vital information they need to make proper eligibility determinations. There is no systematic way, for example, for the city of New York to learn whether a welfare client is also obtaining benefits in Newark, New Jersey, or in lower Connecticut. Moreover, states and localities often lack accurate information to verify how much actual income a welfare applicant receives, and from what sources.

To meet these needs, I can announce today that by next September, we will have laid the. foundations for a new National Recipient System. Under this new system, States will supply HEW with identifying information. on every AFDC recipient; HEW will use this information to determine whether a recipient is receiving payments in more than one jurisdiction We will also give basic identifying information, such as date of birth or social security number, to Federal agencies so

that they can tell the states whether a recipient is obtaining Federal benefits.

This system will *not* create a comprehensive computer file that collects voluminous data on every welfare recipient. It will operate very differently, with built-in safeguards to protect the right of privacy. But the system will work.

We expect it, once it is fully operational, to eliminate millions of dollars of erroneous welfare payments.

- I can also announce today a new program to help banks and educational institutions collect from student loan recipients before these students default on their loans. Under this new "Pre-Claims Assistance Service," which we tested in San Francisco last summer, the Office of Education will help locate "lost" borrowers whose notes are 60 days past due; the Office of Education will send these "lost" borrowers a notice warning that unless they contact their bank or college and begin repaying the loan, Federal collection efforts may follow. After another 30 days, we will send a second, more forceful warning. There too, we have designed the system to safeguard individual privacy.

This experiment had impressive results in San Francisco. We believe that when operating nationwide, it can have major impact on reducing student loan defaults.

Third, I hope we have managed to put the problem of fraud, abuse and error in proper perspective.

This is highly important, and there are several points that need to be emphasized for the American people if they are to understand this issue:

- As the President pointed out yesterday the biggest source of waste in government is not fraud, but error.
- We need also to understand the fact that literally billions of dollars in waste is not the fault of agencies or providers but of the political system: it is "legislated waste"—waste created by the failure or refusal of Congress or State legislatures to pass laws we are urging them to pass. If Congress, for example, had passed the President's Hospital Cost Containment legislation this year, the nation could save between fiscal 1979 and 1983, $19 billion in hospital costs—the most rapidly rising item in the cost of living index.

Certainly great achievements are possible when legislatures and program agencies work together.

One striking example of this kind of partnership is in the new State Medicaid Fraud Control Units. Working with the states, 19 State units have already been set up to monitor the program. Nearly 800 attorneys, investigators, auditors and other professionals are already at work. Eight more states are in the process of setting up these units, with the states providing 10 percent of the money.

- We should remember that the goal of reducing error is not only to weed out those who are ineligible for our programs. It is also to make our programs available to all who truly need them. Some very poor people who are eligible for welfare help, for example, are mistakenly barred from getting the help they need; we need to apply our management skills to help them get on the rolls while we remove others who are not eligible. Helping those people is very much our aim.

And on this matter of putting things in perspective, we need to make another point ringingly, unmistakably clear: This Administration has no intention of singling out human service programs in its attack on fraud and abuse. That attack ranges across all government programs, as the President has said.

We are attacking fraud and abuse in the Small Business Administration, in employment programs, in defense contracting and in the tax system. We believe that poor and vulnerable people will be the beneficiaries of this effort—not its victims.

Fourth and finally, in addition to celebrating our achievements, generating new initiatives, and putting the issue in perspective, I hope this conference has heightened your enthusiasm for our work ahead.

Our job, after all, is far from over—and the most difficult efforts may lie ahead.

If the early, most dramatic successes are also the easiest to achieve, what remains is to solve the most persistent, unyielding problems.

We face the fact, for example, that we cannot act to correct a deficiency until we know what it is and how serious. Our information and reporting systems badly need improvement—but not the kind of improvement that chokes agencies and providers in red tape.

And by no means least, we face the fact of simple human inertia: the fact that programs—and people—begin with a flurry of enthusiasm only to grow weary and stale.

We must not let that happen.

We at HEW want to do what we can toward keeping enthusiasm high. And so today, in closing, I want to announce a new national award, honoring high achievement in conquering fraud, error and abuse.

In honor of a former HEW Secretary who is himself a symbol of distinguished public service and sterling integrity, we have chosen to name it the John W. Gardner Program Integrity Award. The presentations will be made yearly to citizens or officials—not employees of HEW—who have made exceptional contributions to protecting the integrity of HEW programs.

I hope that the next time we meet, it will be when I present the first Gardner Awards. And I hope that the first awards will be to someone in this room today, for an idea born at this Conference.

So we come to the end of our deliberations.

I congratulate you for your powers of endurance—and I'm grateful to you for contributing to this gathering.

No contribution could mean more to the cause of helping needy people—or to restoring public faith in our Democratic system.

By your efforts, you have helped ensure that we will inform our national compassion with competence; that we will match our generous instincts with intelligence and integrity.

We will do these things because the American people are demanding it. But we will act for another reason also: Because it is right.

Thank you.

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