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UNITED STATES GENERAL ACCOUNTING OFFICE
WASHINGTON, D.C. 20548

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HUMAN RESOURCES DIVISION

B-211805

JUNE 8, 1983

The Honorable Margaret M. Heckler
The Secretary of Health and Human Services

Dear Madam Secretary:

Subject: Several States Have Not Properly Implemented Certain AFDC Provisions of the Omnibus Budget Reconciliation Act of 1981 (GAO/HRD-83-56)

We have been monitoring the implementation of the provisions of title XXIII of the Omnibus Budget Reconciliation Act of 1981 (OBRA) (Public Law 97-35, Aug. 13, 1981), which affects the Aid to Families with Dependent Children (AFDC) program.[1] The administration estimated Federal savings of about $1 billion for fiscal year 1982 from implementing these changes.

We found variances in the way some States have implemented (1) the 150-percent income limit for eligibility, (2) the treatment of lump-sum income tax refunds as either a resource or income for eligibility and/or benefit payment amount purposes, and (3) special need allowances for pregnant women. These provisions were expected by the administration to save the Federal Government about $22 million in fiscal year 1982. The variances we found in implementation could result in the Government not realizing the full savings anticipated and may result in inequitable treatment of segments of the AFDC population. Because of the relatively limited scope of our monitoring effort, we did not estimate the savings that might not be realized.

OBJECTIVES, SCOPE, AND METHODOLOGY

Our objectives in monitoring implementation of title XXIII of Public Law 97-35 at the Federal and selected State and local levels were to assess the consistency between the implementing regulations, policies, and operating procedures and the act's provisions and to identify areas where the States may have been experiencing problems.

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[1]At the request of the House Committee on Ways and Means, GAO is also making a major study of the impact of the OBRA changes in the AFDC program that is to include ascertaining the economic well-being of AFDC households removed from the rolls. This study is under the direction of our Institute for Program Evaluation.

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We reviewed the legislative history and provisions of the act to understand the intent of the changes. We compared the implementing Federal regulations with the act and, in the four States visited,[2] compared State and local administrative directives with the Federal regulations for consistency.

Of the States visited, we selected and carried out work in New York first because it has the Nation's second largest AFDC caseload and accounts for over 10 percent of nationwide AFDC expenditures. We examined available information on the timing and effect of the provisions implemented and noted variances in the implementation of the 150-percent income limit, lump-sum payments, and special need allowances for pregnant women. We also selected and reviewed a sample of 727 earned income cases in three New York counties[3] which gave an indication of the impact of New York's application of the 150-percent income limit.

To ascertain whether our findings in New York were occurring elsewhere, we visited Florida, Georgia, and New Jersey. We selected New Jersey because it has a State-administered AFDC program, in contrast to New York's State-supervised, county-administered program. We expected to find more uniformity in applying the provisions in a State-administered program. We selected and carried out work in Florida and Georgia because they operate State-supervised/county-administered and State-administered AFDC programs, respectively, to obtain a different geographic perspective.

In each State visited, we spoke with State and local officials and examined selected case records and related information to determine the effects of implementing various AFDC provisions of OBRA. We found few implementation problems in Florida, Georgia, and New Jersey.

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[2]Florida, Georgia, New Jersey, and New York.

[3]Erie, Monroe, and Nassau counties.

To obtain a broader perspective, we also telephoned officials in 29 other States[4] to determine how they interpreted and implemented selected OBRA provisions. Although the scope of this inquiry was limited, we noted some variances in the way several of them had implemented the Federal regulations concerning the 150-percent income limit and special need allowances for pregnant women. These States were selected because their State plans before and after OBRA had the potential for problems concerning either or both of these provisions.

At the Federal level, we spoke with officials of your Office of Family Assistance (OFA) and of selected regional offices regarding implementation of various provisions and resolution of questions raised by States. We also discussed the results of our monitoring effort with the Acting Associate Commissioner of OFA and her staff, and their comments have been included in this report.

Our review was performed in accordance with generally accepted government audit standards.

IMPLEMENTATION REQUIREMENTS

Because of the increasing size and cost of the AFDC program in recent years, President Reagan made reform a major campaign initiative and established a set of goals to revamp the program. The Congress responded with Public Law 97-35, of which title XXIII contained 21 provisions designed to improve the AFDC program by:

--Limiting eligibility to those most in need.

--Strengthening the program's work requirements.

--Establishing AFDC as a temporary safety net for those who are not economically independent.

--Emphasizing individual responsibilities.

--Improving program administration.

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[4]California, Colorado, Delaware, the District of Columbia, Idaho, Illinois, Indiana, Kansas, Louisiana, Maryland, Massachusetts, Michigan, Minnesota, Montana, New Hampshire, New Mexico, Ohio, Oregon, Pennsylvania, Rhode Island, South Carolina, South Dakota, Tennessee, Utah, Vermont, Virginia, Washington, West Virginia, and Wisconsin.

The provisions fundamentally changed the AFDC program and required States to significantly change the way they administered the program. The provisions' effective date was October 1, 1981, unless a State could demonstrate to the Secretary of Health and Human Services (HHS) that legal barriers under State law prevented its compliance on that date. Of the four States we visited, only New York had been granted a delay (of 3 months) in implementing the provisions discussed in this report.

HHS issued interim regulations on September 21, 1981, and final regulations (Title 45, Code of Federal Regulations, Parts 200-499) on February 5, 1982, interpreting the title XXIII provisions. The regulations provided the basis for States to amend their program plans and bring the plans into conformance with the new Federal requirements for continuing program cost sharing.

FIVE STATES ARE NOT PROPERLY APPLYING THE 150-PERCENT TEST

Federal regulations provide that, as of October 1, 1981, the first step in determining an applicant/recipient family's financial eligibility for AFDC is to add to the State's standard of basic needs for the same size family any allowances for special needs and multiply the sum by 150 percent. This resulting amount is compared to the applicant/recipient family's total income, without any disregards. If that income exceeds the 150-percent limit, the applicant/recipient family is not eligible for AFDC benefits (applicants are denied benefits; recipients are terminated from the rolls). Of the 33 States visited and contacted, 21 offer special need allowances.

We noted two problems concerning application of the 150-percent income limit test. First, of these 21 States, 5--Illinois, New York, New Mexico, Pennsylvania, and Wisconsin--are not counting special need allowances in computing the 150-percent dollar standard, as required by the regulations, even though these allowances are part of their need standards. As a result, clients in these States may be erroneously denied aid because their income would exceed the reduced dollar limit.

Second, New York also incorrectly computes its 150-percent income limit by using a maximum regional rent allowance in its basic need standard, rather than the actual rent paid by a client, which in many cases is lower. State regulations require that the shelter component of the need standard will include

actual rent paid, up to the maximum regional allowance. Consequently, a higher than appropriate income limit is established against which the client's income is compared. We reviewed a sample of 727 earned income cases in three New York counties and adjusted the 150-percent income limit for the actual rent paid in each case. In 45 cases (or about 6 percent), the clients were receiving benefits totaling about $6,000 monthly to which they would not have otherwise been entitled.

On October 21, 1982, we briefed OFA Region II officials responsible for overseeing New York's AFDC program, and they agreed with the issues raised in New York. However, according to an Associate Commissioner of the New York State Department of Social Services, the State's welfare law must be changed to comply with Federal requirements. A bill has been introduced in the New York State legislature to make that change.

LUMP-SUM PAYMENT REGULATIONS ARE SILENT ON WHETHER INCOME TAX REFUNDS ARE INCOME

Federal regulations for implementing the lump-sum payment provision of the act do not specify the types of payments that are to be considered income. As a result, States can treat lump-sum income tax refunds either as a resource or as income when determining a family's need for assistance.

The act requires that all income, including lump-sum payments, be counted in the month received and be considered available to meet future months' needs. If the AFDC family's total earned income (less applicable disregards) and unearned income (including lump-sum payments) exceed a State's need standard for a family of that size, the family is ineligible for aid for the number of full months--including the month the income was received--computed by dividing the total adjusted income by that need standard. Any remaining income is counted as income in the first month following the period of ineligibility.

Of the four States visited, only New York treated income tax refunds differently from other lump-sum payments. According to New York State regulations, local welfare districts must determine whether the amount of the refund, plus the equity value

of all other nonexempt resources a family unit possesses, exceeds the $1,000 resource limit.[5] If the income tax refund plus other nonexempt resources do not exceed $1,000, the household may retain the refund and continue receiving assistance. If the income tax refund plus other nonexempt resources exceed $1,000, the family is given the option of (1) voluntarily transferring the excess to the local district to be applied against past assistance received and retaining program eligibility or (2) being declared ineligible for the applicable number of months computed by dividing the total adjusted income by the applicable basic need standard.

The New York regulation precludes the State from realizing the full saving potential of the act because families can continue to be eligible for AFDC payments rather than being terminated for a period of time.

We asked OFA's Region II officials whether they were aware of New York's method of treating income tax refunds and, if so, whether OFA approved it. OFA responded that the State is allowed to treat a tax refund either as income or as a resource. They added that, although this is not specifically addressed in Federal regulations, it is permitted by an OFA directive to its regional offices, OFA-ROD-79-71, dated March 14, 1979, which stated that:

> "States have the option of choosing whether income tax refunds will be considered as unearned income in the month received and a resource thereafter, or as a resource alone. This is consistent with current policy giving States this option for treatment of lump-sum payments which are in the nature of a 'windfall' * * *."

The treatment of income tax refunds as a resource or as income is being litigated in at least two States. When the litigation has been completed, HHS should issue regulations describing how income tax refunds are to be treated by the States or

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[5]To be eligible for AFDC benefits under Public Law 97-35, a family unit is limited to having nonexempt resources with a value of $1,000 or less. The only exempt resources are a home in which the family lives, one auto or other vehicle having an equity value of $1,500 or less, and household items (as defined by each State) necessary for daily living. The value of an auto in excess of $1,500 must be counted with other nonexempt resources.

seek appropriate clarifying legislation if the final court decisions are not consistent.

SEVERAL STATES ARE IMPROPERLY PROVIDING SPECIAL NEED ALLOWANCES FOR PREGNANCY

Before enactment of Public Law 97-35, States could, at their option, provide AFDC assistance to pregnant women from the time pregnancy was medically verified. States could also consider the needs of the unborn child when determining the grant amount and provide for any special pregnancy-related circumstances that might arise.

Now the act provides that federally shared grants to pregnant women can begin only with the third month before the month in which the birth is expected. In addition, Federal financial participation is not available to meet the needs of the unborn child--only those of the expectant mother.

Federal regulations also allow States to provide other aid to pregnant women through a special need allowance, recognizing special circumstances that may not be covered by the regular grant. As specified in the regulations, if a State agency includes such special need items in its need standard, it must describe those items and the circumstances under which they will be included and provide that they will be considered for all applicants and recipients requiring them.

Of the 33 States visited and contacted, nine[6] provide special need allowances related to pregnancy; five, however, do not adequately define the special need items or the circumstances under which they are provided. California, Colorado, New York, Ohio, and Wisconsin have not defined the circumstances that are covered by the special need allowances they provide pregnant women; instead, they provide the allowance to all pregnant women eligible for assistance, regardless of their individual circumstances. Michigan, Minnesota, and Utah specify in their AFDC plans that the allowance is provided to meet the additional dietary needs of the expectant mother. Massachusetts' plan specifies that $50 will be provided to cover the cost of a layette, and $75 for a crib and mattress.

Of the nine States that provide for special needs related to pregnancy, only Minnesota attempts to determine whether a

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[6]California, Colorado, Massachusetts, Michigan, Minnesota, New York, Ohio, Utah, and Wisconsin.

special need actually exists in each case. None of the States distinguish between the needs of women expecting their first child and those of women expecting their second or third child, even though these needs may change.

Other problems can also arise. For example, according to Federal regulations, if a State chooses to grant special need allowances, they must be available to all applicants and recipients requiring them. Yet, Minnesota has placed a ceiling on the amount that it will spend each year for all special need allowances, including those provided to pregnant women. It appears that this State would not be complying with Federal regulations if it had to deny aid to clients with legitimate special needs because it had reached the annual ceiling.

COMMENTS BY OFA OFFICIALS

On April 21, 1983, we discussed the contents of this report with the Acting Associate Commissioner of OFA and her staff. Regarding New York's incorrect computation of the 150-percent income test, they agreed that actual rent, where lower than the maximum regional rent allowance, should be used. They gave us a copy of their March 18, 1983, compliance letter to New York, advising the State to bring its practice into conformity with Federal requirements by including special need allowances in the test or be subject to having Federal funds withheld.

Concerning the classification of income tax refunds as either resources or income, they agreed to issue regulations when litigation is completed or to seek clarifying legislation if the final court decisions are not consistent.

Concerning the special need allowance for pregnant women, OFA officials agreed that States need to specify the circumstances under which such an allowance should be granted. They gave us a copy of a March 11, 1983, letter to the SSA regional commissioners, requesting the commissioners to notify the States that have not identified the special circumstances in their State plans to do so. They advised us that such circumstances would have to be identified for all applicants/recipients for the first as well as subsequent pregnancies.

RECOMMENDATIONS TO THE SECRETARY OF HHS

We recommend that you direct the Commissioner of Social Security to:

--Require Illinois, New Mexico, Pennsylvania, and Wisconsin to include special need allowances in computing the 150-percent income limit for determining AFDC eligibility and to advise applicants previously denied assistance that they may be eligible and can reapply.

--Monitor New York's compliance with Federal requirements to include special need allowances in its computing the 150-percent income limit to assure that compliance is achieved.

--Require New York to comply with its State regulations by using actual rent paid by a client in computing the 150-percent income limit when such rent is less than the maximum regional shelter allowance and removing from the rolls those with income that exceeds the reduced income limit.

--Determine whether other States--those not covered by our review--are applying the 150-percent income limit improperly and correct any problems found.

--Issue regulations after litigation has been completed on the issue of whether income tax refunds are to be considered as income for AFDC purposes, describing how income tax refunds are to be treated under the lump-sum payment provision by the States or seek appropriate clarifying legislation if final court decisions are not consistent.

--Advise States that failure to specify in their State plans the circumstances under which the special need allowances for pregnancy will be granted and to determine that a need actually exists in each case for the first and subsequent pregnancies will result in their State plans being out of compliance with Federal requirements and could result in the withholding of Federal financial participation.

--Advise Minnesota that since it has chosen to provide special need allowances, it is not in compliance with Federal requirements by placing a ceiling on the total amount it will spend each year for all special need allowances.

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As you know, 31 U.S.C. 720 requires the head of a Federal agency to submit a written statement on actions taken on our recommendations to the Senate Committee on Governmental Affairs and the House Committee on Government Operations not later than 60 days after the date of the report, and to the House and Senate Committees on Appropriations with the agency's first request for appropriations made more than 60 days after the date of the report.

We are sending copies of this report to the four Committees cited above as well as to the House Committee on Ways and Means; the Senate Committee on Finance; the House and Senate Committees on the Budget; the Director, Office of Management and Budget; and other interested parties.

Sincerely yours,

Richard L. Fogel
Director