Economic Impact Analysis
Virginia Department of Planning and Budget

22 VAC 40-325 – Fraud Reduction/Elimination Effort
State Board of Social Services
September 28, 2004

The Department of Planning and Budget (DPB) has analyzed the economic impact of this proposed regulation in accordance with Section 2.2-4007.G of the Administrative Process Act and Executive Order Number 21 (02). Section 2.2-4007.G requires that such economic impact analyses include, but need not be limited to, the projected number of businesses or other entities to whom the regulation would apply, the identity of any localities and types of businesses or other entities particularly affected, the projected number of persons and employment positions to be affected, the projected costs to affected businesses or entities to implement or comply with the regulation, and the impact on the use and value of private property. The analysis presented below represents DPB's best estimate of these economic impacts.

Summary of the Proposed Regulation

The proposed regulations require that expenditures incurred by dedicated fraud prevention units at local departments of social services are reimbursed according to a new methodology. The methodology is to be developed by a work group convened by the commissioner of Department of Social Services (DSS), consisting of representatives from local departments and senior managers from DSS. The proposed regulations also establish performance expectations for local departments of social services.

Estimated Economic Impact

The proposed regulations contain rules for the Fraud Reduction/Elimination Effort (FREE) program administered by the DSS. This is a statewide program to ensure that fraud prevention and investigation goals are pursued for Virginia's public assistance programs. Pursuant to section §63.2-526 of the Code of Virginia, each local department of social services is mandated to establish a fraud prevention and investigation unit, but only insofar as money is appropriated to cover their costs. Currently, DSS reimburses all administrative costs relating to the operation of these units and all 120 local departments have a fraud prevention and investigation unit. These units currently employ a total of about 93 full-time equivalent positions.

The funding sources of the FREE program include the fraud recovery special fund, the general fund, and federal funds. Even though the general fund had been a source of funding in the past, no appropriation is currently provided for this purpose. Thus, the program relies mainly on the fraud recovery special fund for its state share of costs. This fund receives overpayment moneys (net of the federal share) recovered by local departments primarily in the food stamp program and Temporary Assistance for Needy Families (TANF). In fiscal year 2003, payments into the fraud recovery special fund from food stamp and TANF collections was about $1.4 million, compared to $2.1 million incurred by fraud prevention and investigation units in administrative costs. Based on these figures, the state share of revenues the program generates is about 64% of the administrative costs the state reimburses localities. Since the program does not generate enough revenues, DSS is unable to reimburse localities for the full administrative costs of local fraud units.

Thus, if the collections are not sufficient, local departments are no longer likely to be reimbursed for the full administrative costs of their local fraud units. The extent of the funding is likely to be determined by overpayment collections by localities from the food stamp and TANF programs. In 2003, the ratio of collections to expenditures was less than one for about 80 out of 120 local departments. Because these local departments may no longer receive full funding for their administrative expenses, under statute, they have the option to terminate their dedicated fraud prevention and investigation units. Even if they decide to terminate their dedicated fraud unit, localities will continue to deposit overpayment recoveries to the fund, but they will not get reimbursed for their costs from the fund.

Less than full funding of expenditures may cause some departments to reduce their fraud unit staff. However, it will be in the best interest of localities to maintain dedicated fraud units. As they will be receiving some funding, they will be able to reap the advantages of having a dedicated fraud prevention unit without incurring the full costs of having one. The local departments have an obligation to detect and pursue fraud. One option available for them outside the FREE program is designating some eligibility workers for fraud prevention and detection activities. The funding for eligibility workers is provided 50% from federal sources, 30% from state sources, and 20% from local sources. However, continued participation in the FREE program is probably a better choice for local departments. Designating eligibility workers to pursuing fraud activity would take away from resources originally dedicated to eligibility determinations.

The proposed regulations require that the commissioner of DSS convene a work group consisting of local department representatives and senior department managers to develop a methodology for allocation of available funds to localities for fraud prevention and detection. Since local departments and the senior department managers will determine the allocation methodology, the interests of both sides will be represented in the work group. The likely economic effects of the change in reimbursement policy will depend on the final methodology developed by the work group. However, as the reimbursement methodology is yet to be developed, the potential effects of the proposed change are not known at this time.

In general, the way localities are allocated available funds for their fraud prevention efforts will affect the incentives to localities to crack down on fraud and, consequently, the benefits of each dollar that the state reimburses them for their fraud prevention activities. For example, if the funds are allocated regardless of a unit's performance, the full benefit of each dollar spent on fraud prevention may not be realized. Neither does allocating funds purely based on the recoveries of overpayments guarantee that good performance is rewarded. This is because (1) for recoveries to occur overpayments must have been made initially, which could be an indication of bad performance in preventing front-end fraud, and (2) distribution of overpayments among the localities may not be steady and may cause significant variations in the reimbursements regardless of how well the recovery efforts are orchestrated. For this specific case, it appears that fraud prevention efforts would be reasonably encouraged and supported by an allocation methodology that would provide a fixed amount of funding, independent of recoveries, to ensure continuity in fraud prevention efforts and a variable amount of funding based on indicators measuring staff performance as well as collection performance.

The proposed regulations will also allow DSS to develop, implement, and monitor local fraud unit performance expectations. DSS indicates that local department performances are already evaluated internally. The proposed language will provide authority to make this internal procedure external. Since performance evaluations are already done internally, there are not likely to be any significant additional costs as a result of the proposed changes. However, the external performance reviews may allow DSS to withhold funding if the performance expectations are not met. Thus, the proposed changes will provide some incentives to fraud units to maintain high performance standards. In addition, if the funding is reduced because performance expectations are not met, a local department may choose to no longer participate in the FREE program.

Businesses and Entities Affected

The proposed regulations apply to dedicated fraud units housed at 120 local departments of social services.

Localities Particularly Affected

The proposed regulations apply throughout the Commonwealth.

Projected Impact on Employment

The proposed funding methodology may cause some local departments to reduce staffing dedicated to fraud units, as they may no longer be reimbursed for the full costs of their fraud-related expenditures. Currently, local departments have approximately 93 full-time equivalent positions involved in detection and pursing fraud. Thus, this change may reduce the demand for labor by an unknown amount.

Effects on the Use and Value of Private Property

The proposed regulations are not expected to affect the use and value of private property.