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The Honorable Daniel Patrick Moynihan
United States Senate

The Honorable John D. Rockefeller IV
United States Senate

Subject: Welfare Reform: Monitoring Required State Spending Levels

The Personal Responsibility and Work Opportunity Reconciliation Act (PRWORA) of 1996 (P.L. 104-193) changed the way the federal government and states fund programs and services for needy families with children. The law replaced Aid to Families With Dependent Children (AFDC) and two related programs with the Temporary Assistance for Needy Families (TANF) block grant. Under prior law, AFDC was an entitlement for eligible families, and state welfare expenditures were matched with federal funds. PRWORA ended the entitlement to assistance and established TANF block grants, which give states a fixed amount of federal funds to provide time-limited assistance to needy families. To ensure that states would continue to maintain their own spending on needy families at a specified level, the law included a maintenance of effort (MOE) requirement that states must meet to receive their full TANF block grant.[1]

On November 20, 1997, the Department of Health and Human Services (HHS) issued proposed TANF regulations seeking public comment. As of November 1998, these regulations had not been finalized. The proposed regulations elaborate on statutory provisions regarding which state expenditures are countable for MOE purposes and specify the financial data states are required to

[1]States are required to maintain at least 75 percent of their historic welfare spending levels. States' MOE requirements are based on states' federal fiscal year 1994 spending on AFDC, Job Opportunities and Basic Skills (JOBS), and Emergency Assistance (EA) programs; related administrative costs; and AFDC-related child care programs such as the AFDC/JOBS child care, Transitional Child Care, and At-Risk Child Care programs.

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submit quarterly to HHS to facilitate departmental monitoring of MOE expenditures.

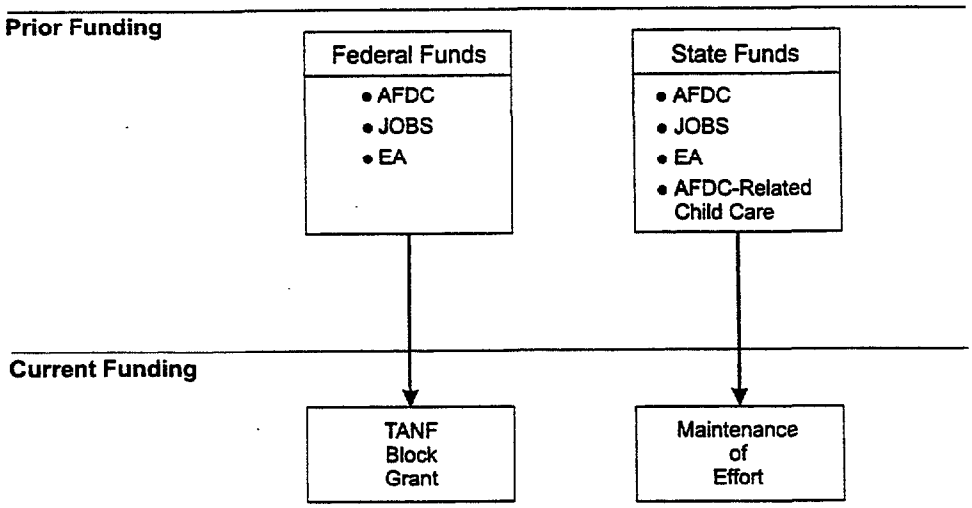
Because of your concern about two aspects of the proposed regulations, you asked that we determine whether (1) the proposed regulations' guidance on which expenditures count for MOE purposes is clear and consistent with the statute and (2) adequate mechanisms are in place for HHS to determine whether states are complying with the MOE requirement. To respond to the first objective, we analyzed relevant statutory and regulatory language and interviewed HHS officials, representatives of state organizations (the National Governors' Association and the National Conference of State Legislatures), a representative of public welfare officials (the American Public Human Services Association), and representatives of organizations that have voiced concerns about the proposed regulations related to MOE issues (the Center on Budget and Policy Priorities and the Center for Law and Social Policy). To respond to the second objective, we reviewed our previous work on auditing procedures for federal block grants and existing federal guidance on auditing the TANF program. We conducted our work in accordance with generally accepted government auditing standards between September and November 1998.

In summary, we found that the proposed regulations' guidance on which expenditures count for MOE purposes is unclear with regard to expenditures that are not related to prior AFDC programs. HHS officials acknowledged the problem and said that it would be addressed in the final regulations, which they expect to be issued by January 1999. In addition, the proposed regulations, as interpreted by HHS officials, appear to be inconsistent with the statute regarding how expenditures related to prior AFDC programs may be counted toward the requirement. To determine whether states are complying with the MOE requirement, officials at HHS told us that it plans to rely primarily on the audit mechanism established in the Single Audit Act to verify the accuracy of the information states report to HHS on their MOE expenditures. We believe this is the appropriate approach because the Single Audit Act established systematic procedures that may appropriately be used to test compliance with MOE provisions in federal programs, including TANF. However, clear guidance on MOE requirements is essential if this mechanism is to function effectively. HHS plans to clarify TANF MOE guidance in the final regulations.

BACKGROUND

PRWORA significantly altered the way programs and services for needy families are funded (see fig. 1).

Figure 1: Funding Mechanisms for Assistance to Low-Income Families With Children, Before and After Federal Welfare Reform



Note: Prior federal funding was also available for AFDC-related child care; federal funding targeted to child care for low-income families is now funded through the Child Care and Development Fund.

PRWORA's MOE requirement is an important part of the law, in that it helps limit the extent to which federal block grant dollars are used to replace state spending on needy families. Without such a requirement, states could replace their own spending in a program area with federal funds and either increase state funding for other programs or reduce taxes.[2]

PRWORA includes provisions that stipulate which state expenditures are countable towards the MOE requirement. For program expenditures to count toward the MOE requirement, the following three criteria apply.

– Expenditures must be for eligible families. These are families that are eligible for assistance under a state's TANF program, would be eligible for TANF assistance if they had not reached the time limit on assistance, or

[2]See Block Grants: Issues in Designing Accountability Provisions (GAO/AIMD-95-226, Sept. 1, 1995), pp. 17-18.

would be eligible for TANF assistance if they had the required immigrant status. In each case, the family must have either a child living with a custodial parent or other caretaker or include a pregnant individual.

- Expenditures must be for specified purposes. Qualifying expenditures include expenditures for cash assistance, child care assistance, work programs, educational activities designed to increase self-sufficiency, certain administrative activities, and other activities not specifically prohibited by the welfare law. Expenditures on these types of assistance may be made in the context of either TANF programs, funded at least in part by federal TANF block grants, or separate state programs, funded solely with non-TANF funds.[3]

- Expenditures must meet one of the following two conditions. Either a state would have to have been entitled to a federal matching payment for these expenditures under AFDC or a related program, or the expenditures would have to represent additional or new expenditures above fiscal year 1995 levels of spending in other state programs. This latter condition is sometimes referred to as the "new spending test." This requirement is designed to prevent states from replacing their spending on cash welfare and other aid historically associated with AFDC-related programs with their expenditures continued from previous years on other state programs that serve needy families with children, such as pregnancy prevention or state earned income tax credit programs.

PROPOSED REGULATIONS' GUIDANCE ON EXPENDITURES THAT COUNT TOWARD MOE

The proposed regulations are unclear regarding the new spending test in two respects. First, the regulations indicate that the new spending test applies to "separate state programs," but HHS officials acknowledged that this term had generated confusion because it was used in two different ways in the regulations.[4] Officials at HHS said that its position is that the new spending test

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[3]Some states are using separate state programs to serve families ineligible for federal TANF assistance. Separate state programs are not subject to TANF restrictions such as mandated minimum work participation rates or time limits for receiving aid.

[4]The proposed regulations use the term "separate state programs" in some places to refer to non-TANF programs–those serving eligible families that are funded with non-TANF funds only–and in other places to refer to programs that are not

applies to all state spending on programs and activities not associated with prior AFDC programs and activities, whether the state funds are now expended in a TANF program or a non-TANF program (that is, a separate state program). However, they acknowledged that the proposed regulations suggest in places that the new spending test applies only to state spending on non-TANF programs.

Second, the proposed regulations are unclear on how prior state spending levels are to be defined for the new spending test; without such a definition, it is not possible to measure the level of new spending countable toward the MOE requirement. HHS officials acknowledged that the proposed regulations do not specify whether the appropriate prior state spending level is total fiscal year 1995 state spending on a particular program or only fiscal year 1995 state spending for eligible families in that program. HHS officials stated that they view either position as a reasonable interpretation of the statute. We believe, however, that the latter position appears to be more consistent with the statute, which stipulates that current expenditures are countable for MOE purposes only if they are for "eligible families." Comparing current expenditures on eligible families with past total program expenditures will not provide an accurate measure of the level of new state spending on eligible families. We believe a valid measure of new spending should compare current spending on eligible families with past spending on eligible families.

In addition to these problems of unclear guidance, the proposed regulations permit expenditures related to prior AFDC programs to be counted toward the MOE requirement in a manner that appears to be inconsistent with the statute. Under PRWORA, current expenditures are countable toward MOE if the state "is entitled to a payment" under prior law with respect to these programs. The payment to which this refers is the federal match that was available under prior welfare law. Because of prior caps on federal payments in some programs, a state might not have been "entitled to a payment" for all its prior welfare expenditures.[5] However, under the proposed regulations, as explained by HHS officials, current expenditures for which a state would not have been entitled to

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related to prior AFDC programs.

[5]Unlimited federal funds were available for most federally matched welfare programs under prior law, but two programs, JOBS and At-Risk Child Care, were subject to caps.

a payment because of a cap would nevertheless be counted toward the MOE requirement.[6]

Representatives of state organizations told us that states have expressed a need for additional guidance about some of the activities allowable for MOE purposes. These representatives said that states had expressed confusion, for example, about the extent to which expenditures on child welfare and child support would be countable for MOE purposes. These representatives also said that states' incomplete understanding of what is allowed has constrained their ability to be more flexible in serving needy families. HHS officials said they were evaluating the need to provide additional guidance in this area.

HHS officials acknowledged the need to provide clearer guidance on the MOE requirement and said that the process of obtaining public comment on the proposed regulations is a key vehicle for accomplishing this objective. These officials said that HHS had received many comments from various groups on the MOE sections of the proposed regulations and that it was taking these comments into consideration in preparing the final regulations. Further, HHS plans to address the identified problems pertaining to unclear guidance on the new spending test in finalizing the regulations, which HHS expects to issue by January 1999.

USING THE SINGLE AUDIT ACT TO ASSESS STATE COMPLIANCE

The proposed regulations would impose on the states various TANF financial reporting requirements pertaining to MOE expenditures. For example, states would be required to report data to HHS on the amounts of MOE expenditures for specific categories, such as cash assistance, work subsidies, and child care, as well as various descriptive and historical financial data on separate state programs. Officials at HHS told us that it would use states' TANF financial reports to determine if each state had met its MOE requirement. Officials at HHS also told us that it would rely primarily on the audit mechanism established under the Single Audit Act to verify the accuracy of the information on the TANF financial reports.

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[6]This raises the question, not addressed in the proposed regulations, of how to treat these state expenditures if they cannot be counted toward the MOE requirement because of caps on federal matching funds. Although the law is not clear on this point, we believe that these amounts would be subject to the new spending test discussed above.

The Single Audit Act provides uniform audit requirements for all federal assistance programs, including TANF, that award funds to states, local governments, or nonprofit organizations. Rather than being a detailed review of individual grants or programs, a single audit is an organizationwide financial and compliance audit that focuses on accounting and administrative controls. A single audit is designed to advise federal oversight officials and program managers on whether an organization's financial statements are fairly presented and to provide reasonable assurance that federal financial assistance programs are managed in accordance with applicable laws and regulations. Each state's TANF program generally would be audited annually because of the high level of program expenditures unless auditors determined a state's TANF program to be at low risk of material noncompliance in a particular year.

Auditors conduct single audits using the Office of Management and Budget's OMB Circular A-133 Compliance Supplement, which provides general guidance on testing MOE provisions in federal programs and more specific information on the TANF program. The Compliance Supplement includes audit objectives and suggested audit procedures for 14 types of compliance requirements, including MOE requirements. In addition, it provides specific information for auditors on the MOE requirement in the TANF program. However, the current Compliance Supplement does not include any information on the new spending test provision of the TANF MOE requirement. Clear guidance on the TANF MOE requirement–both in the regulations and in the Compliance Supplement–is essential to ensure that states understand and carry out the MOE provisions as intended by PRWORA and that auditors can effectively assess compliance with this requirement. HHS officials told us that they plan to update the TANF guidance in the Compliance Supplement to incorporate additional MOE guidance when the regulations are finalized.

While single audits are an important tool to help federal program managers fulfill their oversight responsibilities, the audits are not intended to answer all questions about states' administration of federal programs. If a single audit indicates problems with a state's compliance with the MOE requirement, or if the auditor is unable to adequately assess compliance, HHS will need to take appropriate follow-up action.

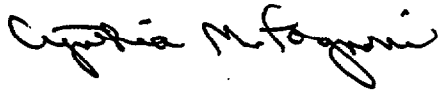
We support the single audit concept for auditing federal assistance programs and believe it is the fundamental mechanism for testing compliance with MOE provisions in TANF. Over time, single audits should provide HHS with a good indication of which states are materially complying with the MOE requirements, information concerning weaknesses found in states' internal controls for

ensuring compliance with the requirements, and information about which states HHS needs to focus its oversight activities on.

AGENCY COMMENTS

We provided a draft of this correspondence to officials at HHS, but they were unable to comment within the time allowed.

We will make copies of this correspondence available to those who are interested upon request. If you or your staff have any questions, please call me or Mark V. Nadel, Associate Director, on (202) 512-7215. Other staff who contributed to this correspondence include Katrina Ryan, Andrew Sherrill, Gale C. Harris, Robert G. Crystal, Sylvia L. Shanks, and George A. Rippey.



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