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NEW JERSEY STATE LEGISLATURE

OFFICE OF FISCAL AFFAIRS

SPECIAL PROGRAM ANALYSIS OF UNEMPLOYMENT INSURANCE FRAUD DETECTION AND CONTROL ACTIVITY IN THE NEW JERSEY DIVISION OF UNEMPLOYMENT AND DISABILITY INSURANCE

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The Law Revision and Legislative Services Commission authorized the release and publication of this special program analysis in August, 1975.



New Jersey State Legislature

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August 18, 1975

MEMORANDUM TO: Members of the Law Revision and
Legislative Services Commission

The Office of Fiscal Affairs herewith submits a special program analysis of unemployment insurance fraud detection and control, prepared pursuant to N.J.S.A. 52:11-47e.

This special analysis was completed by our Division of Program Analysis headed by Gerald D. Silliphant.

Throughout the course of this analysis, the Office of Fiscal Affairs' staff enjoyed the cooperation and assistance of the officials and staff of the Department of Labor and Industry.



Kenneth N. Bragg
Executive Director

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FOREWORD

The Office of Fiscal Affairs was established by Chapter 211 of the Laws of 1971 which requires the Executive Director of the Agency to "ascertain compliance with legislative intent by the conduct of performance audits and efficiency studies..."

Accordingly, a Division of Program Analysis was activated within the Office of Fiscal Affairs to provide a program evaluation organization for the Legislature. The Division is staffed by a group of professional analysts, each assigned to perform comprehensive evaluations of specific State programs. The Division reports to the Legislature through the Law Revision and Legislative Services Commission, chaired by Senator John J. Horn.

This review of unemployment insurance fraud detection activity was initiated under Commission direction in response to an inquiry by Senator John F. Russo and addresses the specific question of whether fraud has been a major factor in undermining the stability of the Unemployment Compensation Fund. The analysis was limited to this general question because of the extreme condition of unemployment in the State during the research period; the interim nature of existing computerized controls; the imposition of several new Federal unemployment insurance programs; and recognition of the efforts of the Department of Labor and Industry to comprehensively evaluate the unemployment insurance system through the Task Force on Unemployment Insurance. A larger effort may be warranted after the conversion to new computer programs is complete and the Department has successfully utilized the new system for a full year.

The unemployment insurance program is a complex one. Its operations involve a unique association of the Federal government, the State of New Jersey, and the employers and employees of industry in the State. The structure of the system had been revised by Chapter 83, Laws of 1974 specifically because the fund reserves had consistently been depleted to provide benefits claimed since 1968. The condition resulted from factors other than fraud as addressed in the review.

The response to this review from Commissioner Joseph A. Hoffman, a copy of which is appended, raises some questions regarding recommendations made in this review. While the scope of the review was limited, the appraisal was thorough and the

differences in opinion raised by the Commissioner's letter are referred to the Legislature for determination. There are two such areas:

- 1) The Department appears hesitant to explore alternatives to the present system of fraud prosecution, possibly in recognition of organizational problems which might result from the recommendation for an administrative court. The review indicates that the present prosecution system is both slow and limited in correcting detected abuses of benefit payments and that a method of abbreviating present procedures, excluding the use of municipal courts, and reducing the demands on prosecution for abuses merits serious attention.
- 2) The Department is opposed to a "permanent disqualification" for persons defrauding the unemployment insurance system and states that "severe penalties are available currently." The review indicates that the "severe penalties" are limited to a fine and temporary (17 week) disqualification from benefits and reduction in benefit amounts possible. These penalties are aimed at persons continuing to receive benefits, indicating early detection and adjudication of individual cases. This has not been the experience of the system, and this review reveals that these penalties are inoperative and ineffective.

The analytical work and report writing on this study were performed by Deborah E. Savar and Wesley R. Westmeyer of the Division of Program Analysis.

Further contact between the Office of Fiscal Affairs and the Department of Labor and Industry will be maintained through the program analysis compliance activity established within this agency and intended to assist both the Legislature and the State Departments under review with the implementation of program analysis recommendations.

The Division of Program Analysis wishes to acknowledge the cooperation and assistance provided by the Commissioner of Labor and Industry, the Assistant Commissioner for Unemployment and Disability Programs and their staffs.

August, 1975



Gerald D. Silliphant
Director
Division of Program Analysis
Office of Fiscal Affairs

SUMMARY OF FINDINGS AND RECOMMENDATIONS

The Law Revision and Legislative Services Commission of the Legislature directed a study be made to determine if fraud in the New Jersey Unemployment Compensation Program was a factor undermining the stability of the Unemployment Insurance Trust Fund. This report centers on five questions in this area and the responses thereto developed during the study, and is not an evaluation of the entire Unemployment Compensation Program.

Question 1: Is the Fraud Detection Unit Activity Adequate?

Response: The organization and procedures followed are adequate. A U.S. Department of Labor, Manpower Administration Review of the New Jersey Benefit Payment Control Program completed on January 16, 1975 found the fraud unit activity to be "an efficient and effective operation with several aspects worthy of commendation."

The huge volume of claims experienced in the last 15 months has doubled the case backlog between 1973 (400 cases) and 1974 (800 cases). While an additional investigator has been requested, the sustained high level of claims (882,000 in 1974) suggests that the backlog will continue to mount.

It is recommended that the Department of Labor and Industry consider raising the number of investigators assigned to fraud documentation from seven to ten to eliminate present case backlogs and speed overpayments recovery and fine and interest collections.

Question 2: Is Fraud Prosecution Adequate?

Response: Currently only cases where a claimant has improperly accepted six weeks of compensation (about \$500) are prosecuted. Additional prosecutions may result because of perceived intent to defraud the State. These standards are based on the capacity of the Attorney General's Office to assign staff to prosecution and an agreement between the Department of Law and Public Safety and the Department of Labor and Industry. The agreement to use these guidelines reduced the flow of cases for prosecution from about 80/month to about 30/month, but increasing workloads have prompted a suggestion that the line be redrawn so that cases of 10 weeks of improper compensation acceptance be prosecuted. Additional problems result from reliance on municipal courts to serve warrants on claimants who in many cases work in seasonal industry and have great mobility.

The deficiencies suggest another procedure is more appropriate.

It is recommended that an administrative court, with appeal procedures to the Judicial system, be established to make findings in cases of unemployment compensation fraud, that penalty consist of fine and permanent disqualification from benefits; and that cases of conspiracy to defraud be subject to both administrative and criminal prosecution.

Question 3: Are There Undetectable Fraud Activities?

Response: There are types of fraudulent claims which are almost undetectable by the standard detection techniques used by Labor and Industry. Misrepresentation of work status is detected by a check against Social Security records, but this detection device fails if a claimant uses multiple Social Security numbers or if a high-wage employee completes his Social Security contribution by the second or third quarter. Several types of claims, the temporary Federal programs and interstate claims, are not computer processed and thus have not had computer records to use in the "cross-match" system. Steps are being taken to correct this within the department.

Employer collusion with a fraudulent claim renders its detection nearly impossible. Non-recorded wages (cash labor) is hard to identify and prosecute. Some check is provided by "cross-match" and some employers have been detected.

Detected fraud amounts to less than one percent of all initial claims. Possible fraud was screened in about 49,000 cases in 1974, resulting in overpayments identified to 5,000 claimants. In that same year, 342 cases were disposed of in court with a backlog in January, 1975 of 988 cases.

Question 4: Are There Operational Problems That May Hinder Fraud Detection?

Response: The very heavy load of unemployment claimants in December, 1974-February, 1975 has affected all parts of claims operations. Fraud detection has suffered in terms of slower processing of unmatched claims to employers and slower reporting of charges to employers (for employer review). This heavy load is accentuated by the addition of two new Federal unemployment programs established on a temporary basis and the Department of Labor and Industry's conversion to a new computer system.

The unemployment insurance system has a central evaluation program, supplemented by annual Federal government reviews and bi-annual self-evaluations in local claims offices. A problem that escaped detection for a three-year period was a build-up in paid benefits that were not incorporated into a specific employer's record of charges. This problem received considerable attention in the Department and a consultant evaluated system-wide controls and recommended improvements (which have been implemented). The specific issue of capturing higher contributions from employers who may have benefited from a lower experience rating than deserved has been referred to the Attorney General's Office. No reply had been received by June 30, 1975.

There is no convincing evidence that the unmatched charge problem has been corrected. Its role in fraud detection is uncertain but of minor impact. Planners for computer conversion have indicated that procedures to be installed by June, 1976 will eliminate the problem entirely.

The amount of backlog in fraud investigations indicates perhaps a greater need for investigatory personnel than the section head acknowledges. The time lag between improper receipt of a check and documentation of charges can be a year or more. Greater productivity of investigatory work would speed up the process. Each investigator is expected to document two cases per day or approximately 500 cases per year. The volume of potential fraud indicates a 10-person unit would be more appropriate than the present seven man force (an additional investigator has been requested).

Question 5: Is Fraud Payout Seriously Affecting Unemployment Trust Fund Stability?

Response: Detected fraud amounts to a little less than one percent of new claims. There is no evidence to indicate large amounts of undetected fraud. With all overpayments estimated at less than one percent of benefit payouts per year, there is no evidence to indicate it is a problem affecting fund stability.

Unemployment Insurance Fund stability relates to broader issues of the type of industrial mix in New Jersey, the length and volume of claims, the structure of the employer and employee contribution schedules, and the special programs of extended benefits imposed on the system that have not been related to additional income. Benefit payment maximums are annually readjusted to correspond to wages while the tax structure had remained basically stable. These issues relate more directly to fund stability than fraud.

CHAPTER ONE: PURPOSE AND SCOPE OF STUDY

Objectives and Scope

Unemployment insurance fraud has been defined by the Department of Labor and Industry as deliberate misrepresentation in order to collect benefits.¹ In its most common form, fraud is committed by a person who is working and collecting benefits simultaneously. There have been instances of collusion between employers and employees to defraud the system. False or multiple Social Security numbers and work records are generally needed to successfully initiate a fraudulent claim. Some claimants have continued to receive checks despite returning to employment - another instance of misrepresenting their employment status. Misrepresentation of claimant identity has also occurred.

Such activities are violations of the legislative intent of the unemployment insurance program and the laws governing it.² Therefore, the primary purpose of this study is to describe and evaluate the adequacy of the fraud detection efforts of the Department's fraud detection section by the Benefit Overpayment Bureau, the referral and prosecution of cases, operational problems hindering fraud detection, and the impact of fraud payout on fund stability.

In limiting the scope of the analysis, Office of Fiscal Affairs (OFA) staff attempted to determine if present fraud detection procedures are appropriate, functional, and adequate. No express attempt was made to measure the extent of undetected fraud.

Methodology

The methodology for the analysis was as follows:

- The Unemployment Insurance Law, N.J. Administrative Code, relevant literature, and background documents were reviewed.
- Discussions were held with officials of the Department of Labor and Industry, the Attorney General's Office, and the Federal Manpower Administration, on the following issues:
 - a) fraud unit activities;
 - b) evaluation procedures for local claims offices;
 - c) conversion from the Spectra 7045 to IBM 370-158;

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1. Memo from Chief of Benefit Overpayments, N.J. Department of Labor and Industry, February, 1975.
 2. N.J.S.A. 43:21.

- d) the \$100 million chargeback omission; the lack of runs for cross-match tapes for two quarters of 1973; and the loss of computer "flags" on people billed for overpayments;
 - e) the collections and deposit process of employer taxes, experience rating of employers, the handling of delinquent accounts, and adjustments to accounts;
 - f) utilization of EDP staff and resources, training programs, development of standards of documentation, and employer chargebacks;
 - g) Federal-State relationship centering on New Jersey's Plan of Service and Cost Model implementation;
 - h) prosecution of fraud cases.
- Five meetings of the Unemployment Insurance Task Force, appointed by the Commissioner, were observed. Subjects dealt with were:
- a) Employment Service - Unemployment Insurance relationship;
 - b) Disqualifications;
 - c) New Federal unemployment legislation;
 - d) Testing labor market attachments;
 - e) Financing;
 - f) Fund solvency;
 - g) Benefit amount;
 - h) Duration of benefits;
 - i) Extension of coverage.
- Site visits were made to three local claims' offices - Toms River, Passaic, Perth Amboy - in order to observe local office conditions and operations and to hold discussions with office managers. Time constraints precluded visits to all 40 local claims' offices and numerous other itinerant offices; however, the offices that were selected are representative of conditions found in every local claims' office in the State.

CHAPTER TWO: OVERVIEW OF UNEMPLOYMENT INSURANCE
IN NEW JERSEY

The Unemployment Compensation Law of 1936 (N.J.S.A. 43:21, et seq.) established a State program for the disbursement of cash payments to covered workers who have lost their jobs through circumstances beyond their control, or are working less than full-time because of the lack of full-time work. The law allows the State to take advantage of Federal government loans and programs for the unemployed while establishing its own rules, contribution system, and benefit structure. The purposes of the law are:

"...to prevent its (involuntary unemployment) spread and to lighten its burden which now so often falls with crushing force upon the unemployed worker and his family...encouraging employers to provide more stable employment and by the systematic accumulation of funds during periods of employment and to provide benefits for periods of unemployment..."³

As of January 1, 1975, a person qualifies for unemployment compensation (of up to \$90 per week for a period of up to 26 weeks), if employed in a covered industry and if earnings in the previous 52 weeks totalled \$2,200 or more (or were at least \$30 in each of 20 weeks). Claimants must file a claim in an Unemployment Insurance Claims Office, report as directed, be available and able for work, and make an active search for work.

In 1975, the system receives contributions from 140,000 employers and 2.6 million employees. Unemployment tax revenues will provide an income of \$440 million in fiscal year 1976 but loans from the Federal government of about \$197 million have been received to match the estimated benefit payout of \$626 million. Some 400,000 claims will receive payments from the Unemployment Compensation Trust Fund during the year at the 39 local claims offices.⁴ There are some 1,765 employees administering Unemployment Insurance and Disability Insurance, with 1,463 positions paid for by the Federal government out of the Federal unemployment insurance taxes (about \$18 million).

Contributions to the fund are fixed by State and Federal law.⁵

3. N.J.R.S. 43:21-2, "Declaration of State Public Policy."
4. Plans have been announced for the number of local offices to grow to 59.
5. Employers see a gross rate reflecting unemployment and disability insurance rates combined as well as the detail of each rate in their quarterly bills.

Employees in New Jersey (only three states require employee contributions) contribute $\frac{1}{2}$ % of taxable wages (up to a maximum of \$4,800). Each employee will pay a total of \$24 each year into the fund. Employer contributions relate to a number of rate schedules depending on the status of the trust fund and an experience rating of the number of their employees involuntarily separated and filing for benefits. In 1975, the employers will be paying at rates between 1.2 percent and 6.2 percent. Employers pay quarterly, within 30 days of the end of a calendar quarter by applying the tax rate supplied by the Division of Unemployment and Disability Insurance against their quarterly taxable wages.

Some significant changes were made in eligibility requirements and tax schedules by Chapter 83, Laws of 1974. The maximum amount of taxable wages increased to \$4,800 from \$4,200 for calendar 1975, and in 1976 and thereafter would be adjusted annually in relation to the statewide-average-weekly-wage paid to covered employees. The rates increased from a range from 0.9 percent to 5.5 percent to a range 1.2 percent to 6.2 percent (when trust fund reserve ratios are under 2.5 percent). The legislation stiffened eligibility by raising the minimum income eligibility requirement from \$15 in each of 17 weeks or \$1,350 in the previous 52 weeks to \$30 in each of 20 weeks or \$2,200 in the previous 52 weeks. Benefit amount maximums were restricted by eliminating one option in effect in 1974.⁶

Description of Programs

Unemployment insurance claims offices process claims and handle payments for five types of programs plus an extended benefits program and two temporary Federal unemployment programs. The programs are:

State Unemployment Insurance - As described previously, presently excluded from coverage are public and non-profit employees, domestic and farm workers, and self-employed.

Interstate Claims Program - If wage credits are earned in another state but the claimant now resides in New Jersey and is unemployed, New Jersey cooperates by transmitting claim information to the state which will pay benefits. The arrangement is reciprocal for people who earned wage credits in New Jersey but are now residing out-of-state and are claiming benefits.

Combined Wage Claims Program - If wage credits are earned in New Jersey and any other state, the wage credits are combined and benefit eligibility requirements are

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6. A further review of the Unemployment Insurance Law was assigned to a Task Force appointed by Commissioner Hoffman. A report from the Task Force was expected to be forwarded to the Commissioner on April 30, 1975. Division of Program Analysis staff were invited to sit in on Task Force meetings and benefited greatly from the exchange of information and analysis generated at these sessions.

governed by the law of the state in which the claim is filed.

Unemployment Compensation for Federal Employees (UCFE) - A Federal government program to compensate involuntarily unemployed persons whose wage credits are in civilian Federal government employment. New Jersey is reimbursed for benefits paid under this program. The State law governs eligibility, benefit amounts, duration, and disqualifications.

Unemployment Compensation for Ex-Servicemen and Ex-Servicewomen (UCX) - A Federal program to compensate members of the armed forces who make the transition into civilian employment. Special benefit structures are in effect and, like UCFE, the State handles the transaction and is reimbursed.

Extended Benefits Program - New Jersey enacted a permanent program to pay benefits for an extended period of time when unemployment is high for sustained periods. The program, effective as of January 1, 1971, covers unemployment insurance, UCFE, and UCX, and will provide benefits when a claimant has exhausted his/her rights to regular compensation by reaching his/her total benefit amount or when his/her benefit year expires before he/she has drawn all his/her benefits and a new benefit year cannot be established. Amounts are limited to one-half of the total benefit amount payable on his regular claim.

Special Unemployment Assistance Program (SUA) - A temporary Federal program of special unemployment assistance to workers who are unemployed during a period when unemployment in the state exceeds 6 percent for three months who are otherwise ineligible for unemployment allowances under any other law. Claimants are eligible for up to 13 weeks of benefits under this program as determined by the State UE insurance law. The Federal government reimburses the State for benefits paid. The program expires on March 31, 1976.

Extended Coverage - Workers in non-covered areas of employment are provided coverage by Federal legislation. State and local government employees, farm workers, and domestic workers may claim unemployment benefits, as determined by the regular State law provisions, but benefits paid are 100 percent reimbursed by the Federal government. The program is temporary and is part of the legislation creating SUA.

Organization of the Division of Unemployment and Disability Insurance

The Division has four distinct operations as described on the organization chart (Exhibit A). The Director has a number of internal organizational functions reporting directly to him, including Personnel and Training, Budget and Accounting, Administrative Appeals, the Appeal Tribunal, and an internal management unit. The Assistant Director for Benefits manages all the claims offices as separated into four districts and a section containing the benefit payments control unit (fraud and overpayment discovery and documentation). The Disability Insurance program is organizationally distinct. Another Assistant Director deals with revenue functions: auditing employer payroll records and maintaining a comprehensive list of covered employers and the billing and collecting function.

The majority of the Division's 1,765 employees are involved with benefit payments in local offices. The functions of the entire division, however, went through an intensive cost analysis in the period July-December, 1972, in the project initiated by the Federal government to establish a cost model for all state unemployment insurance functions. The project (in which the State Division, the Unemployment Insurance Service of the U.S. Department of Labor and the Management Services Company cooperated) documented costs and procedures used at every point of operation. The cost model established administrative costs based on operations performed and the first year of operations under the cost model began on January 1, 1975.

Funding of Administrative Costs

The Federal Unemployment Tax Act (FUTA) is a part of the Internal Revenue Code (Sections 3301-3311) which taxes employers in New Jersey .5 percent of the first \$4,200 of the individual annual wages of employees. Nine-tenths of this tax is earmarked to cover the costs of employment security administration. This segment of the total unemployment tax goes to paying the cost of the administration of the State unemployment insurance law. The salaries, facilities, and supplies thus come entirely from non-state funds.

The first applications of the cost model to actual workload in administering unemployment claims for 1974 indicate that present unemployment insurance workload allows the expansion of permanent staff by some 60 positions. Additional positions will be created by the additions of the temporary Federal programs, SUA and EC.

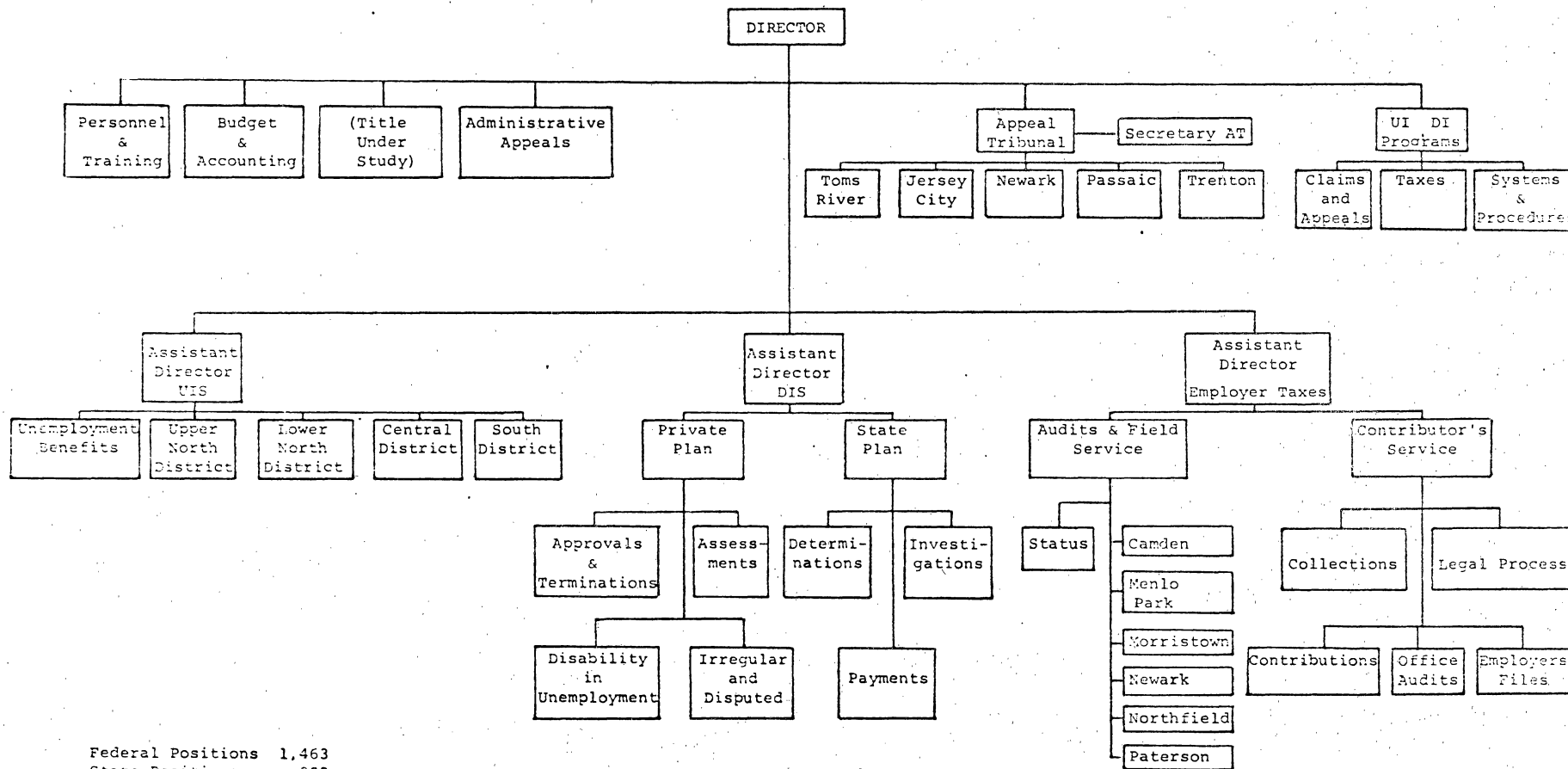
The purpose of the Federal funding of State unemployment insurance administration was to ensure "proper and efficient administration."⁷ The Federal government can set and enforce standards of operation and staffing of unemployment insurance offices would not be subject to individual states' budget priorities.

7. Title III of the Social Security Act.

Exhibit A

ORGANIZATION CHART

DIVISION OF UNEMPLOYMENT AND DISABILITY INSURANCE



Federal Positions 1,463
 State Positions 302
 Total 1,765

Evaluation Systems

The New Jersey Division of Unemployment and Disability Insurance has a three-tier evaluation system to continually monitor operations of the local claims offices. A year-round appraisal is monitored by a central evaluation staff to assess the adequacy of fact-finding, rulings on non-monetary issues (eligibility, disqualification, etc.), and documentation of actions on individual claims. The goal is for each local office manager to sample and evaluate 5 percent of the non-monetary determinations quarterly. Each local office is required to do a semi-annual self-appraisal on all operations and a central staff evaluates 10 local offices a year on all operations. A special set of instructions has been established for a Federal local office evaluation which must be completed in three local offices each year as a basis for the generation of the "Plan of Service."

Features of the Current Unemployment Crisis

The local claims offices in New Jersey are handling an unprecedented volume of claims, compounded by rapid implementation of temporary Federal programs and the conversion within the Department of Labor and Industry from a Spectra 7045 computer to an IBM 370-158. In three local offices visited in February, 1975, severe crowding conditions were noted, with office managers citing a volume of 1500-2000 people being serviced per day in each office.

The problem of overcrowding is being handled with two methods; one, some 20 new temporary locations are being sought; on April 7, claimants will be required to report in person only once in every four weeks instead of once in every two weeks. The space problem in offices was the major problem cited in processing claims with every office extending work hours to accommodate claimants and process paper work. Leasing new locations has proven a difficult process because of the difficulty of locating suitable space and obtaining both Federal and State government approval for the lease.

Exhibit B

MONTHLY VOLUME OF NEW CLAIMS FOR UNEMPLOYMENT
BENEFITS JANUARY, 1974—FEBRUARY, 1975

<u>Month</u>	<u>New Claims</u>	
	<u>UI, UCFE, UCX, IS</u>	
1/74	95,355	
2/74	69,047	
3/74	55,738	
4/74	57,715	
5/74	55,651	
6/74	59,061	
7/74	78,209	
8/74	62,611	
9/74	56,139	
10/74	71,226	
11/74	84,144	
12/74	137,320	(882,216) ¹
1/75	122,679	
2/75	89,107	

¹1974 Total

Source: N.J. Department of Labor and Industry, Division
of Unemployment and Disability Insurance.

CHAPTER THREE: BENEFIT OVERPAYMENT RECOVERY
ACTIVITIES IN LABOR AND INDUSTRY

The Benefits Control Bureau of the Division of Unemployment and Disability Insurance handles three categories of benefit overpayment:

- a) non-fraud - accidental benefit overpayments by the Department;
- b) fraud - wage-benefit conflict cases (collecting Unemployment Insurance benefits while employed). There are approximately 5,000 of these cases annually, amounting to about \$2 million in a system that paid over \$400 million in benefits in 1974.
- c) criminal - cases of deliberate misrepresentation in order to collect benefits. These cases frequently involve an attempt to collect a relative or friend's check by forging a signature, or to collect the check of a deceased claimant.

Presently there exists a \$10 million outstanding debt balance for all categories of overpayments, dating since benefits began in 1939.

Fraud Detection

According to Department officials, the most effective method of fraud detection is a 13-state "cross-matching" system of cooperation with the Social Security Administration, which New Jersey joined in 1971. A computer-generated tape containing information on all people filing Unemployment Insurance claims in New Jersey is sent quarterly to the system's headquarters in Wisconsin, where it is merged with those of other participating states. From Wisconsin, the tape is sent to the Social Security Administration in Baltimore, which runs a check with the participating states' wage reports. This information is sent back to Wisconsin where it is refined by state and returned to the individual states. The final information yields potential wage-benefit conflict cases for field investigation by the Department. An exception listing resulting from the cross-match system generates a mail form directed to a claimant's last employer of record requesting clarification.

It should be noted that to be included in the cross-match system, the state's tape must be received in Wisconsin on the date it is due. Department officials told OFA staff that New Jersey missed cross-match participation in the last two quarters of 1973 because of the failure of the computer section to compile the tape

on time.⁸ This failure was an isolated communication breakdown which should not reoccur.

The cross-match system is ineffective in detecting fraud in those cases of a claimant using multiple Social Security numbers and aliases, which would enable him to collect unemployment benefits under his real name while working under another. It is impossible to determine the extent of this activity, but it has been detected most frequently in claims from seasonal industry employees. Another shortcoming of the "cross-match" system as a fraud detection tool is that the "cross-match" operates most effectively for the first quarters of the year. If an individual's payments to Social Security cease because the annual limit on contributions has been reached, the quarterly tape will not be able to identify an exception. For example, a worker who earns \$600 per week will pay required social security contributions on 1975 standards in 21 weeks, or less than half of the year. If he works and fraudulently collects unemployment insurance benefits in the third or fourth quarters of the year, "cross-match" will not identify him as an exception because no wage reports are received on this individual.

The new Federal benefits programs - EB, EC, and SUA - will be manually processed at the local claims' offices and will by-pass the newly created Administrative Control Unit. Due to the extensive programming required in the implementation of the new computer system, the Federal programs have not yet been able to be included in the "cross-match," further hampering the fraud detection effort. Department officials are planning the inclusion of the Federal benefit programs in the "cross-match" system as soon as these claims are included in computer processing of claims.

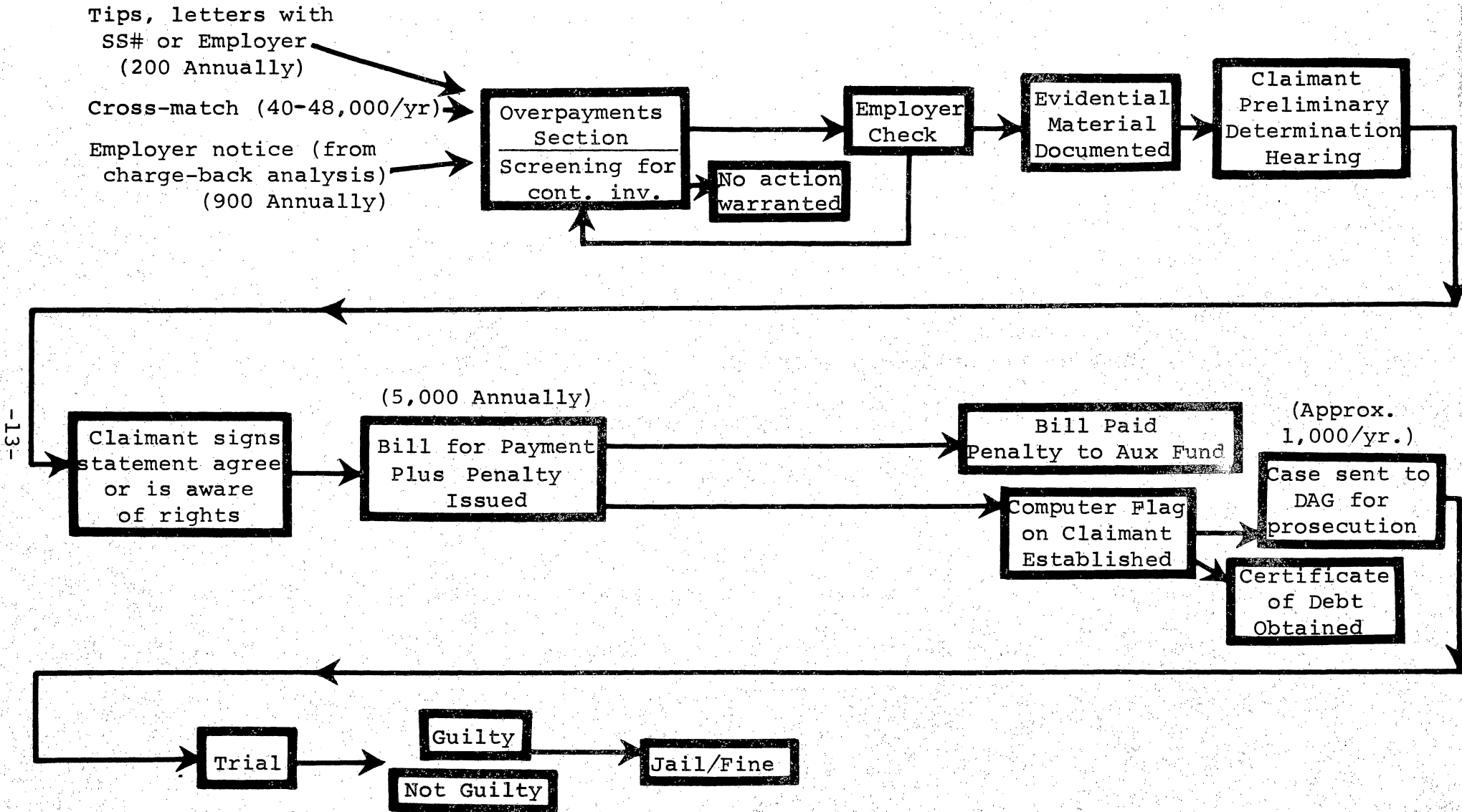
In addition to the "cross-match" system, the Department relies on tip-off letters from neighbors, relatives, or other claimants and employer notices to discover fraud. Approximately 200 letters are received each year with sufficient information (a tip must include the claimant's Social Security number or present employer) to enable the Fraud Unit to pursue an investigation. No estimate of the number of "crank" letters is available. Employer protests after receiving chargeback notices which they feel are unwarranted are another clue to potential fraud and average 900 such notices per year. Approximately 30,000 employers receive chargeback notices each month. (See Exhibit C for a chart of the entire fraud detection flow).

After possible fraud cases have been identified by the previous methods, they are assigned to seven field investigators who comprise two teams, one in Northern New Jersey and one in Southern and Central New Jersey. The investigators examine employer payroll records, cancelled checks, and other evidentiary material in order to develop a case that the individual was employed while collecting UI benefits. If warranted, the claimant is then summoned for a pre-determination

8. Interview with Supervisor of Fraud Inspection Section, January 17, 1975.

Exhibit C

UNEMPLOYMENT COMPENSATION FRAUD IDENTIFICATION AND FOLLOW THROUGH



Source: OFA Interview with Bureau of Benefits, Division of UI, N.J. Department of Labor and Industry, 1/14/75.

hearing, where he is informed of his rights, and confronted with the evidence obtained through the field investigation and asked to return the money. According to Department officials, most individuals admit their guilt.

Criminal Prosecution

A standard has been established by agreement between the Department and the Attorney General's Office, which calls for the criminal prosecution of claimants who fraudulently collected six or more weeks of benefits. This standard limits the number of prosecutions to a level manageable for the Department of Law and Public Safety. Three DAG's handle the prosecution of these cases for the Department in the municipal courts where the UI office is located and offense committed.

Some of these cases have been classified as "waivable misdemeanors," which means the defendant can waive the right to a grand jury indictment process. Most defendants admit their guilt, waive the grand jury, and receive trial and sentencing in municipal courts, where penalties are lighter. Municipal courts are favored by the State because they dispose of the cases faster than would be possible for the process requiring a grand jury indictment, and the procedure is also less expensive for the State.

According to officials in the Department of Law and Public Safety, most claimants involved in fraud cases are itinerants in laboring positions. This condition increases the difficulty in finding the defendants in order to serve warrants and bring them to trial. Currently there are 316 complaints set and awaiting the service of warrants by municipal authorities. For 1974, 322 claimant cases and 20 employer cases were disposed of by trial, most resulting in a fine and/or restitution.

The following statistics are from the January, 1975 Division of Criminal Justice Report:

Exhibit D	
STATUS OF FRAUD PROSECUTIONS	
<u>Claimant Cases</u>	<u>Employer Cases</u> (collusion for fraud)
832 cases on hand	124 new cases
180 new cases processed and pending	7 processed and pending
<u>1,012</u>	<u>131</u>
24 disposed of by trial	6 disposed of by trial
<u>988</u> total cases on hand	<u>125</u> total cases on hand

Employer cases are more difficult to document because of a lack of cooperation from the employer and employee. (Employers usually cooperate in the documentation of a claimant fraud case.) There is no legal penalty for failure to cooperate by an employer.

Repayment Procedure

In those cases of less than six weeks of fraudulent collection of benefits, the Department attempts to recover its money by sending up to three "Demand for Refund" notices. If the claimant responds by making restitution, the process is completed and the administrative fine is deposited in the UI Auxiliary Fund; however, should the claimant fail to repay the money, a computer "flag" is established on his name in the master file. On larger overpayments, the agency also files a certificate of debt which has been found to be an effective recovery method.⁹

The "flag" is an essential component of the offset program of recovering money owed to the State. If the individual who owes money on a previous fraudulent claim attempts to collect benefits, at any future date, his benefits are reduced by the amount he owes. However, in no case has the Department initiated a civil action against a claimant. Department officials feel that, although the offset program is a good means for recovering money, in some cases a court action is justified and desirable.¹⁰ The flagging procedure followed thus far incorporates all overpayments on record since 1936, a system which includes overpayments which are not collectable, and inflates the figure of total overpayments outstanding.

The Manpower Administration Review

The Manpower Administration Review team of the U.S. Department of Labor conducted its analysis of New Jersey's UI Benefit Payment Control Program during the week of December 9, 1974. The conclusion of the report was that New Jersey's benefit payment control program is "an efficient and effective operation with several aspects worthy of commendation," specifically the centralized organizational structure which "enhances operating control, encourages functional integration, and reduces duplication of effort." In addition, the report praised the agency for its well-organized and efficient system for effecting recovery of overpayments."

The report disclosed problem areas and made recommendations for changes in operating procedures to correct them including:

A. Interstate Claims

No comprehensive procedure exists for detecting improper interstate claims where a claim is filed against New Jersey by an individual who is working and claiming benefits while residing in another state. The U.S. Department of Labor recommended extending the Social Security cross-match to include interstate liable claims.

Department officials indicated that plans are presently being formulated to implement the recommendation.

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9. U.S. Department of Labor, Manpower Administration, "New Jersey: Review of Benefit Payment Control Program," December 9-13, 1974.
 10. Interview with Supervisor of Fraud Inspection Section, January 17, 1975.

B. Return to Work Procedures

At present, no verification is made of wages or return-to-work date, which may result in fraudulent forms being submitted. For example, a claimant, after returning to full-time work, may continue to claim benefits for an additional week or more until he receives his first paycheck. Discussions with local office managers corroborated this potential source of fraud. Lacking a formalized verification process, local office employees must assume honesty on the part of claimants.

Although only one or two weeks of fraudulent benefits would be involved in such a case, the Federal recommendation was that the Department revert to a back-to-work verification procedure. The report recommends assigning this duty to the central office in Trenton, a change which would have the "additional advantage of eliminating a potential source of local office internal fraud."

C. Information Pamphlet

The information pamphlet distributed to new claimants fails to mention the administrative and maximum criminal penalties for fraud. Therefore, it was also recommended in the Manpower Review that when revisions are made to the pamphlet, such a statement should be included in the hope that it may act as a deterrent to potential fraudulent claimants.

One indicator of New Jersey's benefit payment control activities for CY 1971-1973 in comparison to national standards is revealed in the following administrative data:

Exhibit E				
NEW JERSEY FRAUD INDICATORS				
	<u>1971</u>	<u>1972</u>	<u>1973</u>	<u>U.S. 1974</u>
Fraud cases per 1,000 first payments	3.67	4.06	9.38	6.80
Non-fraud cases per 1,000 first payments	43.84	44.12	32.91	39.84
Restitution as percent of all overpayments	62.89	56.56	39.58	55.74

Source: U.S. Department of Labor, "New Jersey: Review of Benefit Payment Control Program," December, 1974.

The table shows that fraud cases per 1,000 first payments have been increasing over the past three calendar years and for CY 1973, New Jersey's figure is 38 percent above the national median.

Non-fraud cases per 1,000 first payments have been declining over the three year period, and for CY 1973 are 17 percent below the national median. Restitution as a percentage of all overpayments has also been declining between 1971 and 1973. For CY 1973 New Jersey's percentage was 29 percent below the national figure. Some allowance should be made for the fact that New Jersey collection statistics are cumulative, reflecting all overpayments since 1939.

Fraud is committed in the UI benefit program, as it is in all insurance and welfare programs. The extent of fraud is difficult to measure, because it relies on abuse and misuse of wage records. By establishing the Fraud Section in the Bureau of UE Benefits, the Department has made a determined effort to uncover the fraud that has been committed and to recoup the money falsely obtained. Seven fraud investigators are a part of the Unit. They are stationed in the field, but their case assignments are made and monitored by the central office in Trenton. Although the seven investigators operate under minimal supervision while in the field, they are expected to complete their quota of two case documentations per working day.

As of December 31, 1974, the backlog of active cases was approximately 800. With existing staff and workload standards, it would require the full-time efforts of the investigators for 57 working days to eliminate the accumulated backlog.¹¹ To put this in perspective, if they started on July 1 (the first day of FY 1976), they would finish on September 19. However, this calculation ignores the existing workload, which would then constitute a sizable backlog. At the rate of 890,000 initial claims annually, the backlog could mount to a level justifying 18 new investigators. (See Exhibit F.)

In a discussion with OFA staff, the Chief of the Enforcement Bureau of the Department of Law and Public Safety expressed the feeling that the Department of Labor and Industry is doing an adequate job of documenting fraud cases. He also suggested that the number of fraud cases uncovered is a function of manpower--the more people looking for fraud, the more they'll find.¹²

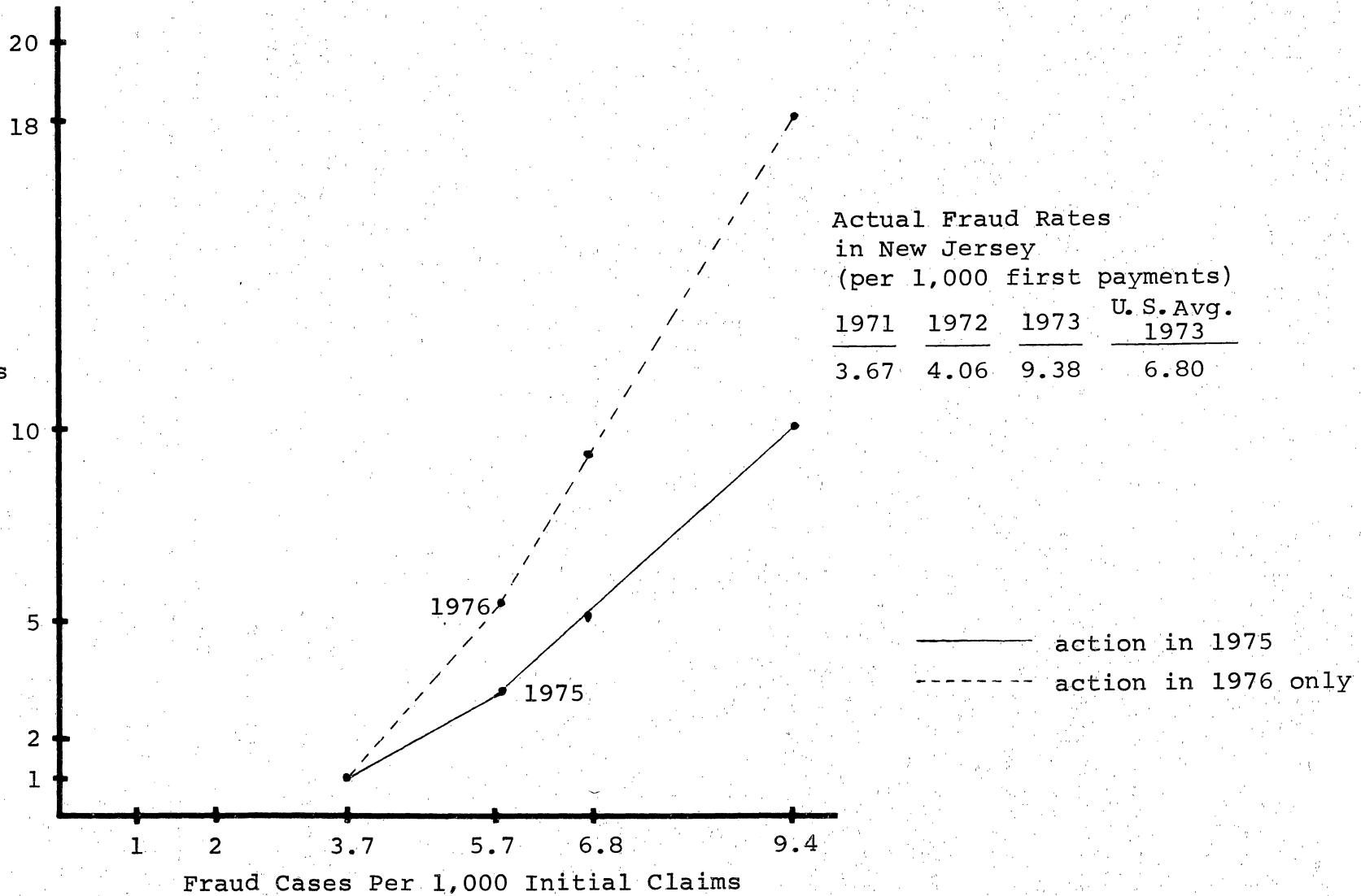
It is apparent that more investigators are needed to diminish the existing backlog, and to handle current ongoing caseloads. Therefore, *it is recommended that the Department make the necessary additions to the Fraud Unit's staff to enable it to more effectively execute the mission for which it was established.*

11. $7 \times 2 \times 57 = 798$.

12. Interview with Chief of Bureau of Enforcement, New Jersey Department of Labor and Public Safety, February 5, 1975.

Exhibit F

ADDITIONAL UI FRAUD INVESTIGATORS REQUIRED
TO ELIMINATE BACKLOG IN NEW JERSEY
(At 890,000 Initial Claims Per Year)



Source: U.S. Department of Labor, Manpower Administration
"N.J.: Review of Benefit Payment Control Program, Dec. 9-13, 1974"

Following documentation, cases meeting the standard of six weeks or more of fraudulent collection are referred to the Department of Law and Public Safety, where three Deputy Attorney Generals handle the prosecution in the municipal courts. As previously mentioned, 322 claimant cases and 20 employer cases were disposed of by trial in 1974, or 29 cases per month. Before the implementation of the six-week standard, the Department was receiving about 80 cases per month. According to Department officials, they were only able to dispose of 30 to 40 cases per month, and were subsequently accumulating a huge backlog which lengthened the time lag from commission of the offense to trial date. This situation was the impetus for establishing a six-week standard, or a maximum of \$540 in benefits, which would reduce referrals. At present, consideration is being given to increasing the number of weeks of illegal collection which would constitute a criminal referral. As many as 10 weeks of benefits would be handled in Department of Labor and Industry administrative hearings rather than in municipal courts, further reducing criminal referrals to the Attorney General's Office.

As of January 30, 1975, 988 claimant cases and 125 employer cases are being prosecuted by the Attorney General's Office; however, 316 complaints are set and awaiting service of warrants and many other cases are in various stages of documentation. The time lag from commission of misdemeanor to trial date is about a year, due to the difficulties involved in municipal court officials locating itinerant offenders and serving them with warrants. It is apparent that the referral of criminal fraud cases is based on an arbitrary, inadequate standard and that the prosecution of these cases in the municipal courts does not justify the time, expense, or rewards of the process. *Therefore, it is recommended that all cases of fraudulent collection of benefits should be handled in Department of Labor and Industry administrative hearings, except for cases of conspiracy to defraud the system, involving several claimants and thousands of dollars. It is further recommended that the penalty be changed to repayment of falsely obtained monies, an administrative fine, and permanent disqualification from the collection of benefits for the lifetime of the offender. Necessary additions to staff should be made in order to fulfill the requirements of the recommendation.*

Different states have different ways of handling fraud statistics. Most states retain fraud debt on their books for the length of the statute of limitations, at which time it is then eliminated. New Jersey retains the debt on its books permanently, a practice which results in a poor comparison with other states in collections. The Northeast Regional representative of the Federal Manpower Administration has suggested that New Jersey's Department of Labor and Industry consider changing this.

On the whole, however, the U.S. Department of Labor is satisfied with New Jersey's fraud detection activities although New Jersey is not doing quite as extensive a job as other states in the Northeast (for example, New York, which has a force of 300+ investigators).

The Federal government annually reviews the performance of the State Unemployment Insurance System as a part of an annual "plan of service" review. The evaluation consists of matching performance in certain areas against national standards. Any substantial deviation requires a specific plan of corrective action to be submitted by the State.

CHAPTER FOUR: STATUS OF THE NEW JERSEY UNEMPLOYMENT
INSURANCE FUND

Historical Background

Since its establishment, the New Jersey Unemployment Insurance Fund has been maintained through three wars (World War II, the Korean campaign, and the Vietnam conflict) and five post-war recessions (1949, 1954, 1958, 1961, and 1974-75). Rapidly built up during World War II, the Fund accumulated reserves until the end of 1953. It absorbed without difficulty the 1946 unemployment resulting from the reconversion of industries to peacetime production and the 1949 post-war recession.¹³ (See Exhibit G.)

After reaching an all-time peak of \$503.6 million in reserve at the end of 1953, three ensuing recessions significantly eroded the Fund until reserves fell to \$298.8 million at the end of 1964. Subsequent economic prosperity, the effects of a contribution base increase and a rise in the taxable employee wage base substantially improved the Fund balance to \$477.1 million at the end of 1969. During 1970, a year which experienced economic slump, the Fund reserves dropped by \$35.5 million. The volume of higher insured unemployment continued into 1971.¹⁴ Through the early 1970's, benefit payouts substantially exceeded contribution income, which further depleted reserves. The present New Jersey situation has arisen because while contributions during 1974 were at an all-time high of \$365 million, benefit payments rose from \$352 million to \$496 million, a more than \$100 million increase in benefit disbursements over a one year period. It now appears that disbursements for the year 1975 will surpass those of 1974 substantially.

The impact of the current recession is being felt acutely in New Jersey, partially due to its industrial mix. New Jersey's industries include many of those being most affected - automobile, manufacturing, garment and textile manufacturers, seasonal shore employers, glass producers, and affiliated housing activities (construction industry, electrical equipment production). The result is a 10.6 percent¹⁵ seasonally-adjusted UE rate, the highest in the nation and the highest in New Jersey since the Depression of the 1930's.

Extended Benefits

Under Title II of the Employment Security Amendments in 1970 and incorporated in New Jersey law, extended benefits are paid at

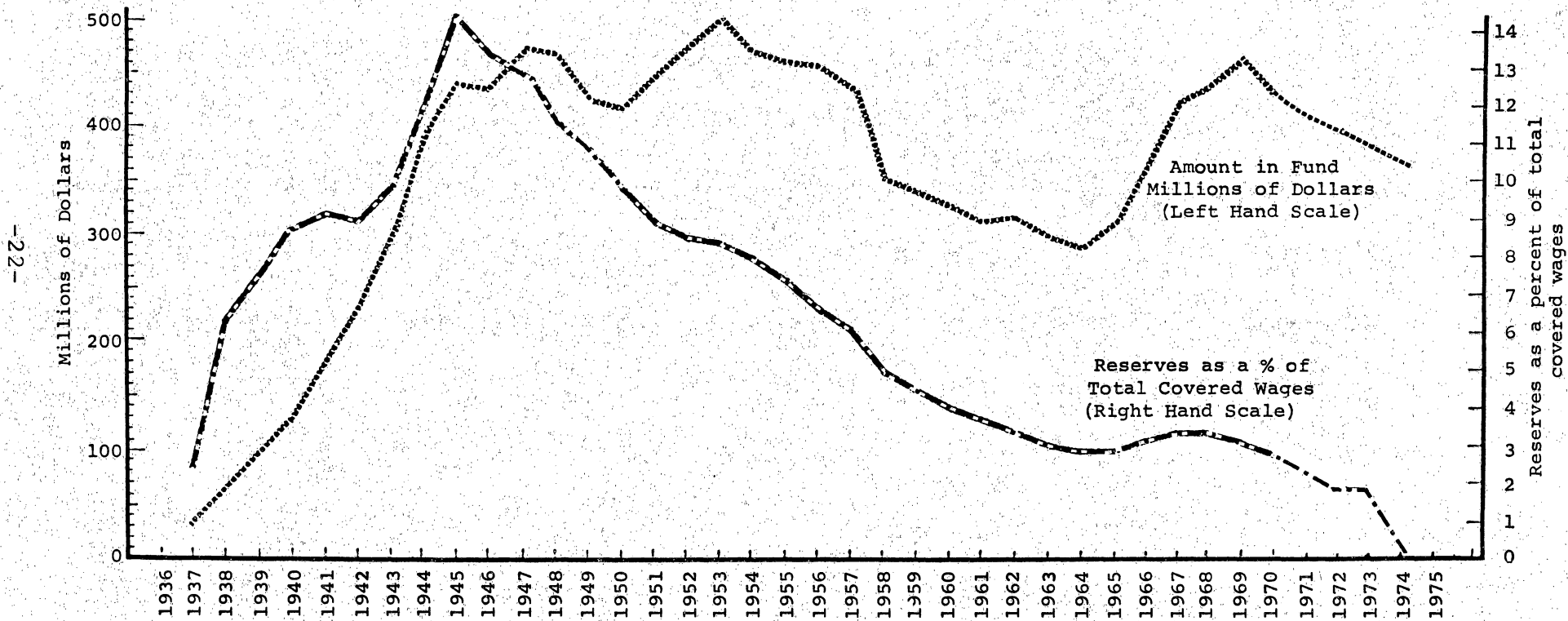
13. UE Insurance in New Jersey, 1936-1970, A Statistical Handbook, June, 1971, p. 9.

14. Ibid., p. 9.

15. As of February, 1975.

Exhibit G

THE NEW JERSEY UNEMPLOYMENT COMPENSATION FUND
RESERVE BALANCES AS OF DECEMBER 31, 1937 - 1975



present under a dual trigger system to unemployed workers who have exhausted their regular benefits during periods of high UE. A worker receives the equivalent of his weekly benefit entitlement up to a maximum of 13 added weeks (26 weeks is maximum regular duration of benefits), with an overall limitation of 39 weeks of combined regular and extended benefits.

The present national and State triggers operate in the following manner:

National "On" and "Off" Indicators

The extended benefit (EB) program triggers "on" for all states when the seasonally adjusted insured unemployment rate (IUR) for the nation is 4.5 percent for one calendar quarter. The national program triggers "off" when the IUR falls below the required level for one calendar quarter.

State "On" and "Off" Indicators

A state program goes into effect in a particular state without regard to the national IUR if the adjusted IUR for that state has averaged 4 percent for any 13-consecutive-week period and has exceeded 120 percent of the state's average IUR for the corresponding 13-week period in the two preceding years. The state program continues in effect until the state's unadjusted IUR for any 13-week period drops below either the 4 percent IUR or 120 percent of the 13-week average rate for the two preceding years.¹⁶

Once triggered "on," both national and state programs are legally required to remain active for at least 13 weeks. Once triggered "off," they must remain off for at least 13 weeks. The IUR has been triggered on in New Jersey several times in the past three years, a situation which has greatly drained the Fund.

Although the EB program operates on a 50-50 cost sharing arrangement between the State and the Federal UI Fund, the costs to the individual state are tremendous. It is presently triggered "on" in New Jersey and the State's share of the cost has been approximately \$3 million per month in 1974.

Federal Borrowing and Repayment

Under Title XII of the Social Security Act, a state which faces the prospect of being unable to pay benefits because of depletion of its unemployment fund may apply for an advance from the Federal UI account in the Unemployment Trust Fund. Requests

16. Explanation and justification of the "UC Amendments of 1975," Interstate Committee of Employment Security Agencies (ICESA), January, 1975.

for such advances must be confined to specific needs for a calendar month and must be formalized in a request from the Governor of the State to the U.S. Secretary of Labor. New Jersey is among several states which are now in this position.

In January, 1975, New Jersey borrowed \$74,380,000 from the Federal Fund, \$43,500,000 in February, and approximately \$47,000,000 in March in order to pay benefits. (All loans are interest-free.) Department officials have related that more will have to be borrowed in April, and possibly more again during the summer months.

The repayment deadline for the money borrowed thus far is November 10, 1977. There are two ways in which New Jersey could repay the loans:

- a) a 2 percent tax on New Jersey employers' taxable wages, 1 percent on 1975 taxable wages, and 1 percent on 1976 taxable wages; or
- b) a .3 percent increase in the FUTA tax on employers, effective after the November, 1977 deadline, until the loans are repaid.

Significant Factors Affecting Fund Stability

No precise definition or standard of fund stability exists in New Jersey law or administrative guidelines; generally, however, if a state's UI Fund reserve ratio is less than one and one-half times the highest benefit cost rate since 1958, it is regarded as inadequate to meet potential liabilities.¹⁷ According to this measure, 31 states, including New Jersey, had inadequate reserves as of the end of 1973.

Primary concerns at this time are what steps should be taken to restore Fund solvency, how to repay borrowed amounts to the Federal Treasury, and, upon resolution of the above, how to then build up Fund adequacy and maintain stability. These and other issues were dealt with by the Unemployment Insurance Task Force appointed by the Commissioner in September, 1974 to study the UI law and administration and develop recommendations for improvements.

The financing mechanisms of the program are the most essential to the attainment of Fund solvency, and departmental research indicates they may be less adequate and equitable than in the past.¹⁸ Among the possible changes being evaluated are the issues of taxable vs. flexible wage base and different standards of experience rating of employers in order to determine contribution amounts.

17. This is the standard developed by the United States Social Security Administration.

18. N.J. Department of Labor & Industry, Issues in the Financing of Unemployment Insurance, unpublished paper presented to the Unemployment Insurance Task Force in January, 1975.

The current economic downturn and resultant high unemployment caused the major drain on New Jersey's Unemployment Trust Fund reserves. Also contributing to the decline are rapidly rising wage levels. Continued inflation of wages directly affects benefit rates but is not reflected to the same extent in the taxable wage base. Since 1940, average benefit payments have increased 500 percent nationally, but the taxable wage base used in most states has increased only 40 percent.¹⁹ The widening gap between taxable and total wages results in progressively inadequate financial support of the program unless accompanied by an increase in the tax rate. However, repeated raising of tax rates can eventually lead to a breakdown of the state experience rating system.²⁰

Several other secondary variables impact on the stability of the Fund and deserve mention. Liberal New Jersey UC benefits have produced an average employer tax rate that is 60 percent more than the national average. This is one aspect of the total business tax structure which results in a flow of New Jersey industries to other states which have a more advantageous business climate. The New Jersey Manufacturers Association conducted a survey of over 2,300 business concerns in October of 1974. The survey reveals that New Jersey government was viewed as anti-business, and that business taxation was especially disturbing. In a January, 1975 issue of "N.J. Business," an analysis of the survey states "Undoubtedly, business' view of the tax picture goes a long way toward explaining the less than enthusiastic endorsement of New Jersey as a location for new or expanded facilities, and is at least partial cause of the planned net outward movement of firms this year."

A campaign to lure industry into New Jersey was recently announced by the Labor Commissioner and subsequent results were that several firms had opened and new jobs made available. The recently established Economic Development Authority is also working in the area of industry stimulation and job creation. These are positive efforts to stem the industrial exodus, but more is needed in the way of a re-evaluation of industry taxation.

It is presently possible for a mandatorily retired person who is receiving Social Security benefits and a pension to collect UE benefits. As there is some question as to whether retirees fulfill eligibility requirements, the granting of benefits to retirees may be in conflict with legislative intent. Thirty-five states have enacted legislation of offset private pension plan payments and twelve others offset Social Security payments. The New Jersey Legislature may wish to pursue an investigation of the effects on the New Jersey Fund of enacting similar legislation to offset pension or other old age insurance payments.

19. Monthly Labor Review, State UI Changes in 1974, January, 1975.

20. Doyle Report.

Existing New Jersey law does not distinguish disqualification for "gross" misconduct from misconduct, a distinction made in several other states. The result is that a temporary disqualification, or postponement of benefits, applies to a claimant discharged for a minor company rule infraction, such as repeated lateness, and a claimant discharged for aggravated assault and battery or embezzlement. Both claimants would receive benefits after the temporary disqualification period. The Legislature may wish to consider the appropriateness of such a provision, which allows felons to collect UI benefits.

CHAPTER FIVE: UNEMPLOYMENT COMPENSATION
TRANSACTION PROCESSING

The operations of the Division of Unemployment and Disability Insurance are heavily dependent upon computer support. Each local office generates checks for UI, CWC, and EB programs through interaction with the central computer facility in Trenton. The Trenton office generates checks for interstate claims, UCFE, and UCX claims and mails them to claimants. Checks for EC and SUA claims will be manually generated until the computer is programmed to accept and account for these claim types. The checks generated in local claims offices are printed on terminals linked to the central computer facility. If the terminal or the central computer is out of order, checks are processed by aged Burroughs equipment which is no longer serviced or produced by the manufacturer. The computer also processes communications with employers on tax rates, bills, account status, and claims charged to a particular employer.

Computer services play an important part in detection of potential fraudulent claims. Two of the three methods used to detect potential fraud depend on computerized systems. The "cross-match" system is a computer tape comparison where exceptions noted result in computer-generated notices to employers requesting further information. Notices of claimants charged to employer accounts also may result in employer generated exceptions for investigation. There have been three significant operational failures in the last five years related to computer services. They are: a build-up in paid claims unmatched to employer accounts, the loss of "cross-match" submissions for the last two quarters in 1973 and the dropping of "flags" on the names of claimants who have received overpayments.

In December, 1973 the Commissioner of Labor and Industry engaged the firm of Coopers and Lybrand (CPAs) to assist the Department in identifying the extent of the discrepancy between paid benefits and charges to employers accounts and to determine an implementation plan for corrective action. The consultant prepared four subsequent reports:

1. Review of Unemployment Insurance Operations, March 15, 1974
2. Plan for Correction 1971, 1972, and 1973 Chargeback Discrepancies, May 11, 1974
3. Manual of Operating Systems and Procedures, Division of Unemployment Insurance Control Unit, November, 1974
4. Controls for the Local Office On-Line Processing System (LOOPS), December 12, 1974

The causes for the discrepancy were identified in the first report as:

"1. Satisfactory experience prior to the 1970's gave assurance that payments and chargebacks had been in reasonable balance and as a result existing mechanisms for reporting discrepancies were thought to be adequate.

2. The substantial increase in claim payment volume, the need to institute new unemployment insurance programs, and the hasty implementation of new computer systems in recent years resulted in the deterioration of existing controls, obscured the existence of problems and diverted attention from the need to establish improved controls.

3. Undue reliance was placed on the ability of the new "terminal" system to prevent discrepancies, and the extent to which the old "Burroughs" system continued to be used was not anticipated."

The system of manual controls was implemented within the Division.

The second report estimated the size of the 1973 discrepancy as \$45.8 million which was subsequently reduced to \$25.1 million by corrective action within the Division. The \$45.8 million discrepancy represented \$11.5 million in revenue for the Unemployment Trust Fund. Coopers and Lybrand suggested another \$6.2 million could be recovered.

The Office of the Assistant Commissioner for Unemployment and Disability Insurance indicates that while the internal steps to identify corrective employer charges have been taken, the legal responsibility to make retroactive charges is unclear. The problems of accounting for prior years charges, the reluctance to add this charge to employers while mounting a campaign to retain existing industry and attract new industry, and the harsh economic problems facing the State's employers may be arguments against implementing corrective chargebacks. The Commissioner did request an opinion from the Attorney General on the legal obligations involved, but no opinion has been rendered.

Final corrective action for this problem is planned for the new computer programming effort which will be tested in April, 1976. There are indications that this unmatched problem continues, and, although it is identified by an error listing in every case, the local office workload mitigates against taking timely correctional action. The follow-up of identified unmatched claims is not currently monitored through local office self-evaluations or central office monitoring procedures.

This weakness in operational procedures postpones some fraud investigations. Improper employer identification or the lack of it is a signal that the claim may be improper. While no information

has been lost, the investigatory and reclaiming activity is delayed for some questionable claims. All of the claims, meanwhile, are subject to "cross-match" procedures.

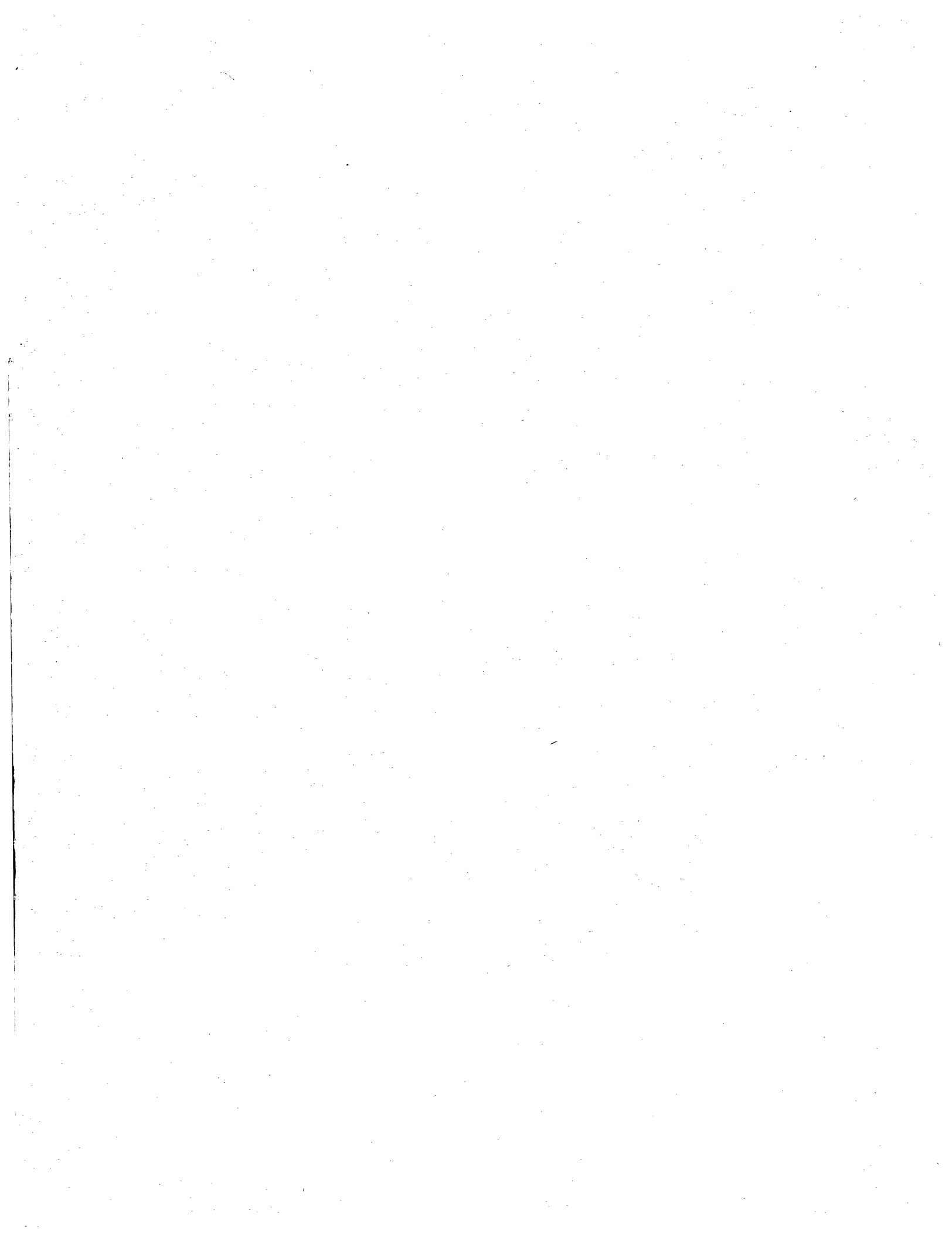
There was a loss of two quarters of "cross-match" input in the last half of 1973. The problem centered on communications between the Divisions of Unemployment and Disability Insurance and Administration. While no explanation exists, the problem has not reoccurred. "Cross-match" is the most important fraud detection device. The loss of two quarters of runs means the loss of thousands of leads for investigation.

Identified recipients of benefit overpayments had been flagged in a master file in the computer. This flag is set to signal that a person owing money to the Unemployment Trust Fund has applied for benefits again. This signal leads to withholding of newly earned benefits until the amount owed plus penalty and interest is fully reclaimed. A reprogramming omission in 1973 led eventually to the purging of all flags from the master file. The flags will be replaced in the reprogrammed system to appear in 1976. Presently claims are processed without this recovery device.

Agency Response

from

Hon. Joseph A. Hoffman
Commissioner of Labor and Industry





STATE OF NEW JERSEY
DEPARTMENT OF LABOR AND INDUSTRY
JOSEPH A. HOFFMAN, COMMISSIONER

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May 30, 1975

Mr. Gerald D. Silliphant, Director
Division of Program Analysis
New Jersey State Legislature
Office of Fiscal Affairs
State House, Suite 232
Trenton, New Jersey 08625

Dear Mr. Silliphant:

This is in response to your request that I review and provide you with my comments concerning the draft special program analysis on Unemployment Insurance Fraud Activity in the New Jersey Division of Unemployment and Disability Insurance.

The overall report commends the work of the Division and the Fraud Inspection Section for the work it is now doing. However, in a number of cases it speaks of the Fraud Inspection Section as a Bureau. Perhaps the use of the title "Bureau" should be explored further.

The report attempts to answer five questions.

1. Is the internal Fraud Detection Unit activity adequate?

I do not believe the persons who prepared the report really examined the adequacy of "internal fraud detection," but rather looked at the overall fraud detection operation. Nowhere in the report did I find anything that related literally to internal fraud. By this I mean that the fraud may be attempted or perpetrated by employees of the Division.

Merely following the recommendations of expanding the number of fraud investigators from 7 to 10 will not really solve the problems of the Fraud Inspection Section. The Supervisor of the Section has already requested an additional fraud investigator, but feels that if the fraud investigation complement were to be expanded to ten, the reorganization of the role and the functions of the Section should also be brought about. I agree with the Section Supervisor's thinking. As noted above, this would probably require Bureau status.

2. Is fraud prosecution adequate?

We are aware of the current policy with respect to standards for fraud prosecution. Unfortunately, there is a shortage of available legal talent to actually pursue any great volume of fraud cases in court. In addition, more Deputy Attorneys General should be assigned to prosecute fraud cases. Further consideration should be given to changing the current six week basis to some standard approaching the ten week basis.

The evaluators suggest an "administrative court." There is some doubt in my mind as to the value of a new bureaucracy such as an administrative court. However, I should be interested in getting further details of what the evaluator had in mind. If we are going to handle more fraud cases on an administrative priority basis, we will need additional staff to perform this function.

3. Are there undetectable fraud activities?

This area was covered effectively by the evaluator. Yet, we agree that less than one percent of all initial claims involved detected fraud. Certainly, our experience has shown that fraud only results in convictions in a very small percentage of cases.

4. Are there operational problems that may hinder fraud detection?

The impact of heavy claims loads and conversion to the computer system have been handicaps. The role of unmatched pay orders as a factor in fraud is unclear. The current method set up to minimize unmatched pay orders should be examined to determine its effectiveness. The problem of delay in fraud detection and documentation is a difficult one and should be carefully reviewed. It is obvious that with larger staffing, more work can be accomplished; provided, there is adequate supply of "straw bosses" and overall supervision.

5. Is fraud payout seriously affecting Unemployment Trust Fund stability?

We feel that the evaluator's judgment is correct in that the Unemployment Insurance Trust Fund stability is not affected to any significant extent by the incidence of fraud.

The report also covers broad aspects of the unemployment, disability, tax and benefit programs.

- a. It refers in some detail to the built-in evaluation system that is practiced by the State of New Jersey with respect to Local Office Claims Processes and Nonmonetary Determinations and other special programs administered by the Bureau of Unemployment and Disability Insurance Programs.
- b. It also reports on some of the limitations of our crossmatching system. We agree that as soon as possible all programs should be included in the computer and thereby become an integral part of the BOASI cross-matching system. This also applies to interstate claims.
- c. Return to Work Procedures

A point is made that there is no verification of return-to-work claims forms BC-260. At one time we did have a verification program which resulted in identification of many small dollar amounts of overpayments at a very high administrative cost. We could reinstitute a verification of back-to-work claims. However, this program would be expensive and again would probably result in a detection of a small amount of monetary errors. Much of this detection will be accomplished in the BOASI crossmatch under the existing system.
- d. The report suggests the use of warnings of administrative and maximum penalties for fraud to claimants. Such statements are frequently used now; such as, on initial claims, continued claims and agency informational pamphlets.
- e. Overall, we agree that as more benefits are paid, the probability of more cases of fraud does exist. This requires tighter systems and greater alertness on the part of our entire staff. The report recommends that the penalties for fraud be made more severe, such as, "permanent disqualification in the collection of benefits for the offender." I do not subscribe to such penalty. We do have severe penalties available for our use currently.
- f. Keeping benefit debts on our books permanently has been explored to make our records more realistic in terms of collectability of such debts. Follow-up action has been taken.
- g. (Omitted from final report)

Mr. Gerald D. Silliphant, Director
Division of Program Analysis

-4-

May 30, 1975

- h. I do agree with the suggestion that there be a more severe disqualification for gross misconduct. Such legislation at one time was introduced in the New Jersey Legislature.

I would suggest that the information provided above be discussed with the evaluation team to clarify their findings.

Sincerely,


COMMISSIONER

PROGRAM ANALYSES PUBLISHED BY THE OFFICE OF FISCAL AFFAIRS,
DIVISION OF PROGRAM ANALYSIS

- 73-1 Program Analysis of the New Jersey Educational Opportunity Fund, January, 1973
- 73-2 Program Analysis of Office Space for State Agencies, May, 1973
- 74-1 Program Analysis of Institutional Maintenance Support Payments, February, 1974, Volumes I and II and Summary
- 74-2 Program Analysis of the Southwestern New Jersey Bus Feeder Subsidy, February, 1974
- 74-3 Program Analysis of Financing and Construction of Dormitories and Student Centers via the Educational Facilities Authority, June, 1974
- 75-1 Program Analysis of the Administration of the New Jersey State Civil Service System, January, 1975
- 75-2 Program Analysis of The New Jersey Urban Renewal Assistance Program, March, 1975
- 75-3 Program Analysis of New Jersey's Seasonal Farm Labor Protection Programs, May, 1975
- 75-4 Program Analysis of The New Jersey State Building and Construction Program, June, 1975
- SPA-1 Special Program Analysis of Unemployment Insurance Fraud Detection and Control Activity in the New Jersey Division of Unemployment and Disability Insurance, August, 1975

New Jersey State Legislature
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