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Follow the Money: Tackling Improper Payments

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My name is Rachel Greszler. I am a Senior Research Fellow in Economics, Budgets, and Entitlements at The Heritage Foundation. The views I express in this testimony are my own and should not be construed as representing any official position of The Heritage Foundation.

Elevated and growing global cybersecurity threats alongside expanding government programs have heightened the need for greater integrity within government programs. In addition to hundreds of billions of taxpayers' dollars that have been improperly distributed, the protection of Americans' privacy, personal identities, and our national security require significant improvements in the integrity of federal programs and payments.

Ensuring the accuracy and expediency of federal payments is not an easy task as the two goals often run counter to one another. This is one reason why federal tax and transfer programs are inherently less efficient than individuals keeping more of their own earnings and being able to spend them without jumping through necessary but bureaucratic hoops.

Like a seesaw, there are trade-offs between improper payments and the ease with which individuals can access government benefits. At a base level, some trade-offs will always exist, but the problem today is that we are not dealing with a normal seesaw balancing on a two-foot base, but rather one with $3.9 trillion in federal transfer payments underneath.[1]

[1]Congressional Budget Office, "CBO's Projections of Federal Receipts and Expenditures in the National Income and Product Accounts: 2022 to 2031," November 2021, https://www.cbo.gov/system/files/2021-11/57432-NIPA.pdf#page=2 (accessed March 28, 2022).

Improving the integrity of federal programs and payments requires limiting the size and scope of government programs so that there is less bureaucracy for Americans to have to navigate and fewer opportunities for criminals to steal Americans' identities and tax dollars. Commonsense security measures must be implemented and enforced to protect the integrity of government programs.

In my testimony today, I would like to briefly review the magnitude of improper payments across the federal government and within a few particular programs, including recommended reforms; discuss widespread fraud and abuse in the pandemic unemployment insurance (UI) programs; and propose solutions that could reduce both the rates and overall level of improper payments across the federal government.

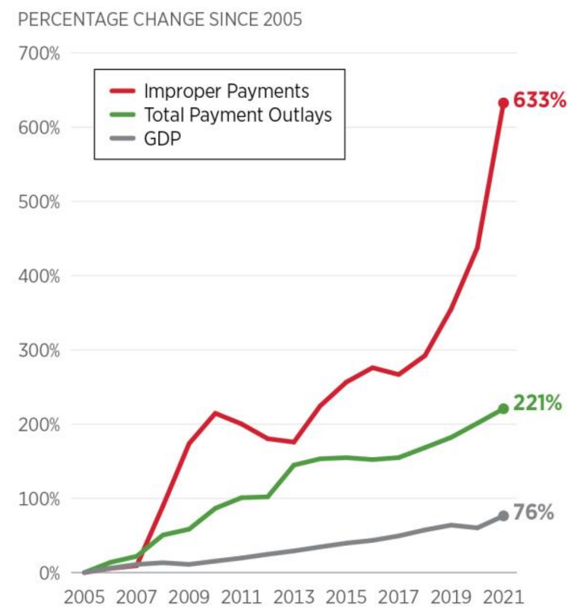
Already Enormous Improper Payments Surged in 2021

According to the Office of Management and Budget's 2021 reporting, improper payments totaled $281 billion in 2021, with an improper payment rate of 7.2 percent.[2] This is an increase from $175 billion and a rate of 5.1 percent in 2019. At $281 billion in 2021, improper payments were the federal government's 5th largest expenditure.

In general, improper payment amounts and rates have been trending upwards over the past 15 years, from lows around $41 billion and 2.9 percent in 2006 and 2007 to amounts exceeding $100 billion every year since 2020 and rates exceeding 4.0 percent in every year except 2013.

What has happened is that outsized growth in government has led to exponential growth in improper payments. Between 2005 and 2019, prior to the pandemic, gross domestic product (GDP) increased by 65 percent as total program payments rose 182 percent, and improper payments surged 355 percent. Extending that comparison from 2005 to 2021, GDP increased 76 percent, total program payments rose by 221 percent, and improper payments increased 633 percent.

Improper Payments Skyrocket



SOURCES: PaymentAccuracy.gov, "Annual Improper Payments Database," 2021 and 2015 datasets, https://www.paymentaccuracy.gov/payment-accuracy-the-numbers/ (accessed March 25, 2022), and Bureau of Economic Analysis, "Gross Domestic Product," National Income and Product Accounts, https://apps.bea.gov/iTable/index_nipa.cfm (accessed March 28, 2022).

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While not all improper payments are 100 percent wrong payments, it is also highly possible that a portion of fraudulent payments go undetected and are not captured in the improper payment total.

Some Simple Solutions to Address Rising Improper Payments

The online migration of government services has opened the door to widespread fraud and

[2] PaymentAccuracy.gov, "Annual Improper Payments Database," 2021 and 2015 Datasets, https://www.paymentaccuracy.gov/payment-accuracy-the-numbers/ (accessed March 25, 2022).

improper payments. No longer necessary to physically walk into the Social Security Administration or Unemployment Insurance Office—government ID and supporting documentation in hand—it has become far easier for individuals to file for and receive benefits that they are not eligible for, and the online format makes it possible for criminals to steal people's identities and illegally claim government payments in their names. And yet, digital records, online filing, and direct transfer payments are extremely efficient for legitimate transfer payments.

Even as criminals become increasingly sophisticated, information security systems, identity verification, and methods of eligibility determination are also continually evolving.

Although no perfect standard nor system exists, the National Institutes for Science and Technology (NIST) has developed a set of digital identity guidelines (NIST 800-63) that provide excellent tools for public- and private-sector organizations. Compliance with these standards results in significant reductions in fraud and improper payments. For example, states that implemented NIST-compliant eligibility checks during the surge in pandemic unemployment insurance programs saw their fraudulent claims payouts plummet immediately, and reported hundreds of billions of dollars in reported fraud prevention.[3]

While solid standards exist and the Office of Management and Budget (OMB) issued a memorandum (OMB 19-17) that requires federal agencies to implement the NIST Special Publication (SP) 800-63-3 and any successive versions, most agencies simply are not doing this.

Even login.gov, which is among the current Administration's primary tools—and one of its proposed solutions for cybersecurity—is not compliant with the NIST standards. Current OMB Deputy Director for Management Jason Miller testified during a March 17, 2022, Senate hearing that login.gov is not where it needs to be, noting that it "needs to be strengthened going forward," including "stronger tools in place on identity verification."[4] And login.gov is not a viable option for the IRS, in part because of its limited capacity and lack of standards.

Simple solutions to reduce improper payments government-wide include:

- **Enforce compliance with federal standards**, including OMB memorandum 19-17, "Enabling Mission Delivery through Improved Identity, Credential, and Access Management."
- **Set and enforce improper payment standards**, such as limits on rates of improper payments, for each program with penalties for failure to achieve standards.
- **Optimize use of the government's Do Not Pay database**

[3]See, for example: Chorus Nylander, "N4T Investigators: State Says Security Measures Protected $75 Billion from Unemployment Fraud," News 4 Tucson KVOA, October 1, 2021, https://www.kvoa.com/news/n4t-investigators-state-says-security-measures-protected-75-billion-from-unemployment-fraud/article_89c57b5e-2307-11ec-921e-87637fd20932.html (accessed March 27, 2022), and Adam Bee, "California's Unemployment Fraud Reaches At Least $20 Billion," *The Los Angeles Times*, October 25, 2021, https://www.latimes.com/california/story/2021-10-25/californias-unemployment-fraud-20-billion (accessed March 27, 2022).

[4]Hearing, *Pandemic Response and Accountability: Reducing Fraud and Expanding Access to COVID-19 Relief through Effective Oversight*, Committee on Homeland Security and Government Affairs, U.S. Senate, March 17, 2022, https://www.hsgac.senate.gov/hearings/pandemic-response-and-accountability-reducing-fraud-and-expanding-access-to-covid-19-relief-through-effective-oversight (accessed March 27, 2022).

(donotpay.treasury.gov), including clarifying which agencies must use the Do Not Pay database, and considering ways to effectively share Social Security's master death file within the system.[5]
- **Do not federalize cybersecurity systems.** The private sector and public sector should be learning from one another and maintaining a competitive market for security services is crucial to protecting taxpayers' identities, their hard-earned tax dollars, and our national security.

While these solutions apply broadly across government programs, individual programs have different eligibility standards that necessitate unique solutions.

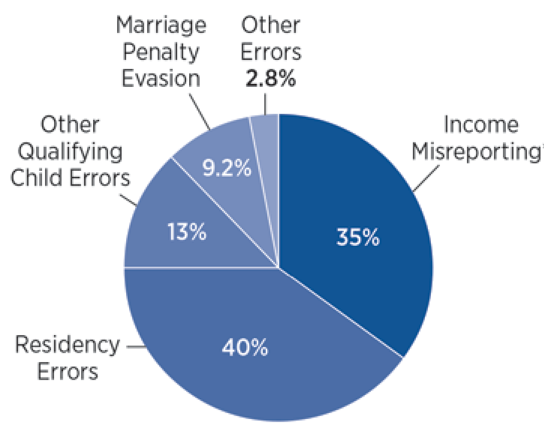
Earned Income Tax Credit and Additional Child Tax Credits

In 2021, improper payments in the Earned Income Tax Credit (EITC) program totaled \$19.0 billion, with a 27.8 percent improper payment rate. This is not an anomaly to the pandemic. Over the past decade, improper payments have averaged \$16.4 billion and 24.7 percent. Virtually all of these improper payments have been overpayments, primarily to people who were ineligible for the credit. An IRS audit publication from 2014 "found that between 79% and 85% of EITC dollars claimed incorrectly were claimed by tax filers ineligible for the credit."[6]

An analysis by my Heritage Foundation colleagues Robert Rector and Jamie Hall reported that between 43 percent and 50 percent of all EITC filings include overpayment claims, primarily due to income misreporting and qualifying child/residency errors.[7]

CHART 3

EITC Overclaim Dollars by Source of Error



* Excludes overlapping multiple errors.
SOURCE: Internal Revenue Service, "Taxpayer Compliance and Sources of Error for the Earned Income Tax Credit Claimed on 2006–2008 Returns," August 2014, https://www.irs.gov/pub/irs-soi/EITCComplianceStudyTY2006-2008.pdf (accessed August 1, 2016).

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[5]See U.S. Government Accountability Office, "Improper Payments, Strategy and Additional Actions Needed to Help Ensure Agencies Use the Do Not Pay Working System as Intended," GAO-17-15, October 2016, https://www.gao.gov/assets/690/680631.pdf (accessed March 27, 2022), and U.S. Government Accountability Office, "General Government: Use of the Do No Pay Working System (2017-11)," last updated March 31, 2020, https://www.gao.gov/action-tracker/general-government-use-do-not-pay-working-system-2017-11 (accessed March 27, 2022).
[6]U.S. Department of the Treasury, Internal Revenue Service, "Compliance Estimates for the Earned Income Tax Credit Claimed on 2006–2008 Returns," Publication 5162, August 2014, https://www.irs.gov/pub/irs-soi/EITCComplianceStudyTY2006-2008.pdf (accessed March 26, 2022).
[7]Robert Rector and Jamie Bryan Hall, "Reforming the Earned Income Tax Credit and Additional Child Tax Credit to End Waste, Fraud, and Abuse and Strengthen Marriage," Heritage Foundation *Backgrounder* No. 3162, November 16, 2016, https://www.heritage.org/sites/default/files/2018-04/BG3162.pdf.

The Additional Child Tax Credit (ACTC), which is the refundable portion of the tax credit, also has high improper payments and rates. In 2021, improper payments for the ACTC totaled $5.2 billion, with a 13.3 percent improper payment rate. Since the ACTC represents only about 40 percent of total Child Tax Credit Payments and ACTC improper payments almost certainly include improper payments within the non-refundable portion of the CTC, total improper payments in the CTC are most certainly higher than $5.2 billion.[8] If the 13.3 percent ACTC improper payment rate were applied across the entire $117.6 billion in CTC and ACTC payments, improper payments would equal $15.6 billion. (The $117.6 billion represents the Joint Committee on Taxation's 2020 estimate for fiscal year 2020 child credits and does not include any additional pandemic-related credits or payments.)[9]

Policymakers in charge of these programs should require, prior to payments, programs:

- **Verify the identity of individuals** who claim the EITC and ACTC,
- **Confirm that the children** for whom they claim these credits actually exist, and
- **Verify that the same child** is not claimed on more than one tax return.

Rector and Hall provide additionally recommended reforms in the EITC and ACTC, which they estimate could save taxpayers $19 billion annually. Some of those directives are:[10]

- **Require the IRS to fully verify income** and not issue any refundable EITC or ACTC payment until all income information is received and checked,
- **Require enhanced income verification requirements** for individuals claiming self-employment or small business income,
- **Require the IRS to deny claims** that do not include the required information, and only pay claims if the individual responds to the denial by providing the required information,
- **Impose financial penalties** for substantial income misreporting, and
- **Only allow individuals with legal custody** of children to claim the EITC and ACTC on their behalf.

Medicare, Medicaid, and CHIP

In 2021, total Medicare improper payments equaled $49.6 billion with an improper payment rate of 7.0 percent. While Medicare improper payment rates have generally been declining in recent years, Medicare Advantage's improper payments surged by $6.9 billion in 2021, as the improper payment rate jumped from 6.8 percent to 10.3 percent.

Both Medicaid and the Children's Health Insurance Program (CHIP) have experienced disturbing jumps in improper payments over the past three years. Between 2012 and 2018, Medicaid averaged $27.1 billion per year in improper payments, with a rate of 8.5 percent. In 2021, Medicaid's improper payments totaled $98.7 billion, with an improper payment rate of 21.7 percent, meaning more than one-in-five Medicaid dollars was an improper payment.

[8]The Joint Committee on Taxation, "Estimates of Federal Tax Expenditures for Fiscal Years 2019–2023," December 18, 2019, https://www.jct.gov/publications.html?func=startdown&id=5238 (accessed March 26, 2022).
[9]Joint Committee on Taxation, "Estimates of Federal Tax Expenditures for Fiscal Years 2020–2024," JCS-23-20, November 5, 2020, https://www.jct.gov/publications/2020/jcx-23-20/ (accessed March 26, 2022).
[10]Rectory and Hall, "Reforming the Earned Income Tax Credit and Additional Child Tax Credit to End Waste, Fraud, and Abuse and Strengthen Marriage."

Even more disturbing is the jump in improper CHIP payments, which went from an average of $851 million and a 7.7 percent rate between 2012 and 2018 to $5.4 billion and 31.8 percent in 2021. Nearly one-of-three CHIP dollars in 2021 were improper payments.

Many improper federal health care program payments stem from an unnecessarily complex and confusing payment process, which results in significant clerical errors. Unnecessary regulations, particularly related to documentation, administrative work, and non-market-based payments, also create an incentive for providers to improperly bill.

An April 2018 *Health Affairs* research article provides a comprehensive review of the complexity of these programs and their costs. In explaining the costly and burdensome billing and payment process, the authors note that hospitals typically have more billing specialists than hospital beds, and physician offices spend $30 billion a year on billing costs.[11]

While there are many reforms necessary to protect the integrity and efficiency of federal health insurance programs one broad directive and one specific reform are to:

- **Streamline or eliminate regulations** that add to complexity and drive up improper payments.
- **Incorporate Direct Primary Care (DPC) providers as an option within federal health insurance programs.** DPCs are innovative practice arrangements in which doctors contract directly with individuals for an annual or monthly fee. By eliminating bureaucracy and regulations that drive up costs, DPCs can often provide better care at a lower cost.

Unemployment Insurance: How Federal Pandemic Programs Resulted in Highest Rates of Fraud in History

The CARES Act, passed by Congress in March 2020, included a dramatic expansion of states' unemployment insurance programs, with the federal government setting benefit levels and eligibility criteria and covering the costs of the program expansions. These expansions simultaneously increased the incentive for fraud with higher benefits, slashed states' capacity to detect and prevent fraud, and reduced states' incentives for proper oversight.

Larger Benefits, Longer Durations. Congress provided an unprecedented $600 weekly supplement to state unemployment insurance benefits from March 2020 through July 2020, and an additional $300 weekly supplement from December 2020 through September 2021, although about half of the states ended the additional $300 benefits during the summer of 2021. Congress also increased the length of benefit availability by a factor of three, from the usual 26 weeks to 79 weeks. Combined, this led to a roughly eight-fold increase in the potential payout from a single unemployment insurance claim, from $10,400 to $79,000.[12]

Expanded Coverage, Added Eligibility Criteria, and Reduced Verification. For starters, Congress created a new program—the Pandemic Unemployment Assistance program—to provide benefits to workers who did not pay into the unemployment insurance systems. This included individuals such as the self-employed, freelancers, and

[11] Joshua D. Gottlieb, Adam Hale Shapiro, and Abe Dunn, "The Complexity of Billing and Paying for Physician Care," *Health Affairs*, Vol. 37, No. 4, April 2018, https://www.healthaffairs.org/doi/10.1377/hlthaff.2017.1325 (accessed March 26, 2022).

[12] Peter Ganong, Pascal J. Noel, and Joseph S. Vavra, "US Unemployment Insurance Replacement Rates During the Pandemic," National Bureau of Economic Research *Working Paper* No. 27216, May 2020, https://www.nber.org/system/files/working_papers/w27216/w27216.pdf (accessed August 1, 2021).

gig workers, as well as others who may not have lost a job or income as a result of the pandemic.

As Inspector General Larry D. Turner of the U.S. Department of Labor testified on March 17, 2022,

> The expanded coverage offered under the PUA [Pandemic Unemployment Assistance] program posed significant challenges to states as they implemented processes to determine initial and continued program eligibility for participants. The reliance solely on claimant self-certifications without evidence of eligibility and wages during the program's first 9 months rendered the PUA program extremely susceptible to improper payments and fraud.[13]

In addition to adding coverage for new groups of workers, Congress added broad-reaching new eligibility criteria—such as being "impacted" by school or daycare closures, quitting one's job for reasons related to COVID-19, losing partial income, or the very broad qualification of having one's employment be "affected" by COVID-19—that were difficult if not impossible to verify.

Widespread Fraud and Identity Theft. By putting an unprecedentedly high dollar value on unemployment insurance benefits, making them available for three times as long as usual, widening eligibility, and reducing verification requirements, these expansions opened the floodgates to individual fraud and abuse as well as large-scale criminal enterprises stealing Americans' identities and taxpayers' money. These unfettered expansions even caused national security risks, including the Chinese military breaking into some states' unemployment insurance systems.[14]

Unemployment insurance fraud has been so high that the Office of Inspector General (OIG) is investigating or reviewing more than 143,000 complaints of fraud—a more than 1,000 times increase in the volume of UI work—and UI fraud investigations account for 94 percent of the Inspector General's cases, compared to 11 percent prior to the pandemic.[15]

The Federal Trade Commission (FTC) reported a 27-fold increase in identity theft claims related to government benefit programs during the pandemic. Between the one-year period leading up to March 2020 and the one-year period afterwards, 23,471 identity theft reports from individuals who said their personal information had been used to obtain a government document or claim a government benefit spiked from 23,471 to 636,520.[16]

[13]Larry D. Turner, "Pandemic Response and Accountability: Reducing Fraud and Expanding Access to COVID-19 Relief through Effective Oversight," testimony before the Committee on Homeland Security and Governmental Affairs, U.S. Senate, March 17, 2022, https://www.hsgac.senate.gov/imo/media/doc/Testimony-Turner-2022-03-17-REVISED.pdf (accessed March 26, 2022).

[14]Sean Lyngaas, "Cybersecurity Firm Says Chinese Hackers Breached Six US State Agencies," CNN, March 8, 2022, https://www.cnn.com/2022/03/08/politics/china-hacking-state-governments-mandiant/index.html (accessed March 28, 2022).

[15]Turner, "Pandemic Response and Accountability: Reducing Fraud and Expanding Access to COVID-19 Relief through Effective Oversight."

[16]See Tableau Public, "Identity Theft Reports by the Federal Trade Commission," Federal Trade Commission *Consumer Sentinel Network Report*, https://public.tableau.com/app/profile/federal.trade.commission/viz/IdentityTheftReports/TheftTypesOverTime (accessed August 2, 2021), and Federal Trade Commission, "Protecting Consumers During the COVID-19 Pandemic: A Year in Review," April 16, 2021, https://www.ftc.gov/system/files/documents/reports/protecting-consumers-during-covid-19-pandemic-year-

While the pandemic unemployment insurance expansions created the perfect storm, states' unemployment insurance systems were in desperate need of modernization and improved oversight long before the pandemic. According to the OIG,

> The unprecedented infusion of federal funds into the UI program gave individuals and organized criminal groups a high-value target to exploit. That, combined with easily attainable stolen personally identifiable information and continuing UI program weaknesses identified by the OIG over the last several years, allowed criminals to defraud the system.[17]

Despite widespread knowledge of flawed government systems and ample oversight recommendations, both state and federal government agencies have often failed to implement the reforms needed to protect the integrity of their programs.

For example, the *Los Angeles Times* reported that although the California state auditor recommended in March 2019 that the Employment Development Department (EDD) stop including Social Security numbers in its mailed documents, the EDD continued to send out 38 million pieces of mail containing Social Security numbers after the onset of the pandemic.[18] Of the California EDD's estimated 10 percent to 27 percent of fraudulent benefits paid out,[19] 35,000 checks[20] totaling $810 million in payments were issued to names of California prison inmates.[21] This demonstrates the problem when those administering a program have little stake in its integrity. With the federal government footing the bill, states had less incentive to prevent inaccurate payments. But it also demonstrates fundamental flaws in programs even prior to the pandemic, such as the need for checks against do-not-pay databases, and the provision of basic privacy protections in the distribution of program information.

We Do Not Even Have an Accurate Count of Improper UI Payments

According to the Department of Labor OIG, the Department's Employment and Training Administration estimated an 18.7 percent improper payment rate within the Pandemic Emergency Unemployment Compensation (PEUC) and Federal Pandemic Unemployment Compensation (FPUC) programs, and it has not yet provided an estimated improper payment rate for the largest, and arguably most susceptible-to-fraud PUA program.[22] An 18.7 percent improper payment rate across the estimated $872.5 billion in pandemic unemployment insurance benefits would mean a minimum of $163 billion in improper payments.

Yet, as the OIG notes, the estimated 18.7 percent improper payment rate is based on the experience of the regular UI programs (not the actual pandemic ones). The OIG notes,

review/covid_staff_report_final_419_0.pdf (accessed July 6, 2021).

[17]U.S. Department of Labor, Office of Inspector General, "DOL–OIG Oversight of the Unemployment Insurance Program."

[18]Patrick McGreevy, "Despite Reports of Unemployment Fraud, California Keeps Sending Mail with Social Security Info," *Los Angeles Times*, November 19, 2020, https://www.latimes.com/california/story/2020-11-19/california-edd-unemployment-social-security-numbers-fraud-forms (accessed June 29, 2021).

[19]State of California Employment Development Department, "California Unemployment: Fraud by the Numbers," January 16, 2021, https://www.edd.ca.gov/Unemployment/pdf/fraud-info-sheet.pdf (accessed July 6, 2021).

[20]Jack Kelly, "The Most Brazen $400 Billion Unemployment Funds Heist in History," *Forbes*, June 12, 2020, https://www.forbes.com/sites/jackkelly/2021/06/12/the-most-brazen-400-billion-unemployment-funds-heist-in-history/?sh=b3bbd302020e (accessed July 6, 2021).

[21]Bee, "California's Unemployment Fraud Reaches At Least $20 Billion."

[22]Turner, "Pandemic Response and Accountability: Reducing Fraud and Expanding Access to COVID-19 Relief through Effective Oversight."

"Based on the OIG's audit and investigative work, the improper payment rate for pandemic UI programs is likely higher than 18.71 percent."

Some researchers have estimated improper payment rates approaching 50 percent within the pandemic unemployment insurance programs. For example, Blake Hall, CEO of the authentication company ID.me, said, "The fraud rates that we're seeing are over 10 times what we usually see at federal agencies."[23] Hall, whose company works with about two dozen states to detect fraudulent benefit claims, estimates that unemployment fraud has potentially cost taxpayers $400 billion.

My Estimate: $357 Billion in Unemployment Insurance Payments Sent to People Who Were Not Unemployed

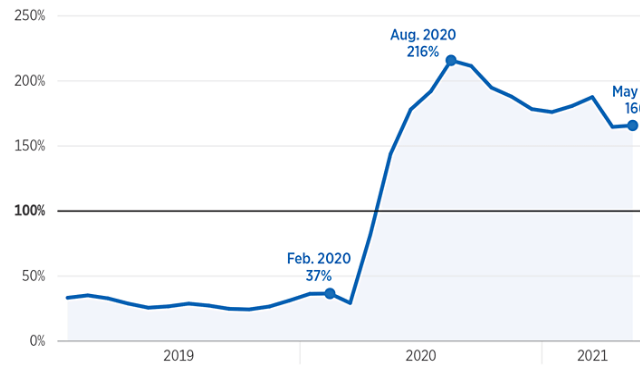
From the onset of the pandemic, I followed weekly Unemployment Insurance (UI) claims payments and monthly unemployment reports and noticed that UI payments were regularly far greater than the number of unemployed people. This led me to conduct an analysis aimed at providing a lower-bound estimate of the number of UI payments that were going to people who were not actually unemployed.

Typically, only about 35 percent to 40 percent of unemployed workers receive unemployment insurance benefits.[24] Between April 2020 and May 2021, the number of people receiving unemployment benefits averaged 176 percent of the number of unemployed people, clearly indicating a massive amount of improper payments.[25]

CHART 1

Unemployment Benefits Exceed Unemployed Workers

Historically, about four out of every 10 unemployed workers received unemployment benefits. Since Congress expanded benefits during the COVID-19 pandemic, about 18 workers have received benefits for every 10 unemployed workers.



SOURCE: News release, "Unemployment Insurance Weekly Claims," U.S. Department of Labor, July 1, 2021, https://www.dol.gov/ui/data.pdf (accessed July 7, 2021).

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A very conservative estimate of the number of fraudulent or improper payments comes from assuming that 100 percent of all unemployed people filed for and received unemployment insurance benefits and comparing that figure with the total amount of benefits that were paid out.[26]

Providing unemployment benefits to 100 percent of all unemployed workers would have resulted in 807 million benefit checks, compared to the 1.365 billion checks that went out the door. That means at least 557 million benefit checks went to people who

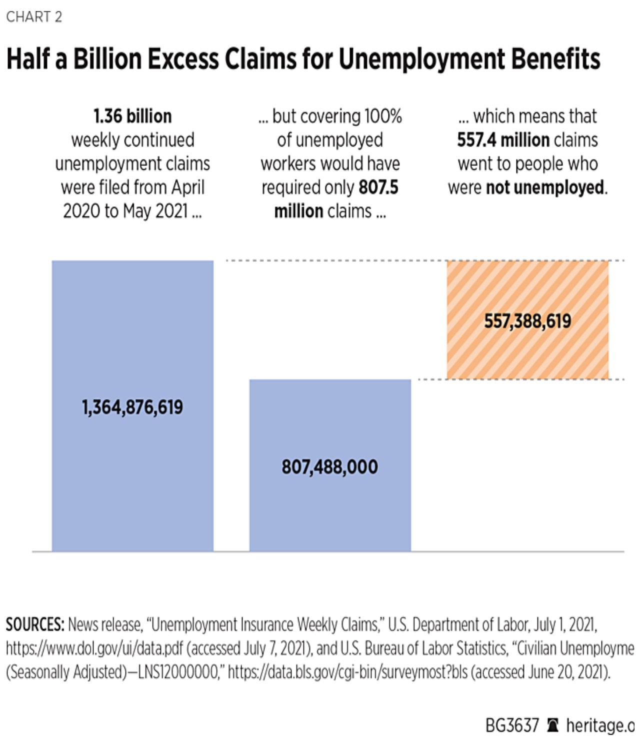
[23]Consumer Bob and Nicholas Kjeldgaard, "Unemployment Benefits Fraud Could Cost $300 Billion Nationwide," NBC San Diego, March 24, 2021, https://www.nbcsandiego.com/news/local/unemployment-benefits-fraud-could-cost-300-billion-nationwide/2558796/ (accessed July 6, 2021).

[24]There are various reasons why not all unemployed workers collect unemployment benefits, including not participating in the UI system due to self-employment, not having worked long enough to qualify for benefits, or choosing not to file for benefits due to short spells of unemployment.

[25]U.S. Department of Labor, Employment and Training Administration, Office of Unemployment Insurance, "UI Weekly Claims," data archive, https://oui.doleta.gov/unemploy/claims_arch.asp (accessed June 30, 2021).

[26]Many people who were unemployed did not file for or receive UI benefits for a variety of reasons, which makes this a conservative estimate.

were not actually unemployed.[27] Translating that across total program costs of $873 billion[28] implies that at least $357 billion in payments went to people who were not actually unemployed.



Even with outdated systems, states failed to perform some very basic checks. Some states had weeks in which a majority of UI claims were made by people with out-of-state IDs, who presumably did not live in the state and thus should have been automatically ineligible. Arizona reported that in the summer of 2020 it was receiving more UI claims than its entire workforce, but after partnering with a certified identity verification provider (ID.me), its claims fell by 99 percent.[29]

UI programs are state-run and thus policies to strengthen them should be state-driven, but considering that the massive pandemic UI fraud was born by federal taxpayers, both federal and state lawmakers should act to reduce improper payments:

- **Federal policymakers: Do not impose UI eligibility rules on states.** By compelling policies on states that they could not securely and effectively carry out, the federal government made it extremely difficult to protect the integrity of taxpayers' dollars.
- **Federal policymakers: Make federal funds for state UI programs conditional on meeting security compliance** (such as meeting NIST standards), as such standards drastically reduce fraud.
- **State policymakers: Modernize UI programs.**
- **State policymakers: Ensure ID verification** through programs that meet state-adopted security standards.
- **State policymakers: Ensure eligibility** through improved sharing of state-based data.
- **State and federal policymakers: Restrict UI programs to UI-participating** individuals and businesses as this provides verification of eligibility and accountability of finances.

[27]For a full explanation of the analysis, see Rachel Greszler, "A Warning Against Embedding Problematic Pandemic Unemployment Benefits," Heritage Foundation *Backgrounder* No. 3637, July 13, 2021, https://www.heritage.org/sites/default/files/2021-07/BG3637.pdf.

[28]U.S. Department of Labor, Office of Inspector General, "DOL–OIG Oversight of the Unemployment Insurance Program," June 10, 2021, https://www.oig.dol.gov/doloiguioversightwork.htm (accessed June 29, 2021).

[29]Nylander, "N4T Investigators: State Says Security Measures Protected $75 Billion from Unemployment Fraud."

Limited Government Can Minimize Improper Payments, Maximize Personal Autonomy

Both prior to and since the pandemic, the size and scope of government has expanded, and large legislative packages have been proposed that would include socialist programs that require individuals to submit to the federal government in order to access everyday goods and services. All of those programs would come with huge potential for improper payments, and also with eligibility criteria and verification processes that would slow down individuals' ability to obtain the things they need when they need them. Below are just a few examples of how the process of utilizing a government program to obtain something individuals could otherwise get on their own can increase improper payments and limit individuals' incomes and autonomy:

Unemployment Insurance Amounts to Forced "Savings" with Limited Access. Although employers pay the taxes that fund UI programs, workers ultimately bear the cost of those taxes through lower wages and benefits. Thus, UI programs are effectively a means of forced savings, but with rigid rules and a bureaucratic process required to access the savings. Moreover, benefits are determined by bureaucrats without regard to individuals' needs. While one worker may need to replace 100 percent of her earnings for four weeks, another 60 percent of his earnings for 12 weeks, and another could get by with 50 percent wage replacement for eight weeks, UI programs pay a standard benefit for a standard number of weeks, regardless of unique circumstances. This structure incentivizes longer periods of unemployment and often fails to meet workers' basic income needs.[30] Individuals and families would be better off receiving their share of UI taxes and putting it into a Universal Savings Account to access based on their unique needs.

Tax Credits Are Inherently Complex and Inefficient and Drive up Marginal Rates. Tax credits require the federal government to levy higher tax rates now or in the future to make up for the revenue lost from the credits. Higher tax rates discourage work and savings—which leads to lower incomes and a smaller economy. Further deadweight loss comes from the inefficiency of those credits. Furthermore, so-called "refundable tax credits" involve the IRS sending cash benefits to individuals and should be more correctly considered spending programs. A May 2021 report from the Treasury Department's Inspector General for Tax Administration suggests that improper payment rates are inherent to the nature of government programs:

> Although error rates for each of these credits remain high, the IRS attributes these refundable tax credit overclaims to their statutory design and the complexity taxpayers face when self-certifying eligibility for the refundable tax credits and not to internal control weaknesses, financial management deficiencies, or reporting failures.[31]

The Child Tax Credit is one such example of an inefficient credit—and one which some policymakers seek to significantly expand. The Additional Child Tax Credit has a 12 percent improper payment rate,[32] and proposals to

[30] Congressional Budget Office, "Economic Effects of Additional Unemployment Benefits of $600 per Week," Letter to the Honorable Charles Grassley, June 4, 2020, https://www.cbo.gov/system/files/2020-06/56387-CBO-Grassley-Letter.pdf (accessed August 1, 2021).

[31] Treasury Inspector General for Tax Administration, "Improper Payment Rates for Refundable Tax Credits Remain High," May 10, 2021, https://www.treasury.gov/tigta/auditreports/2021reports/202140036fr.pdf (accessed March 27, 2022).

[32] Ibid.

permanently enact the American Rescue Plan's expanded tax credits—which take the form of monthly payments of $250 to $300 per child without any work requirement—could significantly increase improper payments.

For starters, the increased amount, from between $1,400 and $2,000 per year to between $3,000 and $3,600 per year, would entice more people—whether criminals or family members who are not entitled to the payments—to wrongly claim them. By removing the current child tax credit requirement that individuals have reported taxable income to claim the credit, it would be easier for people to falsely claim monthly child payments. And the monthly delivery of nearly 900 million child payments (as opposed to the current 70 million annual payments) based on individuals' prior years' tax filings could result in payments delivered to the wrong addresses or wrong bank accounts. [33] I estimate that improper payments could increase by $19 billion to $40 billion per year.[34]

Most families, and the children in them who will effectively have to pay for the child payments their parents receive through higher taxes on their future earnings, would be better off with lower tax rates on their earnings throughout their lifetimes.

Childcare Subsidies: Potentially High Error Rates, Risk for Children's Identities. President Biden has proposed to spend $225 billion of taxpayers' dollars to provide subsidies for the childcare of virtually all young children in the U.S. Setting aside the fact that these subsidies would disproportionately benefit wealthy, city-dwelling families while driving up the cost and limiting the supply of childcare for others,[35] these payments would likely have very high rates of improper payments, similar to the Earned Income Tax Credit (27 percent improper payments in 2021) and Obamacare Subsidies (27 percent improper payments in 2019—the most recent estimate available).[36]

In addition to improper payments, we already know that many parents would lack access to eligible childcare programs, the subsidies would drive up the cost of childcare by as much as 100 percent, and the majority of families that use faith-based childcare would not be able to receive subsidies at those providers. Putting government—instead of parents—in charge of childcare would mean higher costs, fewer childcare options, and smaller after-tax incomes.[37]

Government Paid Family Leave Inferior for Workers and Ripe with Privacy and Fraud Concerns. Among the many other government

[33]There were an estimated 74.1 million children ages zero through 17 in the U.S. in 2021. Multiplying this figure by 12 equals 890 million monthly child payments. The current Child Tax Credit excludes 17-year-olds, resulting in roughly 70 million children ages 16 and under in 2021. Child population figures: Childstats.gov, "POP1 Child population: Number of children (in millions) ages 0–17 in the United States by age, 1950–2019 and projected 2020–2050," https://www.childstats.gov/americaschildren/tables/pop1.asp (accessed August 1, 2021).

[34]Author's estimates based on improper payment rates ranging from 12 percent (ACTC) to 27 percent (EITC) and $1.6 trillion estimated cost of making the ARP child payments permanent in Erica York and Huaqun Li, "Making the Expanded Child Tax Credit Permanent Would Cost Nearly $1.6 Trillion," Tax Foundation, March 19, 2021, https://taxfoundation.org/expanded-child-tax-credit-permanent/ (accessed August 1, 2021).

[35]Rachel Greszler, "Government Childcare Subsidies: Whom Will They Help Most?," Heritage Foundation *Issue Brief* No. 5231, October 20, 2021, https://www.heritage.org/sites/default/files/2021-10/IB5231.pdf.

[36]U.S. Treasury, "Improper Payment Rates for Refundable Tax Credits Remain High."

[37]Rachel Greszler, "The Role of Childcare in an Equitable Post-Pandemic Economy," testimony before the Subcommittee on Economic Policy, Committee on Banking and Urban Affairs, U.S. Senate, June 23, 2021, https://www.banking.senate.gov/imo/media/doc/Greszler%20Testimony%206-23-21.pdf (accessed March 28, 2022).

programs the Biden Administration seeks to establish is a federal paid family leave program. Unlike receiving paid family leave through an employer—who already has the individual's information, regularly sends them paychecks, and has a good gauge of the legitimacy of the individual's paid family leave claim—qualifying for and receiving paid family leave benefits from a federal program would require individuals to provide significant personal, medical, and financial information and then wait weeks or longer to find out if they are eligible to take leave from work, including for an issue that may have required immediate leave.[38] When Washington State's program began, workers were having to wait weeks and months after they needed to take paid leave just to find out if they were eligible for it.[39] This would also provide opportunities for criminals to file fraudulent claims on behalf of individuals, and for improper payments based on false or mistaken eligibility claims.

To simultaneously create a more efficient government, give individuals more autonomy and income, and reduce improper payments, policymakers should:

- **Reduce and/or eliminate tax credits** in favor of lower overall tax rates.
- **Reject new and expanded entitlement programs** in favor of policies that would empower individuals over bureaucrats.
- **Enact Universal Savings Accounts (USAs)** so that more Americans can save in a single, simple, tax-free account for whatever needs arise.[40] When taxed less, Americans can save more, and when they have more savings, they have less need to navigate complex, eligibility-based social programs.

Summary

Improper government payments are at unacceptable levels, exceeding $281 billion in 2021 (even excluding many programs like Obamacare subsidies), with some programs improperly paying more than one of every four dollars.

Preventing improper payments requires three key components: identifying whether individuals filing for benefits are who they say they are, verifying that they are eligible for the benefits they claim, and limiting the number of government programs Americans need to interact with in their everyday lives.

The disastrous pandemic UI programs demonstrate the massive consequences of failure on all three of these components. As cybersecurity threats will only continue to grow and improper payments have been expanding at an exponential rate, it is imperative that policymakers learn from these failures and act now to better protect Americans' hard-earned tax dollars and personal identities.

While standards exist to significantly improve identity verification, as do program-specific policy reforms that would enhance eligibility verification, many government agencies are

[38] Rachel Greszler, "4 Reasons Why Liberal Politicians Should Abandon Federal Takeover of Paid Family Leave," Daily Signal, October 28, 2021, https://www.heritage.org/jobs-and-labor/commentary/4-reasons-why-liberal-politicians-should-abandon-federal-takeover-paid.

[39] Rachel Greszler, "Coronavirus Shows Government Paid Leave a Bad Fit for Employees' Needs," Daily Signal, March 8, 2020, https://www.heritage.org/jobs-and-labor/commentary/coronavirus-shows-government-paid-leave-bad-fit-employees-needs.

[40] Adam N. Michel, "Universal Savings Accounts Can Help All Americans Build Savings," Heritage Foundation *Backgrounder* No. 3370, December 4, 2018, https://www.heritage.org/taxes/report/universal-savings-accounts-can-help-all-americans-build-savings.

not applying these standards or implementing the necessary policy changes. This includes failure of agencies to take actions that they are already capable of or are supposed to be doing on their own, and policy changes that require administrative or legislative action.

In addition to taking needed measures to protect the integrity of existing government programs, policymakers should also seek to limit the number of government programs with which Americans need to interact. Not only are government programs a source of improper payments and a potential for identity theft, but they replace personal autonomy and opportunity with bureaucratic control and smaller incomes, ultimately leaving many people worse off. Policymakers could better protect taxpayers' dollars by taking less in taxes to begin with so that Americans can decide—without bureaucratic approval—what they want to spend their money on and when they want to spend it.

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