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Jane Duffield
Chief
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RE: *Comments for the Proposed Rule by the Department of Agriculture, Food and Nutrition Service, to 7 CFR 271 and 274 - Supplemental Nutrition Assistance Program: Trafficking Controls and Fraud Investigations (RIN 0584-AE26)*

Dear Ms. Duffield:

The New York City (NYC) Human Resources Administration (HRA) supports the efforts of the U.S. Department of Agriculture's Food and Nutrition Service's (FNS) proposed rule to increase program integrity efforts against fraud, waste, and abuse in the Electronic Benefit Tracking (EBT) system. However, we are concerned that the FNS missed the opportunity to address the EBT system's most common vulnerability; retailer fraud. Although the proposed rule provides states with the opportunity to more closely monitor potential fraud and abuse within the EBT system by recipients, it fails to address concerns about retailer fraud. Retailer fraud is one of the Supplemental Nutrition Assistance Program's (SNAP) major program integrity vulnerabilities.

New York City has made significant strides in increasing SNAP program participation and is working to assure program integrity. We take our responsibility to properly administer a program that provides benefits to over 1.8 million residents seriously. The federal investment in benefits and the City's investment in administering the program need to be properly protected.

Over \$3.3 billion per year in SNAP benefits reach New York City residents each year.¹ New York City contributes more than \$626 million annually to administer the Supplemental Nutritional Assistance and the number of recipients rose by more than 700,000 in a four year period. Although the City's program has experienced significant increases in applicants, we remain vigilant in our mission to provide timely benefits to all eligible clients. Over the last five years, HRA took action to make a more efficient

¹ "In April 2008 almost twenty-eight million Americans participated in the SNAP program. By July 2011 participation had reached a record forty-five million, or approximately one in seven Americans." Dan Lesser, *An Emerging Issue in the Supplemental Nutrition Assistance Program Should Be Participants Be Subject to New Identification Requirements?*, 45 CLEARINGHOUSE REV. 290, 291 (Dec. 2011); HRA Facts April 2012, http://www.nyc.gov/html/hra/downloads/pdf/statistics/hra_facts/hrafacts_2012/hra_facts_2012_04.pdf.

process for determining eligibility, issuing referrals for replacement EBT cards, and maintaining the integrity of the program.²

I. We Support the Efforts to Provide States and Localities with More Flexibility in Addressing Multiple Card Replacement Request

As expected, recipient card loss can be a significant issue for the individuals who lose them (because FNS rules do not permit replacement of card balances pending at the time the card is lost) but it also creates an administrative burden in arranging replacements. HRA, as one of the largest SNAP programs in the country, experienced this issue and as a means of reducing traffic inside our regular local centers, created a separate office specifically for replacement card referral. (In New York, counties administer the program, but the State is responsible for actually issuing EBT card and benefits.) Working with the State of New York, we recently created centralized replacement card centers for two of our larger boroughs (Brooklyn and Queens), which issue referrals for up to 9,000 replacement cards per month at each location.³ A similar process is now underway in several of our Bronx offices and by the end of August 2012, this process will expand citywide.

We appreciate the additional flexibility the proposed rule will provide states and local programs in handling multiple replacement cards. The proposed rule provides a method for New York City and OTDA to replace EBT cards because its process can focus on identifying three types of clients: (a) client populations who frequently lose EBT cards—homeless, disabled, and others—(b) clients who need more training to effectively use their EBT cards, and (c) clients using the benefits fraudulently. Existing FNS rules make investigation of card loss through direct contact with recipients extremely difficult.

Enabling agencies to look at circumstances surrounding client populations who frequently lose cards will help find vulnerable clients who need better access to their benefits or help managing their SNAP cases. This small change to the rule will present our agency with the opportunity to continue enhancing and streamlining its application and eligibility determination processes in its centers to provide timely benefits.

II. Prior to Issuing the Final Rules, Further Clarification Should be Provided Regarding the Analysis Used to Determine the Four Card Threshold

We believe that it is important for FNS to share its analysis of how they determined the threshold of 4 replacement cards as stated in the rule, “analysis by FNS of electronic transaction data that demonstrates a statistically significant difference when a

² *Id.*

³ *Id.* at 2.

client reaches his or her fourth replacement card, indicating that the transaction activity is three times more likely to be flagged as potential trafficking. . . .”⁴ This information would be particularly helpful to identify what other recipient variables were included. HRA has a strong background in the use of data analytics that we have used to identify both client and provider fraud not only in our SNAP program but with our Medicaid program that serves over 3 million recipients. The opportunity for HRA and other jurisdictions with long-standing experience in data analytics to review and add to the EBT analysis could be of benefit to FNS’s efforts.

III. The Proposed Rule Should Address Retailer Fraud and Network Trafficking

The proposed rule fails to address a major vulnerability remaining in EBT fraud: networks of both retailers and recipients engaging in trafficking. EBT cards work in the same way as a debit card, requiring either swiping the card through a point-of-sale machine and entering a PIN to authorize a food purchase, or keying entry by hand. “The point-of-sale machine deducts the purchase amount from the household’s monthly SNAP allotment and creates an electronic record of the purchase amount, date, and time.”⁵ The USDA implemented the EBT system specifically to address fraud, waste, and abuse, and it successfully lowered payment error rate estimates to approximately four percent.⁶ However, in a program that is nationally over \$700 billion a year, this small percentage still represents more than \$3 billion a year in overpayments.

The most common fraud schemes involve retailers allowing EBT cardholders to swipe the cards without purchasing SNAP approved items. The retailer rings in a transaction, but the cardholder (or the individual who has obtained the card and PIN from the actual recipient) receives a discounted amount in cash. The retailer’s willingness to convert benefits to cash becomes known and creates a fraud opportunity and a fraud magnet for networks of card traffickers and card aggregators.

In June 2012, a Kingston, NY retailer received four-to-twelve years for SNAP fraud.⁷ Kanwarjit Singh, a gas station and convenience store owner, received \$235,000 for allowing more than 100 customers to repeatedly charge “for example, \$200 to their benefit card. The customer would be given \$100 in cash—which they’d typically use to purchase alcohol, drugs or tobacco. . . .”⁸ Singh or his night clerk pocketed the other

⁴ Supplemental Nutrition Assistance Program: Trafficking Controls and Fraud Investigations, 77 Fed. Reg. 31738 (proposed May 30, 2012) (to be codified at 7 C.F.R. 271 and 274).

⁵ Lesser, supra note 3, at 291.

⁶ U.S. GOV’T ACCOUNTABILITY OFFICE, GAO-10-956T, SUPPLEMENTAL NUTRITION ASSISTANCE PROGRAM: PAYMENT ERRORS AND TRAFFICKING HAVE DECLINED, BUT CHALLENGES REMAIN (2010) [hereinafter GAO REPORT 2010], <http://www.gao.gov/new.items/d10956t.pdf>.

⁷ Michael Novinson, *Judge Comes Down Hard*, Times Herald-Record, June 8, 2012 (Kingston, N.Y.), available at <http://www.recordonline.com/apps/pbcs.dll/article?AID=/20120609/NEWS/206090327>.

⁸ *Id.*

\$100. The report also alleges his counsel tried to negotiate a lesser sentence in exchange for information to “bring down low-level participants.”⁹ Since his store had become the known SNAP trafficking center in Kingston, he had knowledge of hundreds of recipients who had traded their benefits for cash. The identified retailer who takes advantage of a vulnerable customer population and the EBT system creates an electronic trail of transactions that can be systematically data mined for the characteristics of retailers, customers, and transactions that distinguish them from legitimate transactions. If FNS’ study was rigorous and thorough, it could provide useful techniques for identification of other retailers and networks.

Clarify Trafficking Definition Includes Both Recipients and Retailers

The clarified definition of trafficking is very helpful in its addition of the intent to sell and inclusion of on-line purchases. However, as the definition expands we believe it is important to make clear and specify that trafficking encompasses both the actions of individuals and/or retailers. This is an important clarification as most fraud in the post-EBT world cannot be completed without the involvement of a retailer who has been identified by the recipient or trafficker as a willing participant in the scheme. These retailers create an environment where fraud can flourish, and obtain far greater benefits (untaxed income equal to 50% or more of the face value of the benefits) than the recipients (who exchange benefits to which they are entitled for a substantially smaller amount of cash).

The Proposed Regulation Should Place a Focus on Specific Retailers Primarily Engaged in Trafficking

In December 2011, Dan Lesser, Director of the Economic Justice Sargent Shriver National Center on Poverty Law, authored an article reviewing recent state efforts to increase recipient identification measures to weed out fraud, waste, and abuse in SNAP. These stores account for 71 percent of all registered retailers, and their transactions accounted for more than 1 dollar trafficked for every 8 benefit dollars redeemed. Using analyses provided by USDA, Mr. Lesser explained that “most trafficking now occurs directly between a small urban retailer and a SNAP recipient.”¹⁰ Mr. Lesser went on to explain:

Currently 87.3 percent of SNAP transactions occur in publicly owned, large supermarkets, but only 5.4 percent of trafficking occurs in these stores. Conversely 8.9 percent of SNAP benefits are redeemed in

⁹ *Id.*

¹⁰ Lesser, supra note 3, at 292.

privately owned, small convenience and grocery stores, but *these stores account for almost 80 percent of the SNAP dollars trafficked.*¹¹

Thus, although the volume of their transaction may be low in comparison to the larger retail/chain stores, according to USDA's own testing analysis, these smaller independent retailers are eight times more likely to be involved in trafficking. Back in 2000, FNS conducted 375 investigations of public corporations, and undercover investigators found trafficking in only four percent of the stores.¹² This, however, was not the case among privately owned food retailers, where trafficking was found in almost thirteen percent of stores.¹³

In 2006, a Government Accountability Office study noted that implementing the EBT system itself was not enough to stop retailer fraud. "Despite FNS progress, the program remains vulnerable because retailers can enter the program intending to traffic, often without fear of severe criminal penalties."¹⁴ The report went on to identify other weaknesses with FNS' approach, including a failure to conduct "analyses to identify high risk areas and to target its limited compliance-monitoring resources," citing retailer disqualification as an insufficient penalty for deterrence, and noting FNS' reliance on other agencies for prosecution.¹⁵

USDA Policies Should Support and Not Hinder States and Localities from Eliminating Retailer Fraud in the EBT System

According to a Government Accountability Office report in 2006, "USDA estimates suggest trafficking declined between 1995 and 2006 [implementation period for EBT] from 3.8 cents per dollar of benefits redeemed to 1.0 cent, resulting in an estimated \$241 million in food stamps trafficked in 2005."¹⁶ The USDA currently estimates there is a 4.36 percent payment error rate in SNAP, a number that includes "payments

¹¹ *Id.* at 294 (citing Office of Research & Analysis, U.S. FOOD & NUTRITION SERVICE, U.S. DEP'T OF AG., THE EXTENT OF TRAFFICKING IN THE SUPPLEMENTAL NUTRITION ASSISTANCE PROGRAM: 2006-2008, at 11 (Mar. 2011), <http://www.fns.usda.gov/ora/menu/published/SNAP/FILES/ProgramIntegrity/Trafficking2006.pdf>) (emphasis added).

¹² *Food Stamp Fraud: Why Trafficking Persists and What Can Be Done About It: Hearing Before the Task Force On Welfare of the Comm. on the Budget*, 106th Cong. 15 (2000) (statement of Shirley Watkins, Undersecretary for Food, Nutrition, and Consumer Services).

¹³ *Id.*

¹⁴ U.S. GOV'T ACCOUNTABILITY OFFICE, GAO-07-53, REPORT TO CONGRESSIONAL COMMITTEES ON FOOD STAMP TRAFFICKING: FNS COULD ENHANCE INTEGRITY BY BETTER TARGETING STORES LIKELY TO TRAFFIC AND INCREASING PENALTIES 2 (2006), [hereinafter GAO REPORT 2006], <http://www.gao.gov/assets/260/252570.pdf>.

¹⁵ *Id.*

¹⁶ GAO REPORT 2010, *supra* note 13, at 6; GAO Report 2006, *supra* note 25, at 1.

involving fraud and payments in excess of those legitimately due to beneficiaries [and] would total approximately” \$2.2. billion per year.¹⁷

After 2006, FNS began using data mining techniques to look for:

suspicious patterns of transaction activity, such as, for example, (1) multiple purchases from the same SNAP account in a brief period, (2) multiple SNAP purchases by multiple SNAP households in rapid succession from a single point of sale, (3) SNAP transactions that are unusually large for an individual, (4) SNAP purchases that completely deplete a participant’s monthly allotment, (5) transactions that are large for the store’s size and location, and (6) multiple SNAP redemptions in even dollar amounts.

Unfortunately, FNS does not share this data or provide access to states and localities to measure the same information; it carefully guards access to its database, ALERT, and to information ALERT releases. Currently, trafficking is difficult to monitor because the USDA fails to report on those stores doing the most business in the food stamp program.¹⁸

The Proposed Rule Should Allow Large Cities to Assist FNS in Detecting Retailer Fraud

Urban areas have higher concentrations of both SNAP recipients and small, privately owned groceries and convenience stores, making urban areas ideal partners to address retailer fraud. In order to accomplish this, these localities need access to the USDA’s ALERT database and strong penalties for retailers—as promised in December 2011. “Eighty-nine national and local studies document uneven geographic access to supermarkets in urban areas according to income, race, or both and nine had mixed results.”¹⁹ In New York City, there are more convenience stores and fast food chains than supermarkets and produce stands.²⁰ One “study based on focus groups with residents in East Baltimore . . . found that they were reliant on small neighborhood stores that charged extremely high prices and lacked a good variety and selection of healthy foods.”²¹ These highlight urban areas increased familiarity with small, privately-owned retailers. Moreover, many localities are urging the USDA to provide

¹⁷ *Id.* at 2.

¹⁸ Luke Rosiak, *Top Secret: \$80B a Year for Food Stamps, but Feds Won’t Reveal What’s Purchased*, WASH. TIMES (June 24, 2012), available at <http://www.washingtontimes.com/news/2012/jun/24/top-secret-what-food-stamps-buy/?page=1>.

¹⁹ The Food Trust, *The Grocery Gap: Who Has Access to Healthy Food & Why It Matters*, at 13 (2010), <http://www.policylink.org/atf/cf/%7B97C6D565-BB43-406D-A6D5-ECA3BBF35AF0%7D/FINALGroceryGap.pdf>.

²⁰ *Id.* at 14.

²¹ *Id.*

them access to ALERT to enhance their efforts to find retailer fraud. According to a *Washington Times* report, “The USDA is [now] preparing to update a study of the feasibility of capturing detailed purchase data from over 200,000 retailers that redeem SNAP benefits. . . .”²²

The Proposed Rule Should Broaden Access to ALERT Data

The USDA currently does not have the resources to set up a strong presence in areas with a high concentration of small retailers. To effectively execute the ALERT process in high-volume areas like New York City, the locality must have direct access to the database itself, not just the sharing of names, addresses, and risk scores for particular retailers. For example, our agency, through its experience in administering Medicaid as well as public assistance has investigative staff as well as staff skilled in data analytics that could be of great assistance in the USDA’s efforts to combat retailer fraud at the local level.

Direct access to the ALERT database presents a historic concern: states with the resources to use data-matching and investigative techniques will likely impose sanctions on a greater number of innocent-owner welfare fraud violations.²³

The Proposed Rule Should Include Appropriate Penalties for Retailers

Currently, the FNS claims that the penalty provision for retail fraud “makes meaningful distinctions based on the seriousness of the crime and the effect the fine will have on the store.”²⁴ Quite often however, the formula promulgated by the FNS often leads to the same results:

The fine for a store’s first violation is exactly half of the store’s annual food stamp redemptions for violations involving \$99 or less in food stamps, and is exactly the store’s annual food stamp redemptions for violations of more than \$100 or more in food stamps.... The formula guarantees that all these stores will receive the maximum possible, without recognizing any variation in the severity of the offense. The maximum penalty is also the probable sanction for stores with annual redemption between \$20,000 and \$40,000, because the higher penalty applies for any violation involving more than \$100. . . . Even small-time operators routinely conduct illegal food stamp trafficking violations over

²² Rosiak, *supra* note 31, at 1.

²³ See Elliot Regenstein, note, *Food Stamp Trafficking: Why Small Groceries Need Judicial Protection from the Department of Agriculture (and From Their Own Employees)*, 96 MICH. L. REV. 2156, 2181-84 (1998) (discussing the use of an arbitrary and capricious standard to review agency determinations against innocent owners).

²⁴ *Id.* at 2181.

\$100. Because the threshold is so low, the maximum penalty will be assessed in stores with annual food stamp redemptions of \$20,000 or more. The fine can cripple small inner-city stores with low profit margins.²⁵

In December 2011, FNS promised “stronger sanctions and penalties for retailers to allow USDA to take more aggressive action against those that violate program rules and give responsible retailers a bad name.”²⁶ FNS also promised to follow this with a proposed rule in Spring 2012. In February 2012, a Scripps Howard News investigation alleged that it found “dozens of individuals who had been banned as food-stamp vendors nonetheless remained in the business in New York; Los Angeles, Phoenix; San Diego; Tulsa, Okla.; West Palm Beach, Fla.; Baltimore and other communities across the country.”²⁷ This investigative method “involved comparing data from hundreds of current liquor, food and health licenses, state corporate filings and city business records with a list of stores that the USDA has permanently disqualified.”²⁸ There are currently more than 200,000 approved retailers in SNAP. Of the subset of excluded retailers, “Scripps’ analysis identified 137 locations at which merchants had been disqualified as many as four times.”²⁹ Many of the cities identified in the report are urban areas, who have localities willing to help the USDA find and eliminate this form of fraud.

However on May 24, 2012, FNS released that the proposed rule will come sometime in the third quarter of 2012.³⁰ Even if FNS elects not to obtain investigatory help from states and localities, at present, FNS can deter retailer fraud by developing new criteria to ensure the fine imposed is appropriate for a particular violation. For example, the criteria can include the store’s income and financial resources, a distinction between large and small stores, a consideration of whether the store has taken any action against the employee involved in illegal trafficking, and the financial repercussions of the fine on food stamp consumers. These steps will fall in line with the purpose of the Food Stamp Act and reduce some of the hurdles presented to small stores and food stamp consumers in poor communities.

²⁵ *Id.* at 2182-83.

²⁶ Press Release No. 0503.11, USDA Office of Communications, USDA Announces New Tactics to Combat Fraud and Enhance SNAP Program Integrity (Dec. 6, 2011) (available at <http://www.fns.usda.gov/cga/pressreleases/2011/0503.htm>).

²⁷ Isaac Wolf, *Store Owners, Banned from Food Stamps, Still Do*, Scripps Howard News Serv., Feb. 20, 2012, available at <http://www.standard.net/stories/2012/02/20/store-owners-banned-taking-food-stamps-still-do>.

²⁸ *Id.*

²⁹ *Id.* at 3.

³⁰ U.S. Dep’t of Ag., Food & Nutrition Serv., Press Release, *USDA Proposes Additional Steps to Fight Fraud & Enhance SNAP Integrity* (May 24, 2012), available at <http://www.fns.usda.gov/cga/PressReleases/2012/0164.htm>.

Thank you for the opportunity to comment on this proposed rule and we look forward to future opportunities to work with the USDA in addresses fraud, waste, and abuse in the Supplemental Nutritional Assistance Program.

Sincerely,

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cc: Robert Doar, *Commissioner*