



United States Department of Agriculture

# Office of Inspector General





# State Agencies' Food Costs for Food and Nutrition Service's Special Supplemental Nutrition Program for Women, Infants, and Children

Audit Report 27004-0001-22

## What Were OIG's

### Objectives

Our overall audit objective was to evaluate the factors that contribute to high average food costs per participant, as reported for various States within the WIC program. We also evaluated FNS' oversight activities for monitoring food costs.

### What OIG Reviewed

We performed audit fieldwork at the national office, six of the seven regional offices, and eight State agencies. In addition, we conducted follow-up fieldwork at the Georgia State agency and FNS' Southeastern regional office to discuss corrective actions and implemented State controls particular to Georgia.

### What OIG Recommends

FNS needs to develop a national strategy to reduce food costs in the WIC program, including correcting issues identified in the States reviewed and ensuring broader implementation of policies to lower average food costs. FNS should also explore additional avenues for resolving issues in the States, including elevation to the appropriate officials.

## Although FNS has worked with State agencies to reduce food costs for the WIC program, FNS could take further steps to secure additional cost savings.

### What OIG Found

We found that FNS' current strategy for monitoring State agency's food costs does not ensure Federal resources are being used efficiently in the WIC program. Although FNS reports through the *Office of Management and Budget's A-133 Compliance Supplement* that management evaluations (ME) are the WIC program's main oversight tool, we found that the MEs themselves, and the ME process, have several weaknesses. For example, we found that the MEs did not always identify significant issues that may impact a State agency's food costs, and when FNS did identify deficiencies at State agencies, it did not always ensure that those agencies took appropriate and timely corrective actions. Finally, although FNS is aware of policies that various State agencies have implemented to reduce their food costs, it has not evaluated those policies for program-wide implementation. Not evaluating these policies and their cost saving implications has led to missed cost saving opportunities. By strengthening its strategy for monitoring food costs and considering program-wide implementation of proven cost containment measures, FNS could generate savings it could use to provide benefits to more participants and help further the program's mission.

OIG accepted management decision on four of the six report recommendations; however, further action from the agency is needed before management decision can be reached for the remaining recommendations.





United States Department of Agriculture  
Office of Inspector General  
Washington, D.C. 20250



DATE: September 25, 2014

AUDIT  
NUMBER: 27004-0001-22

TO: Audrey Rowe  
Administrator  
Food and Nutrition Service

ATTN: Mark Porter  
Director  
Office of Internal Controls, Audits and Investigations

FROM: Gil H. Harden  
Assistant Inspector General for Audit

SUBJECT: States' Food Costs for the Food and Nutrition Service's Special Supplemental  
Nutrition Program for Women, Infants, and Children

This report presents the results of the subject audit. Your written response to the official draft, dated September 17, 2014, is included in its entirety at the end of this report. Excerpts from your response and the Office of Inspector General's (OIG) position are incorporated into the relevant Finding and Recommendation sections of the report. Based on your written response, we are able to accept management decision on Recommendations 3, 4, 5, and 6. However, we are unable to accept management decision on Recommendations 1 and 2. Documentation or action needed to reach management decision for these recommendations are described under the relevant OIG Position sections.

In accordance with Departmental Regulation 1720-1, please furnish a reply within 60 days describing the corrective actions taken or planned, and timeframes for implementing the recommendations for which management decisions have not been reached. Please note that the regulation requires management decision to be reached on all recommendations within 6 months from report issuance, and final action to be taken within 1 year of each management decision to prevent being listed in the Department's annual Agency Financial Report. Please follow your internal agency procedures in forwarding final action correspondence to the Office of the Chief Financial Officer.

We appreciate the courtesies and cooperation extended to us by members of your staff during our audit fieldwork and subsequent discussions. This report contains publically available information and will be posted in its entirety to our website (<http://www.usda.gov/oig>) in the near future.



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## Background and Objectives

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### Background

The Food and Nutrition Service's (FNS) Special Supplemental Nutrition Program for Women, Infants, and Children (WIC) serves pregnant, postpartum and breastfeeding women, and infants and children up to age five. To be eligible for program benefits, applicants must meet income guidelines and State residency requirements, and be individually determined to be at nutritional risk<sup>1</sup> by a healthcare professional.

In fiscal year (FY) 2013, the WIC program served an average of 8.7 million participants per month, with food benefits totaling more than \$4.5 billion for the fiscal year. More than half (52.9 percent) of WIC participants in FY 2013 were children (ages 1-4), 23.5 percent were infants, and 23.6 percent were women. In FY 2012, for the first time, the proportion of breastfeeding women exceeded that of non-breastfeeding postpartum women. Among all WIC participants in FY 2012, 10.1 percent were pregnant women, 6.8 percent were breastfeeding women, and 6.7 percent were postpartum non-breastfeeding women.

According to FNS data, the average monthly food cost per participant was \$43.26 nationwide.<sup>2</sup> High variances occur between States with regard to food costs. For example, in FY 2013, the highest average monthly cost per participant was \$88.88 in Puerto Rico, compared to the lowest in Texas at \$26.47. As a comparison, New York had the highest food costs in FY 2013 amongst the 50 States and the District of Columbia at \$54.71.

FNS administers the program at the Federal level and provides funding to State health departments or comparable agencies to pay for supplemental foods, nutrition education, breastfeeding promotion and support, and administrative costs. Each State agency administering the program must sign a Federal/State agreement that commits it to observe applicable laws and regulations in carrying out the program. The State agencies in turn, award sub-grants to local agencies to certify applicants' eligibility for WIC program benefits and deliver such benefits to eligible persons.<sup>3</sup> The WIC program has 90 State agencies, which are made up of the 50 States, 34 tribal organizations, the District of Columbia, and 5 U.S. territories.

FNS has already implemented a variety of mandatory practices which have reduced costs nationwide in the WIC program. Examples include rebates on infant formula<sup>4</sup> and the grouping of vendors with similar characteristics to determine competitive price criteria for the redemption of food instruments. Competitive price criteria are computed by increasing the average

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<sup>1</sup> Two major types of nutritional risks are recognized for WIC eligibility: (1) Medically-based risks such as anemia, being underweight or overweight, or having a history of pregnancy complications or poor pregnancy outcomes; and (2) Dietary risks, such as inappropriate nutrition/feeding practices or failure to meet the current Dietary Guidelines.

<sup>2</sup> This number is calculated by taking the total food costs nationwide for the year, dividing it by the number of participants receiving services for the year and then dividing that number by 12 to account for the number of months within a year.

<sup>3</sup> *Office of Management and Budget (OMB) A-133 Compliance Supplement* (March 2013) 4-10.557-1 CFDA 10.557, Special Supplemental Nutrition Program for Women, Infants, and Children Section II Program Procedures.

<sup>4</sup> State agencies solicit bids from infant formula manufacturers to supply and provide a rebate for infant formulas.



redemption amount for each grouping of vendors by either a set percentage or number of standard deviations. This ensures that payments to vendors comply with the State agency's competitive price criteria. Generally, cost containment measures begin as a State agency initiative that is tested by trial and error. As specific measures become refined and employed by multiple State agencies, FNS begins to assist other State agencies in adapting them for use in their retail food delivery systems. When cost containment measures are adaptable to a majority of State agencies, FNS drafts legislative or regulatory proposals to require nationwide implementation, but the requirements usually have ample discretion to permit them to be applicable to most State agencies. Examples of other cost containment measures that are not currently required nationwide, but are being implemented in State agencies, are a policy that restricts foods redeemed to the least expensive brand and obtaining rebates contracts on non-infant formula items (such as infant cereal).

Another avenue for the reduction of food costs in the WIC program is coordination with Medicaid State programs to obtain reimbursements for exempt infant formula and medical foods when recipients are eligible to receive such products under both WIC and Medicaid. A memorandum sent in 2001 by FNS to the WIC State agencies stated that Medicaid is the primary payer of exempt infant formula and medical foods for mutual participants. However, Federal regulations only require that State agencies *coordinate* with the State Medicaid offices for program reimbursement of exempt infant formula and medical foods and do not specify which program will be the primary payer.<sup>5</sup> For example, some States have coordinated their WIC State programs and State Medicaid programs by enacting statutes specifying that WIC is the primary payer.

FNS' oversight of WIC encompasses a review of the program's nine functional areas: Organization and Management; Funding and Participation; Vendor Management; Information Systems; Certification, Eligibility, and Coordination; Nutrition Services; Civil Rights; Monitoring and Audits; and Food Delivery. According to FNS guidance, the management evaluation<sup>6</sup> (ME) is a significant component in FNS oversight activities and is the most critical tool for monitoring State agency program compliance and improving program operations. According to FNS officials, each year FNS regional office staff evaluate as many of these areas as possible, given available resources, focusing on those areas they consider to have the most need for review.

In May of 2012, staff with the U.S. House of Representatives, Committee on Appropriations, Subcommittee on Agriculture, Rural Development, Food and Drug Administration, and related agencies provided information to the Office of Inspector General (OIG) regarding food costs in the WIC program. Specifically, the information highlighted Georgia's high average food costs, as well as the great disparities in food costs nationwide. As a result, we began our work in Georgia. The results of the work done in Georgia led us to initiate an audit to further identify the factors that impact food costs in various States nationwide.

Our audit found that high food costs in Georgia were caused by deficient program management and an antiquated information system that lacked appropriate access controls, resulting in

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<sup>5</sup> 7 Code of Federal Regulations (CFR) § 246.10(e)(3)(vi).

<sup>6</sup> 7 CFR § 246.19.

potentially unreliable data. FNS completed MEs of Georgia for FYs 2008, 2010, and 2012 that identified several problems, including:

- Georgia did not consistently apply its vendor selection criteria and incorrectly assigned vendors to peer groups.<sup>7</sup> In addition, the State agency did not always identify vendors who derived more than 50 percent of annual revenue from WIC. This impacted food costs, as vendor peer groups are used to determine the maximum redemption amount the State agency will pay vendors for supplemental foods. This ongoing area of noncompliance resulted in estimated overpayments to vendors, totaling more than \$65 million in FY 2011 and nearly \$50 million in 2012.<sup>8</sup>
- After receiving notification that a vendor was disqualified from the Supplemental Nutritional Assistance Program (SNAP), Georgia took between 5 and 8 months to disqualify some vendors from WIC in FYs 2011 and 2012. In total, nine vendors were able to redeem \$1.8 million in WIC benefits after being disqualified from SNAP. Although the regulation<sup>9</sup> does not specify an exact timeframe for how soon the disqualification from WIC should occur, the 2012 ME stated that Georgia was not performing these disqualifications timely and notified the State agency that its corrective action plan must include procedures for ensuring WIC disqualification of vendors within 90 days of that vendor being disqualified from SNAP.

In a memorandum dated December 31, 2012, FNS imposed a moratorium on new vendors in the State of Georgia due to FNS concerns related to overpayments contributing to the state's high food costs. Since February 2013, the State has been unable to authorize any new vendors to participate in the WIC program, unless a vendor is needed for the participant's access. This moratorium was lifted on January 15, 2014, when the food and vendor management issues in the State were resolved to FNS' satisfaction. The December memorandum also notified the State agency of FNS' intent to establish a claim for \$19.8 million in estimated overpayments made between October 2010 and June 2012. FNS settled with the State for \$10.6 million in January 2014. Of this, Georgia will need to pay \$2 million in cash to FNS by 2018.<sup>10</sup>

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<sup>7</sup> A vendor peer group is a classification of authorized vendors based on common characteristics or criteria that affect food prices, for the purpose of applying appropriate competitive price criteria to vendors at authorization and limiting payments for food to competitive levels. Peer groups are defined by the State agency in their State Plan.

<sup>8</sup> FY 2011 Above 50 Percent Vendors - \$43,812,182 and Probable Above 50 Percent Vendors -\$21,342,045.

FY 2012 Probable Above 50 Percent Vendors - \$49,908,634.

<sup>9</sup> 7 CFR 246.12(l)(1)(vii) outlines the requirements with regard to SNAP disqualifications and the effect on WIC. This regulation provides that a State agency must disqualify a vendor who has been disqualified from SNAP. This regulation provides that a State agency must disqualify a vendor who has been disqualified from SNAP, and also that the WIC disqualification must be for the same length of time as the SNAP disqualification, may begin at a later date than the SNAP disqualification, and is not subject to administrative or judicial review under the WIC program.

<sup>10</sup> Georgia committed to use \$1.2 million to upgrade WIC program vendor integrity. However, FNS allowed Georgia to include the amounts spent for this purpose for the 2 years prior to the settlement and the remaining balance would need to be spent prior to September 30, 2018. FNS agreed to hold \$7.4 million at risk. If Georgia fulfills all performance measures set by FNS through September 30, 2019, then FNS will forgive the \$7.4 at risk amount. If it does not, Georgia must remit a \$7.4 million cash payment to FNS by December 30, 2019.

## **Objectives**

Our overall audit objective was to evaluate the factors that contribute to the high average food costs reported for various States within the WIC Program. We also evaluated FNS' oversight activities for monitoring food costs.

## Section 1: FNS Oversight

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### Finding 1: FNS Can Strengthen Its Oversight of State Agency Cost Containment Practices

FNS' current oversight strategy has been ineffective with regard to State food cost containment. Although FNS reports through the *OMB Circular A-133*<sup>11</sup> *Compliance Supplement* that MEs are the main oversight tool for the WIC program, we found that MEs themselves and the ME process have several weaknesses. For instance, MEs reviewed did not always identify significant issues that impact WIC food costs; and when MEs did identify deficiencies, FNS did not always take appropriate and timely corrective actions. According to FNS officials, this occurred because FNS used discretion permitted under program regulations to allow State agencies flexibility in managing WIC as partners, instead of issuing nationwide cost containment policies. In addition to addressing deficiencies found within the ME process, FNS needs to strengthen its oversight of State agency coordination with State Medicaid offices and provide tools for State agencies in their search for additional cost containment strategies. By strengthening its oversight of cost containment, FNS could generate savings that it could use to help further the program's mission of promoting healthy mothers and children.

OMB Circular A-123<sup>12</sup> states that management has a fundamental responsibility to develop and maintain effective internal controls for proper stewardship of Federal resources. Federal employees must also ensure that programs operate efficiently and effectively. As the Federal steward over the WIC funds, FNS is responsible for overseeing disbursements to State agencies.

Through OMB Circular A-133, *Compliance Supplement*, FNS reported that its oversight mechanism includes evaluating the program's nine functional areas,<sup>13</sup> focusing on those areas it considers most in need of review. This supplement also reflects that FNS reported that it has enforcement mechanisms through the assessment of a claim to recover losses. In addition, it states that FNS has the authority to notify States of issues identified, and if improvements do not occur, withhold administrative funds for not implementing program requirements. This same supplement shows that MEs are the main oversight tool for the WIC program. However, we found that MEs themselves and the ME process have several weaknesses.

#### ***Improvements are Needed to Ensure State Agency WIC Pricing Structures are Effective in Controlling Costs***

We found that MEs for two of eight State agencies reviewed did not identify policy violations. First, in Ohio, the State agency did not adhere to FNS guidance on obtaining an exemption from FNS to not use the required vendor peer group structure.<sup>14</sup> The State agency was setting prices Statewide, as opposed to separating vendors into different peer

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<sup>11</sup> OMB Circular A-133: Audits of States, Local Governments, and Non-Profit Organizations (Effective July 1, 1996).

<sup>12</sup> OMB Circular A-123: Management's Responsibility for Internal Control (effective beginning with FY 2006).

<sup>13</sup> Functional areas include: Organization and Management; Funding and Participation; Vendor Management; Information Systems; Certification, Eligibility, and Coordination; Nutrition Services; Civil Rights; Monitoring and Audits; and Food Delivery.

<sup>14</sup> 7 CFR 246.12 (g)(4)(ii).

groups and setting different pricing and reimbursement levels for each. FNS guidance explains that vendor categorization is important for controlling costs, as it allows State agencies to determine the appropriate maximum reimbursement levels for specific vendor types (i.e., small corner stores would have higher food costs than large chain grocery stores). Ohio's State agency said FNS' regional office knew about and consented to its pricing structure, even though it did not obtain a formal exemption. FNS provided no documentation that it had granted an exemption or reviewed the Ohio State agency's peer group structure. We notified FNS of the issue, and FNS officials agreed that they should have required an exemption. FNS is working with the State agency to review its system and prepare an application for a formal exemption. The review is especially important, as it will allow FNS to determine whether vendors in Ohio are able to charge higher prices than would be allowed under a peer grouping system.

Second, in Louisiana, we found the State agency set pricing for all vendor groups using outdated formulas that could not be justified or explained. FNS requires State agencies to create competitive pricing criteria for all vendors, based on sound statistical methods. This deficiency was identified only for above-50 percent of vendors during a ME conducted in FY 2011, but the State agency did not correct the problem. After we brought the issue to an FNS official's attention, they conducted a subsequent ME of Louisiana in FY 2013 and discovered that Louisiana had not set appropriate pricing levels for all vendors, and that the State's information system did not have controls in place to enforce proper reimbursement levels for all vendors. The State agency is taking corrective actions on this issue.

Both of these issues occurred because FNS does not assess or verify in their ME process the effectiveness of the State agency's pricing structure. The ME process only confirms that the State agency assesses its own pricing structure. Both Ohio and Louisiana detailed their improper price structures in their State plans. Annually, State agencies submit a plan for FNS approval that includes details of how they will implement WIC. These documents are very detailed, containing extensive figures, and often include hundreds of pages. While FNS does review and approve these documents, it did not identify the incorrect pricing structures in the submitted plans. By incorporating a more in-depth review of State pricing structures within the ME, FNS can create a control to ensure that pricing follows FNS guidance and demonstrates effective cost containment. This would serve as a more effective control to the approval process in ensuring these inadequate pricing structures do not continue.<sup>15</sup>

***Improvements are Needed to Ensure the WIC Program is Coordinating with Other Agencies to Provide Benefits to Mutual Participants and that Proven Cost Containment Strategies are Implemented More Broadly***

Although a Federal regulation requires coordination between WIC State agencies and, at minimum, Medicaid State offices for the provision of benefits to mutual participants, no

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<sup>15</sup> A previous OIG audit (Report 27601-0038-CH, *Vendor Management in the Food and Nutrition Service's Special Supplemental Nutrition Program for Women, Infants, and Children*, March 2013) recommended that FNS reassess the ME process and update guidance and the ME tool. FNS agreed to take these actions by December 31, 2014.

oversight reviews, including MEs, were designed to include any tests to evaluate such coordination efforts (see Finding 2). Also, no oversight review, including the ME process, had a mechanism for reviewers to note examples of cost saving best practices that other States may be able to learn from or implement. As a result, FNS was not taking steps to expand proven cost containment practices, such as policies requiring WIC recipients to purchase the least expensive brand for a particular product, and the expansion of negotiated rebates that some State agencies receive for non-formula food items (see Finding 3).

***Improvements are Needed to Ensure that Appropriate and Timely Corrective Actions are Taken to Resolve Program Violations Identified***

We identified two State agencies with issues that went unresolved for a number of years after they were first discovered in an ME. For instance, in 2008, FNS identified that the Georgia State agency did not effectively identify stores that derive more than 50 percent of their sales from the WIC program that resulted in overpayments to vendors. The finding was still unresolved in follow-up MEs completed for FYs 2010 and 2012. During this time, FNS officials said that the Georgia State agency had five directors and was assigned to report to different departments and secretaries. In December 2012, FNS took action by sending the State a letter that stated its intent to establish a claim for \$19.8 million in estimated overpayments made between October 2010 and June 2012, as well as initiating a moratorium<sup>16</sup> on approving new WIC vendors in the State. FNS and the State agency began a lengthy negotiation, which slowly worked its way up to the Georgia Governor and a Department of Agriculture Under Secretary for Food, Nutrition, and Consumer Services. In January 2014, FNS settled with the State for \$10.6 million and ended the moratorium. Of this, Georgia paid \$2 million in cash to FNS in April 2014.<sup>17</sup> Although some of the necessary improvements to its overall WIC vendor management system were designed and implemented more quickly by the State agency, the claim and its eventual settlement took 6 years to resolve.

Although a 2003 Government Accountability Office (GAO) report found that Puerto Rico's issuance of non-contract and exempt infant formula was the highest in the nation, FNS did not ensure that Puerto Rico is containing costs derived from issuing non-contract infant formula.<sup>18</sup> As recently as May 2013, an FNS review of Puerto Rico found

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<sup>16</sup> The moratorium is an additional administrative restriction on the State agency that is meant to prevent any new vendors from joining the program and allow for the State to correct all issues discovered in the ME.

<sup>17</sup> Georgia committed to using \$1.2 million to upgrade WIC program vendor integrity. However, FNS allowed Georgia to include the amounts spent for this purpose for the 2-years prior to the settlement with the remaining balance needing to be spent prior to September 30, 2018. FNS agreed to hold \$7.4 million at risk. If Georgia fulfills all performance measures set by FNS through September 30, 2019, then FNS will forgive the \$7.4 million at risk amount. If it does not, Georgia must remit a \$7.4 million cash payment to FNS by December 30, 2019.

<sup>18</sup> GAO-03-331, *Potential to Serve More WIC Infants by Reducing Formula Cost* (February 2003).

that the State agency was improperly issuing large amounts of non-contract and exempt infant formula<sup>19</sup> to participants. This issue was cited in a March 2012 review. Although Puerto Rico had informed FNS as early as December 2011 that non-contract formulas would not be authorized, it had not taken steps to ensure non-contract formula wasn't being issued. According to FNS, the State agency did not create policies prohibiting the issuance of non-contract infant formula until early 2013.<sup>20</sup> In addition, the Puerto Rico State plan for FY 2014 informed FNS that 39.73 percent of infant formula issued would be non-contract or exempt.

This is not the first time that OIG has reported on the ME process for WIC. In response to a 2013 OIG report<sup>21</sup> that identified other weaknesses in the ME process, FNS officials indicated they are revising the ME process in order to develop and identify a vision, oversight, and formalize collaborative approaches to secure an agency commitment for consistency in all program areas across the country.<sup>22</sup> FNS is currently working on this project and plans to finish in December 2014. In addition to the ME process changes, FNS told us it is also looking to hire a contractor to conduct a vendor risk assessment that will examine how State agencies currently implement peer group and cost containment systems to control costs, and how these may be improved. Finally, in January 2014, FNS told us that it created a new national Program Integrity Monitoring Branch that will be responsible for MEs and other duties, such as reporting. As of the date of our report, this branch is not yet operational.

In summary, FNS is not effectively containing or recouping costs, such as coordinating with Medicaid for the potential program reimbursement for exempt infant formula (see Finding 2), implementing policies that favor lowest-cost brands, and expanding the use of food rebates (see Finding 3). As to problems identified in MEs that FNS did not act on, in one State alone, FNS allowed a problem to continue that cost an estimated \$19.8 million in less than 2 years. The enforcement actions FNS reported to OMB through the compliance supplement, when utilized, should encourage States to comply with policies and, when properly utilized, should result in cost savings<sup>23</sup> as these issues would be less likely to reoccur.

In response to the areas of improvements needed in FNS oversight, FNS officials said that State agencies are partners, and, therefore, the prior strategy was to use the discretion allowed by program regulations to provide State agencies flexibility in managing their WIC operation to encourage cooperation. As a result, as FNS focused on partnership, we

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<sup>19</sup> “Non-contract brand formula” means all formula, including exempt formula, that is not covered by an infant formula cost containment contract awarded by the State agency. “Exempt formula” means infant formula that meets the requirements for exempt infant formula in 21 U.S.C. 350a (h) and the regulations at 21 CFR parts 106 and 107. Exempt infant formulas (and WIC-eligible medical foods) are authorized only in Food Package III with medical documentation.

<sup>20</sup> As of the date of this report, these policies have not been provided to OIG for verification.

<sup>21</sup> A previous OIG Audit (Report 27601-0038-CH, Vendor Management in the Food and Nutrition Service’s Special Supplemental Nutrition Program for Women, Infants, and Children, March 2013) recommended that FNS reassess the ME process and update guidance and the ME tool. FNS agreed to take these actions by December 31, 2014.

<sup>22</sup> FNS Management Evaluation Collaboration, page 2.

<sup>23</sup> Costs savings are explained in Exhibit A: Summary of Monetary Results.

conclude it placed less emphasis on its oversight role, and did not develop a national strategy to lower food costs. FNS officials acknowledged that they need to change their focus to fulfill more of an oversight role. The focus on partnership, as opposed to controlling the program as the national authority, has weakened FNS' position as an oversight agency.

In 2013, FNS conducted a nationwide survey of State agencies to get an understanding of cost containment practices. States noted several budget pressures in their responses. Most notably, New York said that it provided \$13.6 million in State funds to take care of anticipated WIC budget shortfalls.<sup>24</sup> If money remains in the WIC budget once all applicants are provided food benefits, the State agencies can utilize those funds to promote nutrition through supplemental activities like the issuance of breast pumps to participants who otherwise could not afford them. WIC's position is that breast milk is more nutritious than formula for infants and breast pumps allow low income mothers who may be returning to work to pump and provide breast milk to their children for a longer period of time, as opposed to switching to formula. New York, along with several other States such as Alabama, Kentucky, and Wisconsin, discontinued issuing breast pumps to participants due to the budgetary pressures noted in their responses to the survey. By strengthening its oversight of cost containment, FNS can generate savings that it can use to help further the program's mission of promoting healthy mothers and children.

## **Recommendation 1**

Develop a national cost containment strategy for the WIC program. This should include, at a minimum, guidance to State agencies on the deadlines to correct issues identified during ME reviews, and the enforcement actions FNS will take if the deadlines are missed.

## **Agency Response**

In its September 17, 2014, response FNS stated:

FNS has a national WIC cost containment strategy that requires State agencies to implement a vendor peer group system, competitive price criteria, and allowable reimbursement levels in a manner that ensures the WIC Program pays authorized vendors competitive prices for supplemental foods. It also requires State agencies to ensure vendors that derive more than 50 percent of their annual food sales revenue from WIC food instruments do not cause higher food costs for the program than do other vendors. All of these requirements are codified in program regulations (7 CFR 246.12). FNS also created a new WIC Program Integrity Monitoring Branch which is tasked with developing consistent tools, resources and solutions to program integrity challenges so that State agencies can correct issues identified in management evaluation (ME) reviews and other oversight reports. FNS is developing a system to analyze and use the findings

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<sup>24</sup> WIC is a discretionary program and therefore was impacted by the sequester as opposed to the entitlement programs whose funding is not tied to annual budget appropriations.



from the ME reviews and other data sources to identify State agencies with deficient vendor management practices and provide targeted Technical Assistance to address the findings.

### **OIG Position**

We are unable to reach management decision. FNS' proposed corrective action for this recommendation does not address necessary guidance to State agencies on the deadlines to correct those issues identified in ME reviews, and the enforcement actions FNS will take if the deadlines are missed. To achieve management decision, FNS should specify what actions it will take to ensure that these two items are addressed as part of its cost containment strategy.

## Section 2: WIC Coordination with Medicaid

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### **Finding 2: Improvements are Needed to Ensure the WIC Program is Coordinating with Other Agencies to Provide Benefits to Mutual Participants**

FNS has not effectively coordinated with the Department of Health and Human Services (HHS) to address the provision of exempt infant formula and WIC-eligible medical foods to mutual program participants and clarify what coordination means between WIC State agencies and Medicaid State offices. Federal regulation<sup>25</sup> requires that WIC State agencies coordinate, at a minimum, with Medicaid State offices for the provision of exempt infant formulas and WIC-eligible medical foods that are authorized or could be authorized under the State Medicaid program for reimbursement.<sup>26</sup> Such reimbursement from Medicaid to WIC applies to participants who are prescribed exempt infant formula and medical foods and who take part in both programs (hereafter referred to as mutual participants).

Prior to the issuance of the regulation requiring coordination between WIC State agencies and Medicaid State offices, on September 17, 2001, FNS had issued a memorandum (the “FNS Memorandum”) to FNS Supplemental Food Programs Regional Directors, advising that the Medicaid program would be the primary payer for these products that are issued to WIC participants who are also Medicaid beneficiaries. The FNS Memorandum states that it is applicable in States where the Medicaid office has elected to provide exempt infant formulas and WIC-eligible medical foods as part of their benefit packages. HHS’ Center for Medicaid and State Operations transmitted the FNS Memorandum to its Associate Regional Administrators on October 1, 2001. We found that, while the 2001 FNS Memorandum provided guidance that Medicaid State programs should be the primary payer for exempt infant formula and medical foods, the lack of regulations supporting such an obligation by Medicaid State programs to cover such products may have led to confusion amongst WIC State agencies as to what coordination with Medicaid should entail. For example, some State agencies have told us that they believe they have no authority to force Medicaid to coordinate with them at all, despite the existence of a regulation requiring coordination.

FNS officials stated they had approached HHS regarding coordination in the past year; however, they were unable to explain the delays in the required coordination efforts with their HHS counterparts, except to say that discussions with HHS were pending because HHS was focusing on the Affordable Care Act. Also, we noted FNS has not provided WIC State agencies with the technical guidance necessary to coordinate with their Medicaid counterparts. As a result, WIC State agencies are not consistently coordinating with Medicaid State offices, as required by regulation, which can result in missed cost saving opportunities.

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<sup>25</sup> 7 CFR § 246.10(e)(3)(vi).

<sup>26</sup> Medical foods are specially formulated and processed for a patient who is seriously ill or who requires use of the product as a major component of a disease or condition’s specific dietary management.

In our review of FNS' coordination efforts with Medicaid we requested information from 90 WIC State agencies. We received responses from 79 of the 90 State agencies. Thirty-four State agencies responded that they have agreements with their Medicaid counterparts for exempt infant formula and medical foods. Of these 34, two State agencies, Texas and Virginia, have agreements for direct program reimbursements where WIC provides the products to mutual participants and then bills Medicaid directly for the cost. In FY 2012, the Texas WIC State agency was directly reimbursed by the State Medicaid program for \$23.8 million (\$2.05 in monthly savings per participant) and the Virginia WIC State agency received \$8.3 million from the State Medicaid program (\$4.31 in monthly savings per participant). Another 17 State agencies reported that they coordinate with Medicaid to "refer" mutual participants, meaning that when a mutual participant needs these products as part of their nutrition prescription,<sup>27</sup> WIC State agencies will refer the participant to the State Medicaid office to obtain the products. An additional 12 State agencies reported that they coordinate with Medicaid, but WIC is the primary payer. The remaining 3 State agencies did not provide sufficient explanation of the terms of these agreements to indicate whether the agreement is for program reimbursement or referral, or whether the agreement specifies which entity is the primary payer.

Of the 45 State agencies reporting that they do not have agreements with their Medicaid counterparts:

- Eleven reported that Medicaid State offices had not been willing to coordinate with them.
- Five reported having discussions with Medicaid but have not yet reached any agreement.
- Twenty-nine reported not having an agreement with Medicaid, but did not provide sufficient explanation for why no agreement exists.

In following up with FNS national office officials, they stated that State agencies must coordinate more with Medicaid to establish agreements that will ensure (1) Medicaid is the primary payer for exempt infant formula and WIC-eligible medical foods, and (2) WIC should be reimbursed for costs associated with providing these products to mutual participants. They also informed OIG that they plan to reissue the FNS memorandum this year after discussing it with HHS to notify State agencies that Medicaid is the primary payer for those products that are authorized or could be authorized under the State Medicaid program for reimbursement. However, we again note that there is no regulatory requirement that Medicaid must be the primary payer, only that coordination take place.

## **Recommendation 2**

In collaboration with HHS, clarify what coordination between WIC State agencies and Medicaid State offices means with regard to the provision of exempt infant formula and WIC-eligible medical foods to mutual program participants. Record this clarification between HHS and FNS in an appropriate decision document.

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<sup>27</sup> WIC assigns benefits to participants based on the nutritional risks and needs of each participant based on the determination of a physician, nutritionist, or nurse. WIC refers to the benefit as a nutrition prescription.

## **Agency Response**

FNS will consult with HHS on the provision of exempt infant formulas and WIC-eligible medical foods to mutual program participants. Following these discussions, FNS will update and reissue the policy memorandum to provide guidance to WIC State agencies about coordination with Medicaid on the provision of exempt infant formulas and WIC-eligible medical foods to mutual program participants, including information on primary payer for these products.

## **OIG Position**

We are unable to reach management decision for this recommendation. While FNS' proposed corrective action addresses the need for FNS to consult with HHS, we cannot accept management decision solely based on the reissuance of the policy memorandum to WIC State agencies. To reach management decision, FNS should record the results of the coordination efforts between HHS and FNS in the appropriate decision document. This document should include specific elements, such as the responsibilities of each office for coordination, as well as the conditions in which each party has the responsibility of primary payer for the provision of exempt infant formulas and WIC-eligible medical foods to mutual program participants.

## **Recommendation 3**

Provide technical assistance to WIC State agencies to assist in their coordination efforts, including sharing best practices from WIC State agencies that have successfully coordinated with Medicaid for the provision of exempt infant formula and WIC-eligible medical foods.

## **Agency Response**

In its September 17, 2014, response FNS stated:

FNS has initiated work on technical assistance for WIC State agencies that will assist in their coordination efforts with Medicaid. In January 2014, FNS held discussions with WIC State agencies that have successfully coordinated with Medicaid for reimbursement of exempt infant formulas and WIC-eligible medical foods to obtain useful tips and lessons learned from their coordination efforts. FNS plans to continue similar discussions with WIC State agencies that have successfully coordinated with Medicaid using a referral process, such that mutual participants are referred to Medicaid for the provision of these products. The information obtained from State discussions will form the basis of technical assistance provided to all WIC State agencies. The discussions with HHS will also help inform technical assistance.

FNS provided an estimated completion date of September 30, 2015, for these actions.

## **OIG Position**

We accept FNS' management decision on this recommendation.

## Section 3: WIC Food Cost Containment Policies

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### **Finding 3: FNS Has Not Taken Effective Steps to Expand Cost Containment Measures Used Effectively by Some State Agencies**

Although some WIC State agencies' policies have been shown to decrease costs in the States where implemented, the FNS national office has not yet undertaken steps to evaluate and potentially expand these initiatives throughout the nation. FNS officials stated they need additional analysis to mitigate concerns that implementing these measures will cause some participants to avoid buying an item, which could affect the nutritional aspect of the program. We note that 42 of the 79 State agencies that responded to the OIG survey have some kind of least expensive brand policy in place and 16 have contracted for rebates on infant cereal, baby food, or both while still nutritionally serving their participants. For example, Texas has a least expensive brand policy and a rebate contract on infant cereal that contributes to its success of having one of the lowest costs per participant in the nation in FYs 2012 and 2013. By not making greater use of these practices, State agencies may incur higher food costs, potentially reducing available funding to serve more eligible participants.

OMB Circular A-123 states that proper stewardship of Federal resources is an essential responsibility of agency managers and staff. Federal employees must ensure that programs operate and Federal resources are used efficiently and effectively to achieve desired objectives. FNS' FY 2013 Strategic Priorities states that "promoting access to nutrition assistance program goes hand-in-hand with managing them in a manner that ensures public confidence and maximizes the impact of the Federal investment."<sup>28</sup>

During our review we found that State agencies have implemented other cost containment measures that can provide additional savings to WIC if implemented in more States. We discuss two of these cost containment measures, least expensive brand and obtaining rebates on other food items, in the subsequent sections.

#### ***FNS Has Not Taken Effective Steps to Analyze and Expand the Least Expensive Brand Policies***

State agencies provided different reasons for not having the least expensive brand policy in place. Some responded saying they had policies requiring that participants purchase only generic or store brands, which are normally cheaper than national brands. The State agencies believed this practice is easier for participants to comply with. Although limiting WIC purchases to in-store brands is a good alternative to the least expensive brand, such brands are more available at large box stores, rather than at smaller or local convenience stores, which often might carry only one or two brands for a particular product.

Some Indian Tribal Organizations that did not have least expensive brands stated that they had limited vendors or food options for their participants (i.e., a small store with

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<sup>28</sup> FNS FY 2013 Strategic Priorities, Increase Access to Nutritious Food, Improve Program Integrity.

only one brand available), making the least expensive brand unfeasible in their program. Other reasons that State agencies provided for not implementing the least expensive brands were that it causes participant confusion, is burdensome to participants and vendors, limits product variety, increases difficulty in compliance investigations, or would require updates to electronic systems and vendor equipment. While implementing least expensive brand policies will inevitably require additional compliance activities from the State agencies, we note that Texas' policy places the bulk of the burden of implementation on vendors, yet is still carried out Statewide. Congress has mandated that all WIC State agencies use electronic benefit transfer (EBT) systems by 2020, which means that information technology upgrades that would aid in implementing the least expensive brand policy will soon be underway.

### ***FNS Has Not Taken Effective Steps to Analyze and Expand Rebate Use Among State Agencies***

To further understand the use of rebates, we surveyed all 90 State agencies and asked whether they received rebates on foods other than infant formula. Four did not have retail food delivery systems, and another eight were in our original sample. Of the remaining 78, 10 agencies reported rebate amounts of an estimated \$3.9 million from foods other than infant formula in FY 2012. Three agencies reported they received rebates, but did not report the amount. A total of 54 did not receive rebates from other foods and 11 did not respond to the question.

Three of the eight States in our sample had rebate programs that led to significant savings. For FY 2012, Texas received \$1.68 million from infant cereal rebates that it negotiated with a manufacturing company (\$0.14 in monthly savings per participant); Ohio has two contracts for rebates and received \$501,736 from infant cereal (\$0.15) and \$2,459,805 from baby food (\$0.74); and New York received \$2,403,586 from infant cereal rebates (\$0.38). The other five State agencies did not have rebate contracts for any foods other than infant formula.

Because FNS aims to give States flexibility in operating their programs, FNS officials stated they do not have a policy requiring State agencies to negotiate rebates for non-formula foods. In a prior GAO report, FNS also said that the rebate contracts must undergo the State procurement process and set up monitoring redemptions, billings, and collections, which can be cumbersome and might cause an undue burden on those who run the WIC program.<sup>29</sup> Some State agencies that had not implemented rebates pointed out that their paper coupon systems would require them to issue separate checks for rebate items vs. non-rebate items, and then count the number of rebate checks redeemed—which would pose administrative costs. They also said that for products made by a variety of manufacturers, it is often hard to get an effective rebate contract from the fragmented market.

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<sup>29</sup> GAO/RCED-97-225, *A Variety of Practices May Lower the Costs of WIC*, September 1997, page 6.

FNS officials are aware of WIC State agencies cost containment policies such as least expensive brand policies and rebates contracts; however, they have not taken steps to potentially expand these policies nationwide. Exploring these options will help FNS better meet its strategic priorities and maximize the impact of Federal funding. FNS officials have concerns that implementing some of these cost containment measures will adversely impact participation rates contrary to the goal of the program. While we agree that nutrition is a priority, we also note that 42 State agencies determined that a least expensive brand policy and 16 State agencies determined that other rebates were appropriate cost containment measures. OIG acknowledges that, while additional cost containment measures may present implementation challenges, obtaining and analyzing available State agencies cost containment data and providing guidance to State agencies will aid in expanding additional measures in ways that States find appropriate to reduce costs.

#### **Recommendation 4**

Develop and issue guidance to State agencies for implementing the best cost containment practices available to reduce food costs.

#### **Agency Response**

In its September 17, 2014, response FNS stated:

FNS concurs with this recommendation. Guidance will be developed using existing State agency practices and will be made available to all State agencies.

FNS provided an estimated completion date of April 30, 2015, for this action.

#### **OIG Position**

We accept FNS' management decision on this recommendation.

#### **Recommendation 5**

Request that State agencies provide FNS with an analysis of implementing the available cost containment measures to reduce food costs.

#### **Agency Response**

In its September 17, 2014, response FNS stated:

FNS concurs with this recommendation. FNS will request State agencies submit an analysis of implementing available cost containment measures to reduce food costs.

FNS provided an estimated completion date of September 30, 2015, for this action.

## **OIG Position**

We accept FNS' management decision on this recommendation.

## **Recommendation 6**

Conduct a study that examines the methods of implementing various cost containment measures and their relative effectiveness.

## **Agency Response**

FNS concurs with this recommendation. FNS is working with ERS [Economic Research Service] on its update of the 2005 report, Interstate Variation in WIC Food Package Costs: The Role of Food Prices, Caseload Composition, and Cost-Containment Practices. This study will examine the degree to which food prices, caseloads, and the implementation of various cost containment measures influence in State agencies' food package costs.

FNS provided an estimated completion date of September 30, 2015, for this action.

## **OIG Position**

We accept FNS' management decision on this recommendation.



## Scope and Methodology

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We performed our audit fieldwork in FNS Headquarters in Alexandria, Virginia; FNS' Southeast and Southwest Regional Offices located in Atlanta, Georgia; Dallas, Texas; and eight WIC State agencies located in California, Georgia, Kentucky, Louisiana, Texas, Ohio, New York, and Puerto Rico. We also conducted interviews with program officials in four other regional offices. FY 2012 WIC funding for these eight States totaled \$2,239,863,233. The scope of this review covered the State's Food Costs for the WIC Program.

We judgmentally selected the eight State offices, based primarily on reported high average monthly food cost per participant for FY 2012, and, secondarily, on the method used for gathering data monthly for review and use of rebates. Also, some States were selected based on congressional interest or past concerns reported within the WIC Program. Identification of these judgmental factors by State follows (listed in alphabetical order):

- **California** - California had the highest total food costs of all 90 State agencies for FY 2012. California has been subject to a moratorium on authorizing new vendors in the past, and has a history of FNS concerns with its WIC program. The State uses paper food instruments.
- **Georgia** - We selected Georgia due to Congressional interest in its high food costs. Georgia had the highest food cost per participant of the 50 States and the District of Columbia.
- **Kentucky** - Kentucky had the lowest average monthly food costs per participant in the Southeast region. The State uses an EBT on-line system, which means the State receives transactional data in real time.
- **Louisiana** - Louisiana had the highest average monthly food costs per participant of all the States, not including the Indian Tribal Organizations, in the Southwest region. The State uses paper food instruments.
- **New York** - New York had the highest average monthly food costs per participant of all of the States, not including Indian Tribal Organizations, in the Northeast region. The State uses paper food instruments.
- **Ohio** - Ohio had the lowest average monthly food costs per participant in the Midwest region. Ohio made extensive use of rebates on other food items. Ohio uses paper food instruments.
- **Puerto Rico** - Puerto Rico had the second highest average monthly food costs per participant of all 90 State agencies, including the Indian Tribal Organizations. OIG received reports of vendor fraud and overcharging of participants, as well as a high number of authorized vendors who derive more than 50 percent of their business from WIC. These vendors account for over 80 percent of WIC redemptions. Puerto Rico uses paper food instruments.
- **Texas** - Texas had the lowest average monthly food costs per participant in the nation. The State uses an EBT off-line system, which means they gather data on a daily basis, but transactions are not monitored in real time.

To accomplish our objectives, we conducted interviews with agency officials and gathered and analyzed documents within FNS' Headquarters, regional offices, and States selected for review. At FNS Headquarters, we:

- Determined the cost factors used in determining each State's food costs per participant and average food costs.
- Gained an understanding of FNS' oversight responsibilities.
- Obtained and reviewed WIC funding levels for FYs 2010 to 2012.
- Identified State agencies that experienced food cost problems since FY 2010 and MEs conducted since FY 2010.
- Reviewed ME reports and correspondence between FNS and State agencies concerning WIC program operations in States.
- Gained an understanding of the integrity profile database of vendors, which keeps track of high-risk vendors.
- Obtained data and supporting documentation on the factors that influence food costs for each State we selected for review.

At the FNS regional offices, we:

- Conducted fieldwork at FNS' Southeast and Southwest Regional Offices.
- Interviewed officials at four other regional offices by conference call. We discussed possible deficiencies and potential recommendations for FNS' oversight of WIC food costs.
- Conducted follow-up fieldwork at the Southeast regional office in order to discuss corrective actions in Georgia.
- Developed and distributed a State questionnaire with various questions relating to cost containment procedures and policies.
- Evaluated oversight activities for monitoring food costs.
- Obtained the status of EBT implementation milestones for States that have yet to implement EBT.

At the eight State agencies, we:

- Conducted interviews with officials responsible for the WIC program.
- Reviewed State rebate reports for October 2009 through April 2013.
- Interviewed staff that select and create food instruments.
- Obtained and analyzed procedures related to high risk vendors.
- Discussed the vendor peer group system, competitive price criteria, and setting maximum allowable reimbursement levels for each peer group. Evaluated the process for setting competitive price criteria for each vendor peer group.
- Identified measures State agencies take for competitive pricing structures, and evaluated the appropriateness of the measures.
- Obtained redemption totals for FYs 2011, 2012, and 2013 for each group of vendors.
- Reviewed cost containment measures and MEs.

- Met with officials and obtained and analyzed information regarding investigations, in order to determine their impact on food costs.
- Determined how State officials set the maximum allowable reimbursement levels.
- Distributed WIC questionnaires that included questions on State cost containment measures.
- Obtained and reviewed the structure and controls of each State's Management Information Systems.
- For those States that have implemented EBT (Texas and Kentucky), we obtained and reviewed EBT procedures and policies, and reviewed transactions on-line.
- Obtained, reviewed, and analyzed the procedures for establishing peer groups and food prices, cost containment measures, controls over high-risk vendors and above 50-percent vendors, and the potential impact of fraud and investigations.

We conducted this audit in accordance with generally accepted government auditing standards. These standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions.

## Abbreviations

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|           |   |
|-----------|---|
| CFR.....  | Code of Federal Regulations   |
| EBT.....  | Electronic Benefit Transfer   |
| FNS.....  | Food and Nutrition Service  |
| FY.....   | Fiscal Year   |
| GAO.....  | Government Accountability Office  |
| HHS.....  | Department of Health and Human Services                                 |
| ME.....   | Management Evaluation   |
| OIG.....  | Office of Inspector General   |
| OMB.....  | Office of Management and Budget   |
| SNAP..... | Supplemental Nutritional Assistance Program                             |
| WIC.....  | Special Supplemental Nutrition Program for Women, Infants, and Children |

## Exhibit A: Summary of Monetary Results

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The table below shows the amount the agency should save once the OIG recommendations are implemented.

| Finding Number | Description  | Amount       | Category  |
|----------------|--|--------------|---|
| 1              | Savings to be realized from the implementation of the recommended improvements to the ME process.  | \$19,789,789 | Funds to be put to Better Use - Management or Operating Improvement Savings <sup>30</sup> |
| 1              | The difference between FNS's calculated overpayments as a result of identified issues in the State of Georgia and the settlement amount. | \$9,189,789  | Questioned Costs-No Recovery <sup>31</sup>  |

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<sup>30</sup> As stated in the Finding, implementing the recommendation for this Finding should save the agency this type of expense in the future.

<sup>31</sup> As the settlement should result in a return of \$10.6 million in estimated remuneration, the remaining \$9,189,789 million was not recovered by the agency. However, we are not recommending recovery of this amount as the settlement was agreed to by both parties and adjudicated.

## **Exhibit B: FY 2012 Food Costs for Three Sampled State Agencies that Had Rebates from Foods Other than Infant Formula**

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The table below shows the average monthly amounts per participant that three sampled State agencies received through rebates for infant formula to compare to the amount they received through rebates for infant cereal and baby food.

| <b>State Agency (Rank)<sup>32</sup></b> | <b>Average Monthly Amounts per Participant</b> |                               |  |
|---|--|-------------------------------|--|
|   | <b>Net Food Cost</b>                           | <b>Infant Formula Rebates</b> | <b>Infant Cereal &amp; Baby Food Rebates</b> |
| Ohio (6)                                | \$36.02  | \$17.26                       | \$0.89                                       |
| New York (50)                           | \$55.02  | \$17.83                       | \$0.38                                       |
| Texas (1)                               | \$29.30  | \$16.97                       | \$0.14                                       |
| <b>Average For The three States</b>     | <b>\$37.96</b>                                 | <b>\$17.27</b>                | <b>\$0.33</b>                                |

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<sup>32</sup> Rank based on average monthly food costs per participant for the 50 States and the District of Columbia with 1 being the lowest and 90 being the highest.

## Exhibit C: FY 2012 Food Costs and Participation for 10 Surveyed State Agencies that Had Rebates from Foods Other than Infant Formula

The table below shows the average monthly amounts per participant that three sampled State agencies received through rebates for infant formula to compare to the amount they received for infant cereal and baby food.

| State Agency (Rank) <sup>33</sup> | Average Monthly Participation | Average Monthly Net Food Costs | Average Monthly per Participant |                        |                                   |
|-----------------------------------|-------------------------------|--------------------------------|---------------------------------|------------------------|-----------------------------------|
|                                   |                               |                                | Net Food Cost                   | Infant Formula Rebates | Infant Cereal & Baby Food Rebates |
| Massachusetts (18)                | 122,568                       | \$5,004,493                    | \$40.83                         | \$15.79                | \$0.70                            |
| Connecticut (45)                  | 56,584                        | \$2,952,917                    | \$52.19                         | \$13.53                | \$0.67                            |
| Maine (20)                        | 25,537                        | \$1,049,820                    | \$41.11                         | \$13.49                | \$0.63                            |
| Wisconsin (25)                    | 118,585                       | \$5,080,558                    | \$42.84                         | \$15.23                | \$0.60                            |
| New Hampshire (4)                 | 16,299                        | \$561,571                      | \$34.45                         | \$16.49                | \$0.59                            |
| West Virginia (29)                | 47,891                        | \$2,107,536                    | \$44.01                         | \$18.37                | \$0.27                            |
| Maryland (32)                     | 146,272                       | \$6,564,813                    | \$44.88                         | \$17.04                | \$0.27                            |
| District of Columbia (30)         | 16,474                        | \$725,202                      | \$44.02                         | \$24.36                | \$0.27                            |
| Delaware (19)                     | 22,214                        | \$907,440                      | \$40.85                         | \$18.38                | \$0.26                            |
| New Jersey (47)                   | 172,333                       | \$9,085,131                    | \$52.72                         | \$15.17                | \$0.26                            |
| <b>TOTAL</b>                      | <b>744,757</b>                | <b>\$34,039,481</b>            | <b>\$45.71</b>                  | <b>\$16.00</b>         | <b>\$0.44</b>                     |

<sup>33</sup> Rank based on average monthly food costs per participant for the 50 States and the District of Columbia with 1 being the lowest and 90 being the highest.

**USDA'S  
FOOD AND NUTRITION SERVICE  
RESPONSE TO AUDIT REPORT**







**United States  
Department of  
Agriculture**

Food and  
Nutrition  
Service

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Room 712

Alexandria, VA  
22302-1500

DATE: September 17, 2014

AUDIT  
NUMBER: 27004-0001-22

TO: Gil H. Harden  
Assistant Inspector General for Audit

FROM: /s/ <Jeffrey Tribiano> (for): Audrey Rowe  
Administrator  
Food and Nutrition Service

SUBJECT: States' Food Costs for the Food and Nutrition Service's Special  
Supplemental Nutrition Program for Women, Infants, and Children  
(WIC Program)

This letter responds to the official draft report, dated August 18, 2014, for audit report number 27004-0001-22, States' Food Costs for the Food and Nutrition Service's Special Supplemental Nutrition Program for Women, Infants, and Children (WIC Program). Specifically, the Food and Nutrition Service (FNS) is responding to the general content, Section 3: WIC Food Cost Containment Policies, and the six recommendations in the report.

**FNS General Response to the audit report:**

The success of the WIC Program is measured by the health outcomes of program participants. Food packages align with the Dietary Guidelines for Americans and infant feeding practice guidelines of the American Academy of Pediatrics. They provide supplemental foods designed to meet the special nutritional needs of low-income pregnant, breastfeeding, non-breastfeeding postpartum women, infants and children up to five years of age who are at nutritional risk. WIC participation has been associated with improved fetal development, reduced incidence of low birth weight and short gestation for infants, and with reduced incidence of anemia, and improved dietary intake for children and pregnant and postpartum women. Good stewardship of Federal funds should not be based solely on the costs of goods and services but on their value relative to their costs in achieving the Program's mission and goals.

FNS would like to highlight the WIC Program's long history as an effective and efficient government program. Since 1990, the Thrifty Food Plan food inflation has increased by 85%, while WIC average food package cost has increased by 49%. During fiscal year (FY) 2013, the Food and Nutrition Service (FNS) provided extensive technical assistance to State agencies to help them lower the WIC Program's food cost. As a result, State agencies have more cost-effective vendor peer groups, participants

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are purchasing more reasonably priced food items, and WIC rebates are higher and net food costs are lower. The FY 2013 average food package cost per participant (\$43.26) was 3.86% lower than the FY 2012 food package cost (\$45.00). Every year, FNS works with all 90 State agencies to ensure that sufficient funds are available to serve all eligible women, infants and children who seek program benefits and services.

### **FNS response to Section 3: WIC Food Cost Containment Policies**

**Finding 3: FNS Has Not Taken Effective Steps to Expand Cost Containment Measures Used Effectively by Some State Agencies**, does not acknowledge the steps FNS has taken to expand the use of cost containment practices to nearly all WIC State agencies. Over the past 30 years, FNS and State agencies have worked together to develop and implement a number of successful cost containment measures. During the 1980s and 1990s, State agencies implemented an infant formula rebate system that significantly reduces the need for annually appropriated Federal funds. During the 2000s, FNS promulgated new food delivery regulations to strengthen vendor selection and management, including a requirement for State agencies to limit the amounts they pay retail grocery stores for WIC foods based on their vendor peer group's prices. More recently, State agencies have been making administrative adjustments to their food packages and authorized food lists to ensure that participants purchase more reasonably priced food items. In response to a May 2013 survey conducted by FNS, all State agencies, except for two extremely small Indian Tribal Organizations (ITO) State agencies, reported implementing one or more administrative adjustments to their food packages or authorized food lists to reduce their food costs. A majority of State agencies have made at least four of the seven adjustments included in the survey.

In the first paragraph of this section, OIG states: "FNS officials stated they need additional analysis to mitigate concerns that implementing these measures will cause some participants to avoid buying an item, *which could affect the nutritional aspect of the program*. We note that 42 of the 79 State agencies that responded to the OIG survey have some kind of least expensive brand policy in place and 16 have contracted for rebates on infant cereal, baby food, or both *while still nutritionally serving their participants*."<sup>27</sup> For example, Texas has a least expensive brand policy and a rebate contract on infant cereal that *contributes to its success of having one of the lowest monthly average food costs per participant in the nation for FYs 2012 and 2013.*" (*emphasis added*). In response to FNS' May 2013 survey, several State agencies indicated they had to reverse adjustments made to their food lists when they determined that the much lower pick-up rates by participants of the food items (e.g., least expensive brand) undermined the nutritional goals of the WIC Program. If participants do not pick up food items, it reduces both the nutritional benefits and food costs of the WIC Program.

In the section **FNS Has Not Taken Effective Steps to Analyze and Expand the Least Expensive Brand Policies**, the OIG does not provide clear evidence that least expensive brand measures would be the most effective cost containment practice in all State agencies.

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FNS would like to clarify that: 1) There are significant differences in the retail grocery market and variety and availability of brands across the country; 2) The administrative costs of implementing least expensive brand measures in some State agencies may outweigh their food costs savings; and 3) State agencies may have already implemented the most efficient cost containment measures based on the capabilities of their management information systems, food instrument systems, and their retail grocery markets. FNS provides technical assistance to State agencies in implementing various administrative adjustments to authorized product lists, including: 1) Adding generic or store brands; 2) Eliminating national brands; 3) Reducing number of brands and/or flavors; 4) Limiting to lowest cost item; and 5) Limiting package size. The OIG's statement in the opening paragraph that, "42 of the 79 State agencies that responded to the OIG survey have some kind of least expensive brand policy in place," points to the success of FNS in expanding least expensive brand measures to a majority of State agencies.

In the final section included in Finding 3, **FNS Has Not Taken Effective Steps to Analyze and Expand Rebate Use Among State Agencies**, the OIG offers no support that expanding rebates on foods other than infant formula would provide "significant savings." In the opening paragraph of this section, the OIG states: "10 agencies reported rebate amounts of an estimated \$3.9 million from foods other than infant formula in FY 2012." Including the three State agencies in OIG's sample in the second paragraph, the total savings OIG found from rebates on foods other than infant formula was about \$11 million, which equates to about 0.2% savings in annual FY 2012 food costs. Since 1985, FNS has been working with State agencies on expanding rebates on foods other than infant formula with very little success. The administrative costs of procuring and maintaining these contracts often outweigh their savings. With limited competition among these foods, manufacturers have not extended some rebate contracts, have filed protests in response to bid solicitations, or have not met technical requirements. Some of the recent rebate bid solicitations on foods other than infant formula have resulted in cancellation due to numerous protests from manufacturers, State alliances falling apart, and lack of bids from manufacturers.

### **FNS response to the report's recommendations:**

#### **OIG Recommendation 1:**

Develop a national cost containment strategy for the Special Supplemental Nutrition Program for Women, Infants, and Children (WIC) program. This should include, at a minimum, guidance to State agencies on the deadlines to correct issues identified during management evaluations (ME) reviews, and the enforcement actions FNS will take if the deadlines are missed.

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**Food and Nutrition Service Response:**

FNS has a national WIC cost containment strategy that requires State agencies to implement a vendor peer group system, competitive price criteria, and allowable reimbursement levels in a manner that ensures the WIC Program pays authorized vendors competitive prices for supplemental foods. It also requires State agencies to ensure vendors that derive more than 50 percent of their annual food sales revenue from WIC food instruments do not cause higher food costs for the program than do other vendors. All of these requirements are codified in program regulations (7 CFR 246.12). FNS also created a new WIC Program Integrity Monitoring Branch which is tasked with developing consistent tools, resources and solutions to program integrity challenges so that State agencies can correct issues identified in management evaluation (ME) reviews and other oversight reports. FNS is developing a system to analyze and use the findings from the ME reviews and other data sources to identify State agencies with deficient vendor management practices and provide targeted Technical Assistance to address the findings.

**Estimated Completion Date:** June 30, 2015

**OIG Recommendation 2:**

In collaboration with the Department of Health and Human Services (HHS), clarify what coordination between WIC State agencies and Medicaid State offices means with regard to the provision of exempt infant formula and WIC-eligible medical foods to mutual program participants. Record this clarification between HHS and FNS in an appropriate decision document.

**Food and Nutrition Service Response:**

FNS will consult with HHS on the provision of exempt infant formulas and WIC-eligible medical foods to mutual program participants. The intent of the discussions will be to learn whether the basis for WIC Policy Memorandum #2001-6, Medicaid Primary Payor for Exempt Infant Formulas and Medical Foods, remains valid, and to gain a better understanding of how State WIC and Medicaid Programs can interact. Following discussions with HHS, which are targeted for completion by December 2014, FNS will update and reissue the policy memorandum to provide guidance to WIC State agencies about coordination with Medicaid on the provision of exempt infant formulas and WIC-eligible medical foods to mutual program participants, including information on primary payer for these products.

**Estimated Completion Date:** June 30, 2015

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**OIG Recommendation 3:**

Provide technical assistance to WIC State agencies to assist in their coordination efforts, including sharing best practices from WIC State agencies that have successfully coordinated with Medicaid for the provision of exempt infant formula and WIC-eligible medical foods.

**Food and Nutrition Service Response:**

FNS has initiated work on technical assistance for WIC State agencies that will assist in their coordination efforts with Medicaid. In January 2014, FNS held discussions with WIC State agencies that have successfully coordinated with Medicaid for reimbursement of exempt infant formulas and WIC-eligible medical foods to obtain useful tips and lessons learned from their coordination efforts. FNS plans to continue similar discussions with WIC State agencies that have successfully coordinated with Medicaid using a referral process, such that mutual participants are referred to Medicaid for the provision of these products. The information obtained from State discussions will form the basis of technical assistance provided to all WIC State agencies. The discussions with HHS will also help inform technical assistance.

**Estimated Completion Date:** September 30, 2015

**OIG Recommendation 4:**

Develop and issue guidance to State agencies for implementing the best cost containment practices available to reduce food costs.

**Food and Nutrition Service Response:**

FNS concurs with this recommendation. Guidance will be developed using existing State agency practices and will be made available to all State agencies.

**Estimated Completion Date:** April 30, 2015

**OIG Recommendation 5:**

Request that State agencies provide FNS with an analysis of implementing the available cost containment measures to reduce food costs.

**Food and Nutrition Service Response:**

FNS concurs with this recommendation. FNS will request State agencies submit an analysis of implementing available cost containment measures to reduce food costs.

**Estimated Completion Date:** September 30, 2015

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**OIG Recommendation 6:**

Conduct a study that examines the methods of implementing various cost containment measures and their relative effectiveness.

**Food and Nutrition Service Response:**

FNS concurs with this recommendation. In addition to FNS studies, we rely on the USDA Economic Research Service (ERS) for current program research. In response to this OIG recommendation, FNS is working with ERS on its update of the 2005 report, *Interstate Variation in WIC Food Package Costs: The Role of Food Prices, Caseload Composition, and Cost-Containment Practices*. This study will examine the degree to which food prices, caseloads, and the implementation of various cost containment measures influence in State agencies' food package costs.

**Estimated Completion Date:** September 30, 2015

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