June 10, 2003

SUBJECT: Final WIC Policy Memorandum #2002-1, Revision 1
Clarification of WIC Food Delivery Systems Final Rule
Questions and Answers

TO: Regional Directors
Supplemental Food Programs
All Regions

This policy memorandum updates our response to an issue regarding incentive items that was addressed in Final WIC Policy Memorandum #2002-1, dated November 8, 2001, includes answers to other questions that have been raised since the issuance of that policy memorandum, and incorporates the original and new questions and answers in a new format.

Revised Questions and Answers

Following the issuance of Final WIC Policy Memorandum #2002-1, FNS received requests for clarification of our answer to question #54 on a vendor's provision of incentive items to program participants. Based on section 246.12(h)(3)(ii) of the WIC regulations, the policy memorandum stated: "Providing diapers or other incentive items to participants is strictly prohibited by the vendor agreement." After considering this issue further, FNS has determined that WIC regulations do not give State agencies clear authority to prohibit vendors from providing incentive items to participants. The revised response, #I-2, also indicates that FNS intends to seek regulatory authority in this area.

This memorandum also reflects minor editorial changes to other questions and answers contained in Final WIC Policy Memorandum #2002-1. We added a reference to Final WIC Policy Memorandum #2002-7, dated September 20, 2002, which instructs State agencies to begin applying the new $25,000 maximum penalty for fraud or abuse, and changed cross-references to fit the new numbering format described below.

New Questions and Answers

This policy memorandum includes 20 new questions and answers. These questions arose subsequent to issuance of Final WIC Policy Memorandum #2002-1. We have inserted the new questions and answers at the end of the applicable section.

New Format

The revised policy memorandum uses a new format that allows questions and answers to be added to the document easily. For your reference, the following chart indicates the new numbers that have been assigned to the original questions and answers from WIC Policy Memorandum #2002-1, as well as the location and number of the added questions and answers.

Questions and Answers in Policy Memorandums
#2002-1 and #2002-1, Revision 1

Questions and Answers from Policy Memo #2002-1		New Questions and Answers in
New Numbers	Old Numbers	Policy Memo #2002-1, Revision 1
A. 1 – 7	1 – 7	A. 8 – 11
B. 1 – 5	8 – 12	B. 6 – 7
C. 1 – 4	3 – 16	C. 5
D. 1 – 5	17 – 21	
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G. 1 – 2	38 – 39	G. 3
H. 1 – 13	40 – 52	H. 14 – 15
I. 1 – 16	53 – 68	I. 17 – 22
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/signed/ Patricia N. Daniels
PATRICIA N. DANIELS
Director
Supplemental Food Programs Division

Attachment

Questions and Answers Regarding the WIC Food Delivery Systems Final Rule

Food and Nutrition Service
Special Supplemental Nutrition Program
for Women, Infants and Children (WIC)

June 2003

Table of Contents

A. Vendor Authorization

Question 1: Under §§ 246.12(g)(4) and (i)(1), if there is a break in a vendor's authorization, is the vendor's subsequent authorization considered an initial authorization, which requires the State agency to conduct a preauthorization visit and provide interactive training?

Answer: If during its break in authorization the vendor did not experience a change in ownership or location or cessation of operations (§ 246.12(h)(3)(xvii)), the vendor's subsequent authorization would not be considered an initial authorization for the purposes of §§ 246.12(g)(4) and (i)(1). However, if during its break in authorization the vendor did experience a change in ownership or location or cessation of business, the State agency must conduct both an on-site preauthorization visit and provide interactive training. Whenever a vendor experiences a break in authorization, the vendor must reapply for the Program and be selected by the State agency in accordance with § 246.12(g). If the vendor is subsequently reauthorized, the State agency must ensure that the vendor fully understands the conditions of its new vendor agreement and any changes in program rules since its previous authorization. For this reason, we recommend that the State agency conduct an on-site preauthorization visit and conduct interactive training when the vendor's break in authorization exceeds one year.

Question 2: If there is no break in a vendor's authorization and the State agency conducts a preauthorization visit, may the State agency count the subsequent preauthorization visit as a routine monitoring visit?

Answer: Yes, provided such visits meet the definition of routine monitoring, which means overt, on-site monitoring during which program representatives identify themselves to vendor personnel.

Question 3: Under § 246.12(g)(5), how may the Sate agency obtain information about the sale of a store and the relationship of the new owner to the previous owner to determine if the store has been sold in an attempt to circumvent a sanction?

Answer: The avenues for obtaining and verifying information about the ownership of businesses and the sales price and market value of businesses and their property will vary based on State laws and State cooperating agencies. For this reason, each State agency should seek advice from its General Counsel or Attorney General's

office on how to access such information. At a minimum, we recommend that the State agency include a question or series of questions on its vendor application to obtain information regarding a vendor applicant's relationship to the store's previous owners. For example, the vendor application could include the following questions: "Has the store been sold within the past two years? If so, are any of the current owners related by blood or marriage to any of the previous owners? If yes, please specify."

One source of information that may be useful in the State agency's determination of whether a store has been sold to circumvent a WIC sanction is the Food Stamp Program's (FSP) Store Tracking and Redemption Subsystem (STARS) database. Regulations at § 246.12(g)(8) now require the collection of a vendor applicant's FSP authorization number at the time of application. The State agency may use a vendor applicant's FSP authorization number or business name and address to access information in the STARS database. If the store is authorized as a retailer in the FSP, the owner of record in the FSP STARS database should be the same as the owner on the application for WIC vendor authorization. A discrepancy regarding store ownership could indicate an attempt to circumvent a sanction and warrants follow-up action to determine whether such evidence is sufficient to support denying WIC authorization to the vendor applicant. Although the FSP STARS database is updated frequently, the State agency should verify such information with its FSP counterparts prior to using it to support a denial of application. To maintain access to the STARS database, State agency staff with passwords must access the database at least once every 30 days.

Question 4: Under § 246.12(g)(8), why is the State agency required to collect shelf prices?

Answer: Regulations at § 246.12(g)(8) require the State agency to collect the vendor applicant's current shelf prices at the time of application because § 246.12(g)(3)(i) requires the State agency to consider the prices a vendor applicant charges for supplemental foods when selecting vendors for authorization. Even if it uses bid prices to select vendors for authorization, the State agency must collect shelf prices in addition to bid prices to ensure that the vendor applicant's bid prices do not exceed its current shelf prices.

Question 5: Is the State agency required to verify a vendor applicant's shelf prices prior to or at the time of the vendor's authorization? If so, does the State agency have to verify the price of each individual WIC-approved supplemental food item? Because shelf prices may vary on a daily basis, what action is the State agency required to take when there are discrepancies between the shelf prices the vendor applicant submitted with its application and the actual shelf prices when they are verified?

Answer: Regulations at § 246.12(g)(4) do not specifically require the State agency to verify the vendor applicant's shelf prices during the on-site preauthorization visit. However, the purpose of the preauthorization visit is to verify the information provided on the vendor application, such as the store's address, and to ensure that the vendor applicant appears to meet the selection criteria used by the State agency to select vendors for program authorization. If during the preauthorization visit the State agency discovers the vendor applicant either provided false information on its application or does not appear to meet the selection criteria, the State agency should not authorize the vendor applicant. If only minor discrepancies or problems are discovered during the preauthorization visit, the State agency must determine whether to require the vendor applicant to make corrective actions prior to receiving program authorization.

Question 6: Under § 246.12(g)(8), is the State agency required to collect a vendor applicant's shelf prices at reapplication if the State agency uses the vendor's actual price history, based on redemption data, to implement the competitive price vendor selection criterion?

Answer: Yes. Regulations at § 246.12(g)(8) require the State agency to collect the vendor applicant's current shelf prices at the time of application. The intent of this provision is to ensure that all vendor applicants, whether new applicants or current vendors, submit the same type of price information, so the State agency may objectively consider the prices a vendor applicant charges as compared to other vendor applicants. Similar to how we recommend that the State agency use the preauthorization visit to verify information, such as shelf prices, submitted by a new applicant on its vendor application, we recommend that the State agency use a vendor's actual price history to verify the shelf prices submitted with its current application.

Question 7: Under §§ 246.12(g)(3)(i) and (g)(8), may the State agency streamline the application process for obtaining and assessing the shelf prices of chain stores?

Answer: Yes, provided the process applies the competitive price vendor selection criterion in a fair and consistent manner.

Question 8: Under current rules, if there is a change in vendor ownership with little or no change to store management or staff, is the State agency still required to conduct an on-site preauthorization visit and provide interactive vendor training?

Answer: Yes, the State agency would be required to conduct an on-site preauthorization visit and provide interactive vendor training if there is a change in vendor ownership, even if there is little or no change in store management or staff. Regulations at § 246.12(h)(3)(xxi) clarify that a WIC vendor agreement is not a license or property interest that may be transferred to a new owner when a store is sold. Consequently, the new owner must submit a vendor application and be selected for vendor authorization by the State agency using current selection criteria. The only exception to the above requirements is when the State agency determines, under § 246.12(h)(3)(xvii), that a reported change represents a change in business structure rather than a change in ownership.

Regulations at § 246.12(g)(4) require the State agency to conduct an on-site visit prior to or at the time of a vendor's initial authorization. Therefore, the State agency must conduct a preauthorization visit, even though the vendor was previously authorized under a different owner. With regard to training, regulations at § 246.12(i)(1) state, in part, "Prior to or at the time of a vendor's initial authorization, and at least once every three years thereafter, the training must be in an interactive format that includes a contemporaneous opportunity for questions and answers."

Question 9: What should a State agency do if it suspects that a vendor applicant, who has been denied authorization due to a history of noncompliance, may be attempting to circumvent the denial of authorization by having a relative or other third party submit a vendor application?

Answer: Regulations at § 246.12(g)(5) state: "The State agency may not authorize a vendor applicant if the State agency determines that the store has been sold by its previous owner in an attempt to circumvent a WIC sanction. The State agency may consider such factors as whether the store was sold to a relative by blood or

marriage of the previous owner(s) or sold to any individual or organization for less than its fair market value." The State agency should require the current vendor applicant to disclose all owners, officers, and managers involved in the business, including whether the previous owner is a relative or is involved in the business in any way. If the current owner indicates that the previous owner is involved in the business, then the State agency may deny the application for the same reason it denied the previous owner's application. If the current owner indicates that the previous owner is a relative, but is not involved in the business, the State agency must decide whether there is sufficient evidence to support denying the current owner's application. This would include determining whether the current owner purchased the business at fair market value, or whether the previous owner's name is still on the deed or lease for the property.

If the current owner indicates that the previous owner is not involved in the business in any way, then as noted at 65 FR 83252 of the preamble to the WIC Food Delivery Systems final rule, the State agency may require the new owner to sign an affidavit during the application process stating that the previous owner has no interest in and is not involved in the business. The State agency may want to verify with the State's business license and/or tax agency that the previous owner does not appear on the current owner's business license or corporation registration. If this information is not available at the time of application, the State agency should follow up and verify the accuracy of the application when it becomes available. Under § 246.12(h)(3)(xvi), if the State agency determines at any time during the application process or during a vendor's authorization period that the vendor has provided false information in connection with its application, then the State agency will immediately deny/terminate the vendor's application or agreement.

Question 10: Is a State agency allowed to collect a vendor's Federal tax identification (ID) number on its vendor application?

Answer: The Employer Identification Number (EIN) is a unique taxpayer identification number assigned by the Internal Revenue Service. Since there appears to be no prohibition against the collection of the EIN, or Federal tax identification number, a State agency may request the EIN, but should protect this confidential information once collected. In addition, any vendor who fails to provide its EIN should not be prevented from participating in the WIC Program solely for failure to do so. We would advise a State agency that is considering collecting the EIN to consult with its legal counsel regarding the intended use of this number and whether other State information or mechanisms would be more appropriate.

Question 11: Do the WIC regulations require State agencies to take steps to accommodate vendor applicants with limited English proficiency?

Answer: No, WIC regulations do not require State agencies to take any specific action to accommodate vendors of limited English proficiency. However, we would advise State agencies to take "reasonable steps" to provide information on WIC authorization to vendors with limited English proficiency.

The Food Stamp Program serves as an example of the types of actions State agencies might take relative to vendors of limited English proficiency. While FSP has no legal obligation to provide materials in multiple languages, the program has undertaken a major effort to train retailers, including those of limited English proficiency, primarily as a customer service initiative. FSP staff meets with merchant associations representing different ethnic groups to explain the program. FSP also provides selected information (such as store signs indicating acceptance of food stamps, in-store posters for clients summarizing what they can or cannot purchase with food stamps, and in-store cards identifying the penalties for violation of the FSP) for authorized retailers in seven different languages. FSP also has a retailer training guide and video in English and Spanish. FSP holds the retailer responsible for bringing an interpreter to training sessions or other meetings, as necessary.

B. Vendor Selection Criteria

Question 1: Under §§ 246.12(g)(3)(i) and (g)(3)(ii), what are some examples of how the State agency may establish vendor peer groups?

Answer: Vendor peer groups are often established based on a combination of two factors—vendor size and vendor location. Vendor size may be determined through a variety of factors, such as total business volume, WIC business volume, square footage of store, number of cash registers, or type of store (e.g., supermarket, grocery store, convenience store, military commissary, nonprofit co-op, or pharmacy). Vendor location is often divided into geographic categories, such as urban, suburban, and rural, which may also include a number of subcategories within the State.

Question 2: Under § 246.12(g)(3)(ii), how may the State agency address the minimum variety and quantity of supplemental foods vendor selection criterion in situations in which there are no infant participants in a local service area, and therefore no need for vendors to carry soy infant formula?

Answer: If the State agency wants to make exceptions to its minimum variety and quantity of supplemental foods vendor selection criterion, it should do so when it establishes or modifies this criterion and include such exceptions in its State Plan to ensure that the criterion is applied consistently throughout the State. In addition, if an exception has conditions, such as making the excepted supplemental foods available within 24 hours upon request by the State or local agency or a participant, then the conditions should also be specified in the vendor selection criterion included in the State Plan. Although we understand the reasons why a State agency may want to establish such exceptions, we do not recommend the widespread use of them, especially in open (i.e., non-vendor-specific) food instrument systems in which vendors may accept food instruments from participants who live outside the local service area.

Question 3: Under § 246.12(g)(3), may the State agency deny a vendor application for a State-established selection criterion even if denial of the vendor applicant would result in inadequate participant access?

Answer: No, unless the State agency either authorizes another vendor or implements an alternative food delivery system in the area in which the denied vendor applicant operates. Regulations at § 246.12(g)(1) state in part: "The State agency must authorize an appropriate number and distribution of vendors in order to ensure adequate participant access to supplemental foods." To ensure adequate

participant access, three of the four mandatory vendor selection criteria allow for enough flexibility to authorize vendor applicants even when they do not meet the criteria.

The mandatory vendor selection criteria in §§ 246.12(g)(3)(iii) and (g)(3)(iv) specify that "unless denying authorization of a vendor applicant would result in inadequate participant access, the State agency may not authorize a vendor applicant that" does not meet these criteria. The competitive price vendor selection criterion (§ 246.12(g)(3)(i)) provides the State agency with the flexibility to establish vendor peer groups to address situations in which the State agency must authorize higher-priced vendors to ensure adequate participant access. Only the vendor selection criterion for minimum variety and quantity of supplemental foods (§ 246.12(g)(3)(ii)) strictly prohibits the State agency from authorizing a vendor applicant "unless it determines that the vendor applicant meets these minimums." As stated in the preamble, "authorizing vendors that do not maintain the required minimum stocks of supplemental foods undermines the nutritional goals of the Program." Similarly, failing to provide participants with adequate access to supplemental foods because vendor applicants do not meet State-established selection criteria would also undermine the nutritional goals of the Program.

Question 4: Under § 246.12(g)(3)(iii), how should the State agency determine whether a vendor applicant meets the business integrity vendor selection criterion?

Answer: At a minimum, we recommend adding the following question to the vendor application: "During the past six years, has any current owner, officer, or manager at your store been convicted of or had a civil judgment for any of the following activities: fraud, antitrust violations, embezzlement, theft, forgery, bribery, falsification or destruction of records, making false statements, receiving stolen property, making false claims, or obstruction of justice. If so, please specify the name of the owner, officer, or manager and the activities involved." If the answer to this question is negative and the State agency is unaware of any information to the contrary, the State agency may assume the information provided is correct and authorize the vendor. If the answer to this question is affirmative, the State agency must determine whether authorization of the vendor applicant is necessary to ensure adequate participant access.

Question 5: Under §§ 246.12(g)(3)(ii), (g)(3)(iii), (g)(3)(iv), and (g)(5), what does "may not" mean?

Answer: Under the standards established for writing in "plain language," the words, "may not," mean there is no option. In the citations listed in the question above, when the regulations state, "the State agency may not . . .," it means that the State agency does not have any discretion in the matter.

Question 6: What should a State agency do if it learns during a reassessment that a vendor no longer meets the vendor selection criteria?

Answer: Regulations at § 246.12(h)(3)(xxiv) require the State agency to terminate the vendor agreement if the vendor fails to meet the current vendor selection criteria. Regarding this requirement, section 2.e. of the preamble to the WIC Food Delivery Systems final rule (65 FR 83251) states: "The State agency may include as part of both its vendor selection process and its reassessment process an opportunity to correct any deficiency that would otherwise lead to nonselection or termination of the vendor agreement. However, this is at the discretion of the State agency; and the State agency must make this clear in its procedures for implementing its vendor selection criteria." Before terminating the vendor agreement, the State agency must provide advance written notice of not less than 15 days (§ 246.12(h)(3)(xvi)).

Question 7: Under § 246.12(g)(3)(iv), a State agency may not authorize a vendor applicant who has been disqualified from the Food Stamp Program (FSP). How does this provision apply to a vendor who is appealing a FSP disqualification?

Answer: When a WIC vendor applicant is appealing a FSP disqualification, a State agency may authorize the vendor while awaiting the outcome of the appeal, unless other vendor selection and/or limitation criteria justify not authorizing the vendor. This approach is consistent with the preamble to the WIC/FSP Disqualification Proposed Rule (63 FR 19417), which incorporates wording from Final WIC Policy Memorandum #98-2, entitled "WIC Vendor Disqualification Resulting from Permanent Disqualification from the Food Stamp Program." This memorandum states that a WIC reciprocal disqualification based on a permanent FSP disqualification should not take effect until all FSP appeal actions have been exhausted and a final administrative or judicial decision is rendered. If the FSP disqualification is upheld, the State agency must disqualify the vendor unless disqualification would result in inadequate participant access, as stated in § 246.12(l)(1)(ix) of the regulations.

C. Vendor Agreements

Question 1: Under § 246.12(h)(1)(i), when the State agency provides a vendor with advance written notice of the expiration of the vendor agreement, may the State agency also notify the vendor that it does not intend to reauthorize the vendor, because the vendor's redemption history indicates that it does not meet the State agency's current vendor selection criterion for competitive price or minimum redemptions, etc.?

Answer: At the time the State agency provides advance written notice of the expiration of the vendor agreement, the State agency may notify the vendor that, based on its recent redemption history, it does not meet the State agency's current selection criteria. However, the State agency may not prohibit the vendor from reapplying for vendor authorization, must assess the vendor's subsequent application along with other vendor applicants and authorized vendors using the selection criteria in effect at the time, and must apply its selection criteria consistently throughout its jurisdiction.

Question 2: Under § 246.12(h)(3)(xvi), when the State agency terminates a vendor for cause, may the State agency set a minimum period the vendor and/or location must wait before it reapplies?

Answer: No, unless such periods are established through either vendor sanctions or vendor selection criteria. Although regulations at § 246.12(g)(7) permit the State agency to limit the periods during which it accepts and processes vendor applications, this provision does not permit the State agency to prohibit particular vendors or particular store locations from reapplying for vendor authorization. All vendor applicants, except those who are currently disqualified, must be permitted to apply for vendor authorization whenever the State agency is accepting and processing applications for vendor authorization. To address the types of violations that trigger termination of vendor agreements, we recommend that the State agency either establish State agency sanctions for these violations that result in vendor disqualification or establish vendor selection criteria for these violations that result in denial of vendor applications.

For example, although regulations at § 246.12(h)(3)(xvi) require immediate termination of the vendor agreement when the State agency determines the vendor provided false information in connection with its application for authorization, we recommend that the State agency also establish a one-year disqualification for this violation. In addition, depending on the severity of the violation, we recommend that the State agency, in accordance with § 246.12(u)(5), refer the vendor to

Federal, State, or local authorities for prosecution under applicable statutes. If the vendor's owners, officers, or managers subsequently are convicted or have a civil judgment entered against them for making false statements, they may be denied vendor authorization under § 246.12(g)(3)(iii) for a period of six years.

In addition to establishing vendor sanctions, the State agency also may establish vendor selection criteria to address violations that trigger termination of vendor agreements. For example, the State agency could establish a State agency selection criterion that states: "Unless denying authorization of a vendor applicant would result in inadequate participant access, the State agency will not authorize a vendor applicant if during the last 90 days the vendor applicant's previous vendor agreement was terminated for cause by the State agency." The timeframes established for such vendor selection criteria must be reasonable, and, as required by § 246.4(a)(14)(ii), all of the State agency's vendor selection criteria must be included in its State Plan.

Question 3: Under § 246.12(h)(3)(xvii), if a vendor grants "power of attorney" to someone to operate its business, is this considered a change in ownership?

Answer: No. Granting power of attorney to another party does not mean that ownership has been transferred to that other party, rather it means that the other party has been legally granted the power to make business decisions on the owner's behalf.

Question 4: Under § 246.12(h)(3)(xvii), if a vendor sublets its store, is this considered a change in ownership?

Answer: The vendor agreement, which authorizes a vendor to accept and redeem food instruments, is between the State agency and a business entity operating a store at a single location. As § 246.12(h)(3)(xxi) indicates, the vendor agreement is not a license or property interest that can be transferred or sold to another business entity. If a vendor sublets its store to another business entity to operate, the other business entity would need to apply and be selected for vendor authorization before it could accept and redeem food instruments.

Question 5: Does § 246.12(h)(3)(xvi) allow a State agency to terminate a vendor agreement immediately for a change of ownership?

Answer: No. This provision requires a State agency to terminate the vendor agreement immediately if it determines that the vendor provided false information in connection with its application for authorization. In other instances, such as

change of ownership, the State agency may terminate the agreement after providing advance written notice of not less than 15 days.

D. Exchanges of and Rain Checks for Supplemental Foods

Question 1: Under § 246.12(h)(3)(ii), does the State agency have the discretion to prohibit all exchanges of supplemental foods or to prohibit exchanges unless approved by the State or local agency?

Answer: No. Regulations at § 246.12(h)(3)(ii) state in part: "The vendor may not provide refunds or permit exchanges for authorized supplemental foods obtained with food instruments, except for exchanges of an identical authorized supplemental food item when the original authorized supplemental food item is defective, spoiled, or has exceeded its 'sell by,' 'best if used by,' or other date limiting the sale or use of the food item. An identical authorized supplemental food item means the exact brand and size as the original authorized supplemental food item obtained and returned by the participant." This provision of the vendor agreement establishes the specific circumstances under which vendors may provide exchanges of supplemental foods to participants.

Under previous regulations, which strictly prohibited all exchanges of supplemental food items, participants were unable to exchange defective, spoiled, or outdated supplemental food items, resulting in unnecessary food loss. Retail stores generally provide exchanges of defective, spoiled, or outdated food items to all customers regardless of whether they provide receipts. Consequently, vendors typically do not know whether a customer requesting an exchange is a program participant, unless the exchange is requested directly after a WIC transaction. In addition, FNS routinely receives complaints from participants about vendors refusing to exchange defective, spoiled, or outdated supplemental food items. Participants often ask why they are not being offered the same courtesies offered to other customers, which is required by both previous and current regulations (§ 246.12(h)(3)(iii)).

For these reasons, we included an exception to our "no exchanges" provision in the proposed rule. The exception was supported by a vast majority of those who commented on the proposal and was modified to address concerns that commenters had about what constitutes an "identical authorized supplemental food item." Requiring all exchanges of defective, spoiled, or outdated supplemental food items be approved by the State or local agency would not only be an inconvenience for vendors and participants but would also be an administrative burden on State and local agencies. For these reasons, we believe the exception permitted under § 246.12(h)(3)(ii) of the final rule is in the best interests of the WIC Program.

Question 2: Under § 246.12(h)(3)(ii), may the State agency require *all* infant formula exchanges to be processed through the State or local agency?

Answer: No. As noted in the above answer to Question 1 of this section, regulations at § 246.12(h)(3)(ii) specify the circumstances under which vendors may, without the approval of the State or local agency, provide participants with exchanges of defective, spoiled, or outdated supplemental food items, including infant formula. Under this provision, vendors may only provide exchanges for the exact same brand and size of infant formula that was originally obtained by the participant. Providing exchanges for alternative brands or sizes of infant formula is strictly prohibited under the vendor agreement and is a vendor violation under § 246.12(l)(1)(iv).

Question 3: Under § 246.12(h)(3)(ii), may the State agency allow exchanges of contract brands of infant formula for noncontract brands of infant formula when medical documentation is provided?

Answer: Yes, provided such exchanges are in accordance with § 246.10(c)(1). As noted in the above answer to Question 2 of this section, vendors are strictly prohibited from providing exchanges for alternative brands of infant formula. Consequently, exchanges of contract brands of infant formula for noncontract brands must be processed through the State or local agency. For exchanges of food instruments, the participant, caretaker, or proxy must return his or her unused food instruments, and the State or local agency must void the returned food instruments and issue new food instruments for the same amount of infant formula. For exchanges of unopened containers of contract brand infant formula, the State agency has the discretion to permit such exchanges. If the State agency decides to permit exchanges of unopened containers of contract brand infant formula, it must establish standard procedures for how such exchanges will be processed.

Question 4: Under § 246.12(h)(3)(ii), may the State agency allow exchanges for a different flavor of the exact same brand and size of supplemental food item? For example, if the parent/caretaker purchases 24 cans of strawberry Pediasure and discovers that the child does not like strawberry, may the parent/caretaker return to the vendor and exchange the unused cans of strawberry Pediasure for cans of chocolate Pediasure?

Answer: Yes, provided the different flavor is also an authorized supplemental food item.

Question 5: In rural areas in which a vendor cannot provide all the supplemental food items on the food instrument that day but will have sufficient stock the following day, may the vendor provide part of the supplemental food items listed on the food instrument, give the participant a raincheck, and provide the remaining supplemental food items the following day?

Answer: No. Regulations at § 246.12(h)(3)(ii) specifically prohibit the use of rainchecks in the WIC Program. When a vendor has insufficient stock of supplemental foods, the participant is faced with a difficult choice: 1) transact the food instrument and purchase the authorized supplemental foods that are available, 2) return when the vendor has sufficient stock of supplemental foods, or 3) travel to another vendor and transact the food instrument. To avoid such situations, the vendor agreement requires the vendor to comply with the minimum variety and quantity of supplemental foods selection criterion throughout the agreement period (§ 246.12(h)(3)(xxiv)). Vendors that frequently do not have sufficient stock of supplemental foods inconvenience participants and potentially undermine both the integrity and the nutritional goals of the Program. When the State agency becomes aware of such situations, the State agency should warn the vendor that failure to meet the requirements for minimum stock may result in termination of the vendor agreement. The State agency should follow up such warnings with a reassessment of the vendor. If the vendor fails to meet the current selection criteria, the State agency should terminate the vendor's agreement.

Although the minimum stocking requirements are intended to ensure that participants have access to supplemental foods, we recognize that situations arise, especially in rural areas, in which vendors experience stocking problems, and that terminating vendors' agreements would result in inadequate participant access. To address these types of situations, we recommend that the State or local agency work with local vendors to resolve such problems. For example, vendors may complain that their stocks of particular supplemental food items, such as infant formula, are often depleted during particular periods of time, such as the beginning of each month, when participants typically transact their food instruments for their monthly supplies of supplemental foods. To resolve this type of problem, the State or local agency could adjust their food instrument issuance patterns to prevent vendors' stocks of supplemental foods from being depleted. For instance, a rural local agency could stagger the "first date of use" on the food instruments it issues, so participants are not all attempting to transact their food instruments on the same day of the month. Similarly, the local agency could issue multiple food instruments for particular food packages, such as infant food packages, so participants may obtain smaller quantities of supplemental foods.

E. Food Instrument Requirements

Question 1: Under § 246.12(h)(3)(viii), may the State agency impose an administrative fee on rejected food instruments?

Answer: Yes, provided the food instruments are rejected due to vendor error and the fees for resubmitting the food instruments for payment are reasonable and represent the costs of doing business. Since food instruments are typically rejected due to vendor error, it is appropriate that vendors bear the costs associated with processing food instruments that are resubmitted for payment. However, when the State agency determines that food instruments were rejected due to errors committed by either the State agency or its financial institution, the State agency may not charge fees to vendors for food instruments that must be resubmitted for payment as a result of such errors.

Question 2: Under §§ 246.12(g)(3)(i) and (h)(3)(viii), how may the State agency establish vendor price limitations on food instruments submitted by vendors for redemption?

Answer: On page 83254 of the final rule, under section 4.a. of the preamble, we provided the following three scenarios that would satisfy the price limitations requirements: "*Scenario 1*: The State agency assigns vendors to peer groups upon authorization and then makes price adjustments to its payments to vendors based on the price limitations applicable to the vendor's peer groups; *Scenario 2*: The State agency compares the prices a vendor applicant charges for supplemental foods with those charged by other vendor applicants and authorized vendors to determine which vendors to authorize and then periodically conducts a reassessment of the vendor's prices to ensure they meet the applicable price limitations; and *Scenario 3*: The State agency establishes a maximum price it will pay for each type of food instrument and then includes a provision in the vendor agreement that the State agency will not pay vendors in excess of the maximum price established for each food instrument."

The above list is not intended to be exhaustive. The State agency has discretion to determine how it establishes its price limitations; however, the price limitations must be designed to ensure that the State agency does not pay a vendor at a level that would otherwise make the vendor ineligible for program authorization. One consideration in establishing price limitations is who, the State agency or the vendor, has the responsibility to ensure that the vendor's prices comply with the price limitations. For example, some State agencies print a maximum price on each type of food instrument and assign the responsibility to the vendor, via the

vendor agreement, to ensure that the purchase price entered on food instruments does not exceed the maximum price. If the vendor submits a food instrument for redemption that exceeds the maximum price, then the vendor has committed a vendor overcharge, which the State agency collects through the establishment of a vendor claim. If the State agency assumes the responsibility to ensure that the vendor does not exceed the maximum price, then when the vendor submits a food instrument for redemption that exceeds the maximum price, the State agency makes a price adjustment to the purchase price on the food instrument and pays the vendor according to the established price limitations. Some State agencies have sophisticated redemption systems that pay vendors based on a rolling average redemption price for each food instrument type for the vendor's peer group. In this type of system, the State agency makes price adjustments to all food instruments that exceed the price limitations and pays the vendor up to the rolling average, or in some cases, up to a percentage (e.g., 10%) above the rolling average.

There are a variety of ways in which the State agency may implement the price limitation provision. State agency personnel may want to contact counterparts in other State agencies to seek information about how they have implemented the price limitation provision. If a State agency is having difficulty determining how to implement this provision, it should contact its FNS regional office for assistance.

Question 3: Under §§ 246.12(g)(3)(i) and (h)(3)(viii), how may the State agency make price adjustments to food instruments submitted for redemption by military commissaries that do not accept price adjustments and that make participants pay restitution for food instruments not paid or partially paid by the State agency?

Answer: On February 7, 1983, FNS and the Department of Defense entered into a Memorandum of Understanding (MOU) entitled "Military Commissaries as WIC Program Vendors." Section 5 of the MOU states: "In view of Federal immunity from State claims or review, the State agency may not … require claims to be paid [by commissaries]. However, a State agency may review redeemed food instruments prior to payment. If the food instruments are found to contain errors or omissions, payment may be denied unless or until further justification or correction is provided by the submitting commissary. If the State agency identifies a possible problem, it shall write the commanding officer of the installation requesting repayment, investigation, or other appropriate action. The commanding officer of the installation or his designee shall take necessary action and promptly reply to the State agency, including repayment if appropriate."

Although the MOU does not provide the State agency with the authority to make prepayment price adjustments to food instruments, it does provide the State agency with the authority to deny payment of food instruments with errors or omissions. Rather than make prepayment price adjustments, the State agency may need to establish special procedures to deny payment of food instruments submitted by commissaries for redemption that exceed its price limitations and return such food instruments to commissaries to resubmit with appropriate justification or correction. These special procedures may require the State agency to use a nonstandard vendor agreement for commissaries, which must be documented in its State Plan in accordance with § 246.12(h)(2). The special procedures also may require the State agency to amend its banking contract to ensure that prepayment price adjustments are not made to food instruments submitted by commissaries for redemption. Alternatively, the State agency may wish to use vendor-specific food instruments for participants that obtain their supplemental foods from commissaries in order to exempt these food instruments from prepayment price adjustments.

The practice of commissaries making participants pay restitution for food instruments not paid or partially paid by the State agency is unacceptable under Federal law and regulations governing the WIC Program. Regulations at § 246.12(h)(3)(x) make clear in the vendor agreement that such practices are not permitted in the WIC Program. Commissaries that refuse to accept this provision as part of the vendor agreement should not be authorized. If the State agency determines that a commissary makes participants pay restitution for food instruments, the State agency should terminate for cause the commissary's vendor agreement. If the State agency is unable to authorize a commissary because it either fails to accept or to abide by program requirements, the participants that typically shop at the commissary will need to obtain their supplemental foods from other vendors in the area. If the State agency needs assistance on issues regarding commissaries, it should contact its FNS regional office, which will work in conjunction with the Department of Defense to resolve problems.

Question 4: Under § 246.12(h)(3)(ix), may the State agency establish in the vendor agreement that it will provide the vendor with either an opportunity to justify food instrument errors or an opportunity to correct food instrument errors?

Answer: No. Whenever the State agency delays or denies payment to a vendor for a vendor claim, it must provide the vendor with an opportunity to justify or correct the food instrument error. This opportunity must be provided by the State agency because disputes regarding food instrument payments and vendor claims are not subject to administrative review under § 246.18(a)(1)(iii)(F). Regulations at

§ 246.12(h)(3)(ix) use the coordinating conjunction "or" rather then the correlative conjunction "either/or," which is consistent with previous regulations at § 246.12(r)(5)(iii). The use of a coordinating conjunction in this provision does not provide the State agency with the discretion to restrict the vendor's opportunity to either justifying food instrument errors or to correcting food instruments errors. Such a restriction would be inappropriate because some types of errors lend themselves to justification, which does not propose a change to the original purchase price, whereas other errors lend themselves to correction, which proposes a change to the original purchase price.

For example, on occasion, in response to vendor claims for what appear to be vendor overcharges, a large number of vendors may justify exceeding the State agency's maximum prices because of increases in the wholesale prices for supplemental foods. Regulations at § 246.12(g)(3)(i) permit the State agency to include a factor in its price limitations to reflect fluctuations in wholesale prices. The justification provided by vendors in response to the vendor claims may lead the State agency to increase its maximum prices to reflect the increases in wholesale prices of supplemental foods and pay vendors up to the new maximum prices.

Other situations may lend themselves to correction of food instrument errors. For example, on occasion, a cashier may inadvertently transpose the amount from the cash register (e.g., $19.21) and enter the wrong amount (e.g., $91.21) as the purchase price on a food instrument. When the State agency establishes a vendor claim against the vendor for what appears to be a gross vendor overcharge, the vendor should be provided with the opportunity to correct the purchase price ($19.21) and receive payment for the corrected purchase price of the food instrument. Naturally, such errors should not occur too frequently, but when they do, the State agency should provide vendors with the opportunity to correct food instrument errors that clearly appear to be honest mistakes and not systematic fraud or abuse.

Question 5: May the State agency establish in the vendor agreement that certain errors (i.e., fatal errors), such as missing signatures or purchase prices, will not be paid by the State agency and cannot be justified or corrected by the vendor as permitted under §§ 246.12(h)(3)(ix) and (k)(3)?

Answer: Regulations at §§ 246.12(h)(3)(v) and (h)(3)(vi) require vendor agreements include provisions that require vendors to ensure that purchase prices be entered on food instruments at the time of the transaction and that participants, parents/caretakers, or proxies sign food instruments in the presence of cashiers. The State agency may establish in the vendor agreement that certain errors (e.g.,

missing signatures, missing and/or altered purchase prices) are "fatal errors" and that food instruments containing such errors will not be paid by the State agency. However, the State agency is still required to provide the vendor with an opportunity to justify or correct such errors.

For example, it is possible that the State agency's banking institution's pre-payment edit system inadvertently codes food instruments with faint signatures as missing signatures and rejects payment on them. If the vendor resubmits such food instruments as justification that the fatal errors were the result of the banking system, the State agency may be convinced by the evidence and subsequently make payment to the vendor for the food instruments. Regulations at §§ 246.12(h)(3)(ix) and (k)(3) do not require the State agency to automatically make payment on all food instruments that contain errors for which vendors submit justification/corrections. Instead, the regulations require the State agency to have a system to receive vendors' justifications/corrections for food instrument errors, to consider the information and/or evidence provided by vendors, and make payments to vendors when justified.

Question 6: On page 83262 of the preamble, the last sentence in section 6c states that the review required by § 246.12(k)(1) "must be done on a continuing basis." How does FNS define "on a continuing basis?"

Answer: In the proposal, we specified that the review of food instruments required by § 246.12(k)(1) must occur "not less frequently than quarterly." In the final rule, we specified that the State agency must take follow-up action on food instrument errors within 120 days of detection, but we did not specify a time period for conducting the review. By "on a continuing basis," we mean that the review must occur routinely and frequently enough to provide the State agency with sufficient time to take follow-up action on food instrument errors that affect vendor payments. In the same section of the preamble, we stated that "as State agencies continue to automate their food instrument redemption systems, they should design their systems to include a review of all food instruments before they make payment on them." Our expectation is that eventually all State agencies will implement pre-edit systems that review all food instruments submitted for redemption to detect all the food instrument errors listed in § 246.12(k)(1).

Question 7: Under § 246.12(k)(1), what does FNS consider to be a representative sample of food instruments?

Answer: A representative sample is a randomly selected sample of a population that is large enough to make inferences or draw conclusions about the characteristics of that population. For the purposes of § 246.12(k)(1), the size of

the sample would depend on how frequently the State agency conducts its reviews of food instruments. If the State agency conducts its reviews on a monthly basis, the population would be the total number of food instruments submitted for redemption during the month being reviewed. If the State agency conducts its review on quarterly basis, the population would be the total number of food instruments submitted for redemption during the quarter being reviewed. Each sample of food instruments should be such that all types of food instruments (e.g., pregnant woman, postpartum woman, breastfeeding woman, infant, child, etc.) are proportionately represented. One method used by State agencies to meet this requirement is to randomly select one week out of each month, or one month out of each quarter, and review all the food instruments redeemed during that period. For further assistance, we suggest that State agency staff contact a statistician employed by the State or a statistics professor at a local college or university.

Question 8: Would a pre/post-edit system that reviews all food instruments submitted for redemption for all the items listed in § 246.12(k)(1) meet this requirement without having to review a representative sample of food instruments?

Answer: Yes. However, we still recommend that the State agency periodically review a sample of food instruments submitted for redemption to ensure that the State agency's pre/post-edit system is operating properly.

Question 9: Under § 246.12(k)(1), is the State agency required to review (i.e., edit) food instruments to determine if they were transacted either before or after the specified period? If so, how does the State agency accomplish this when the redeemed food instrument only shows the date it was submitted for redemption, not the date it was transacted?

Answer: Regulations at § 246.12(k)(1) require the State agency implement a system to review printed food instruments to detect those transacted or submitted for redemption *after* the specified time periods. The provision does not require the system to detect food instruments transacted or submitted for redemption *before* the specified time periods. Nevertheless, some State agencies have indicated that their pre-edit systems are able to detect such food instrument errors.

If its food instrument transaction procedures do not include entering the transaction date on the food instrument, the State agency cannot review food instruments to determine if they were transacted after the specified period for transaction. To implement this provision, the State agency will need to implement a procedure to enter the transaction date on its food instruments. Entering the transaction date on food instruments is typically accomplished through two

methods: 1) the transaction date is entered manually, similar to writing the date on a personal check; or 2) the transaction date is entered electronically when the cashier feeds the food instrument into the cash register to print the total sale on the back of the food instrument. The State agency has the discretion to determine the method used to enter the transaction date on its food instruments and whether the review of the transaction date will be accomplished through a pre-edit, a post-edit, or a representative sample.

Question 10: Under § 246.12(q), if a food instrument has been issued but never redeemed, is the State agency required to "void" the food instrument, and if so, within what timeframe should this take place?

Answer: No. Regulations at § 246.12(q) require the State agency to account for the disposition of all food instruments as either issued or voided, and as either redeemed or unredeemed. This process must be performed within 150 days after the first valid date for participant use of a food instrument and must be conducted in accordance with the financial management requirements in § 246.13. Consequently, a food instrument that was issued and never redeemed should be accounted for as "issued" and "unredeemed," and the State agency should adjust its projected expenditures in accordance with § 246.13(h) to deobligate food funds associated with unredeemed food instruments.

Question 11: Does a print-on-demand system that will not issue food instruments unless there is a valid electronic certification record meet the food instrument disposition requirements in § 246.12(q) for matching redeemed food instruments against valid enrollment and issuance records? If not, how is this match to be achieved without having to examine individual food instruments and individual enrollment records?

Answer: No. A print-on-demand system does not match a *redeemed* food instrument against valid enrollment and issuance records, rather it verifies that an enrollment record exists *before* it issues (i.e., prints) a participant's food instruments. The process of disposition is intended to account for food instruments *after* they have been issued to participants. Whereas previous regulations at § 246.12(n)(2) required the State agency "to demonstrate to FNS its capability to reconcile a given food instrument to a valid certification record," current regulations at § 246.12(q) now require the State agency to actually match redeemed food instruments with valid issuance and enrollment (i.e., certification) records as part of the food instrument disposition process. Our expectation for this requirement is that the State agency will utilize its Management Information System (MIS) to complete this task electronically.

The State agency's MIS should have an issuance file (Issuance File) that identifies the enrollment (i.e., certification) record to which specific food instrument serial numbers have been issued. The MIS should also have a redeemed file (Redeemed File) that identifies the food instrument serial numbers that have been paid or rejected by the State agency and their redemption amounts. To begin the disposition process, the system should retrieve the Issuance File for all food instruments that have a redemption date within the month of issuance that will be reconciled. Then, the system should retrieve the Redeemed File compiled for all food instruments paid or rejected during that period. Next, the system should complete a one-to-one match of the food instrument serial numbers in the Issuance File with the serial numbers in the Redemption File. All food instruments on the Redeemed File must be matched with a valid enrollment record on the Issuance File. For food instruments that have no matching enrollment records, the State agency should prepare an exception report for each local agency that issued the unmatched food instruments. The local agency should investigate the matter. If there are redeemed food instruments that still cannot be matched to valid issuance and enrollment records, the State agency would need to identify the reasons why the food instruments are unmatched and to take appropriate actions to improve its procedures.

For further information, the State agency should refer to the Food Instrument sections of the Functional Requirements Document (FReD) for MIS development. This document has detailed information about the core requirements for such systems. A new revision of the FReD document was released early in 2002.

Question 12: Is the expectation of § 246.12(q) that all food instruments with MICR encoding errors be manually matched with participant case files, which would be very expensive to do?

Answer: No. Although regulations at § 246.12(q) require the State agency to account for the disposition of all food instruments, the regulations regarding claims and penalties clarify the expectation regarding unmatched food instruments. Regulations at § 246.23(a)(4) state: "FNS will establish a claim against any State agency that has not accounted for the disposition of all redeemed food instruments and taken appropriate follow-up action on all redeemed food instruments that cannot be matched against valid enrollment and issuance records, including cases that may involve fraud, unless the State agency has demonstrated to the satisfaction of FNS that it has: "(i) Made every reasonable effort to comply with the requirement; (ii) Identified the reasons for its inability to account for the disposition of each redeemed food instrument; and (iii) Provided assurances that, to the extent considered necessary by FNS, it will take appropriate actions to

improve its procedures." Below is a discussion regarding how we recommend the State agency reconcile food instruments with MICR encoding errors.

The line on the bottom of all checks used in the U.S. banking system is printed in special magnetic ink using a font called MICR, which stands for "Magnetic Ink Character Recognition." The MICR line, as it is commonly known, typically encodes the following four items: the check number, the bank's routing number, the account number, and the check amount, which is blank when the check is issued. The bank that processes the check after it is deposited encodes the check amount on the MICR line.

Food instruments that will be processed through the commercial banking system must contain a MICR line. MICR encoding errors can occur either when a food instrument is printed (i.e., issued in a print-on-demand system) or when the bank that processes a vendor deposit encodes the check amount on the MICR line of a food instrument. If the State agency is able to determine that a MICR encoding error affects its ability to reconcile a food instrument, then the State agency should be able to identify which MICR field (i.e., the check number, the bank's routing number, the account number, or the check amount) contains the error.

If an error has been made encoding the check number on the MICR line, the State agency should be able to identify the correct check number. This can be accomplished by either examining the upper right corner of the food instrument, where the check number is typically printed, or by identifying the check number through enrollment and/or issuance records, which can be accessed using the participant information on the food instrument. After the check number has been identified, the State agency should be able to enter the correct check number into its system and complete the disposition process electronically, without having to manually match the food instrument to a participant case file. If an error has been made encoding the State agency's bank routing number or account number, the State agency should check with its bank to ensure that the vendor was paid for the food instrument from the proper account. For MICR encoding errors that occur when food instruments are printed, the State agency should investigate the matter to identify the reasons for the errors. For example, the MICR encoding errors may be tracked to a batch of misprinted food instruments or to a local agency's MICR encoding device that needs repair. If specific problems are identified, the State agency should take appropriate actions to limit the recurrence of such errors in the future.

If an error has been made encoding the check amount, the State agency must attempt to identify the correct check amount (i.e., purchase price) of the food instrument. This can be accomplished by examining either the amount entered in

the purchase price space on the face of the food instrument or, if applicable, the transaction amount printed by the cash register on the back of the food instrument. After it has identified the correct check amount, the State agency must a make a price adjustment to the food instrument to ensure the vendor is paid the correct amount for the supplemental foods provided to the participant. After it has made the price adjustment, the State agency should be able to enter the correct check amount into its system and complete the disposition process electronically, without having to manually match the food instrument to a participant case file. For MICR encoding errors that occur when the check amount is entered on food instruments, the State agency should investigate the matter to identify the reasons for the errors. If specific problems are identified, the State agency should take appropriate actions to limit the recurrence of such errors in the future.

F. Vendor Claims

Question 1: Under § 246.12(k)(3), is the State agency required to provide the vendor with an opportunity to justify or correct the five food instrument errors cited in § 246.12(k)(1)?

Answer: Yes. Regulations at § 246.12(k)(3) state: "When payment for a food instrument is delayed or a claim is established, the State agency must provide the vendor with an opportunity to justify or correct the vendor overcharge or other error. If satisfied with the justification or correction, the State agency must provide payment or adjust the proposed claim accordingly." This opportunity must be provided to vendors because regulations at § 246.18(a)(1)(iii)(F) strictly prohibit the State agency from providing vendors with administrative review of "disputes regarding food instrument payments and vendor claims." However, as discussed in the above answer to Question 5 in Section E, the State agency may establish in the vendor agreement that certain errors, such as those listed in § 246.12(k)(1), are "fatal errors" and that food instruments containing such errors will not be paid by the State agency. However, the State agency is still required to provide the vendor with an opportunity to justify or correct such errors.

Question 2: Under § 246.12(k)(2), when a food instrument is submitted by a vendor for redemption above the maximum price, is the State agency required to send a formal written claim letter to the vendor for a pre-edit vendor claim?

Answer: No. Regulations at § 246.12(k)(2) do not require formal written claim letters be sent to vendors. However, in order to provide vendors with an opportunity to justify or correct food instrument errors that give rise to vendor claims, the State agency must provide vendors with notification that errors have occurred and the claim amounts associated with such errors. The vendor agreement should specify what type of notification the State agency will provide vendors regarding vendor claims. A rejected food instrument returned to the vendor may serve as notification if specified as such in the vendor agreement.

Question 3: Under § 246.12(k)(2), is the State agency required to establish vendor claims for inventory discrepancies found during inventory audits?

Answer: Yes. Regulations at § 246.12(k)(2) state in part: "When the State agency determines the vendor has committed a vendor violation that affects the payment to the vendor, the State agency must delay payment or establish a claim. Such vendor violations may be detected through *compliance investigations*, food

instrument reviews, or other reviews and investigations of a vendor's operations" (emphasis added).

Question 4: For sanctions based on compliance buys and/or inventory audits, is the State agency required under §§ 246.12(k)(1)-(k)(4) to issue claims in addition to sanctions, because vendors argue during administrative reviews that as long as they pay claims they cannot be sanctioned and hearing officers sometimes permit vendors to pay claims in lieu of receiving sanctions? If so, how should the State agency address this issue?

Answer: Yes. As discussed in the answer to Question 13 of Section I. below, in addition establishing a vendor claim, the State agency may sanction a vendor in accordance with the State agency's sanction schedule. Vendor claims and vendor sanctions are not mutually exclusive. Payment of vendor claims does not absolve vendors of vendor violations that give rise to vendor sanctions. If a hearing officer suggests that a vendor cannot be sanctioned as long as he pays vendor claims, the State agency should direct the hearing officer's attention to the vendor agreement provision that specifies that in addition to denying payment or assessing a claim, the State agency may sanction the vendor in accordance with the State agency's sanction schedule (§ 246.12(h)(3)(ix)).

Question 5: May a State agency establish administrative fines for vendor overcharges in lieu of imposing vendor claims?

Answer: No. Regulations at § 246.12(h)(3)(ix), *Vendor Claims*, state that when the State agency determines that a vendor has committed a violation that affects the payment to the vendor, the State agency must delay payment or establish a claim in the amount of the full purchase price of each food instrument that contained the vendor overcharges or other error. However, in addition to denying payment or assessing a claim, the State agency may sanction the vendor for vendor overcharges or other errors in accordance with the State agency's sanction schedule.

Vendors who have a pattern of overcharging, as defined by the State agency, are subject to a mandatory sanction, i.e., a three-year disqualification under § 246.12(l)(1)(iii)(C). Section 246.12(l)(2)(i) prohibits the State agency from imposing sanctions for overcharging other than the mandatory sanction prescribed under § 246.12(l)(1)(iii)(C).

G. Vendor Training

Question 1: Under § 246.12(i), may the State agency count toward the interactive training requirement an interactive, onsite preauthorization visit that takes place before the effective date of a vendor agreement?

Answer: Yes, provided the State agency covers the vendor training content required by § 246.12(i)(2) and provides the vendor applicant's representative with a contemporaneous opportunity for questions and answers. If the vendor applicant is subsequently authorized as a vendor, the State agency must document the content of and vendor's participation in the training in accordance with § 246.12(i)(4).

Question 2: If the State agency provides vendor training to a chain store's trainer, does this meet the requirements of § 246.12(i), or is the State agency required to provide vendor training to at least one representative of each vendor (i.e., each chain store location)?

Answer: For the annual training requirement, the State agency must document that it provided training materials (e.g., a newsletter) to each vendor (i.e., each chain store location). For the interactive training requirement, the State agency may provide interactive training to a chain store's trainer, provided the State agency receives documented assurances that at least one representative of each vendor will receive interactive training covering the required content (§ 246.12(i)(2)) during the current year.

Question 3: Under § 246.12(i), may the State agency modify the content of the annual training for vendors that only provide exempt infant formulas to participants and are paid by the State agency without the transaction of food instruments?

Answer: Yes. Although the training topics listed in § 246.12(i)(2) usually apply to all retail vendors, occasionally a State agency will have a contract or other unique arrangement with certain vendors, such as pharmacies, that might make a particular topic irrelevant for a training session with those particular vendors. In the example mentioned above, the pharmacies do not transact WIC food instruments; rather, the State agency orders the exempt infant formula to be provided to the participant. The pharmacy is paid directly by the State agency. In this instance, the State agency would not have to train these vendors on procedures for transacting and redeeming food instruments. Instead, the State agency would

train them on the relevant requirements for filling the State agency's request and receiving payment for formula provided.

In addition, the State agency should tailor a topic such as "minimum varieties and quantities of authorized supplemental foods" to apply only to the items that the pharmacies are expected to provide. This might include a review of approved exempt formulas and the quantities that participants generally require on a monthly basis, based on recent data. By starting with the training agenda in § 246.12(i)(2) and tailoring the content to fit the type of vendors being trained, the State agency complies with the regulations and provides training that is relevant to vendors.

H. Vendor Monitoring

Question 1: There appears to be a conflict in the regulations between § 246.12(j)(1), which allows the State agency to delegate vendor monitoring to a local agency or contractor if the State agency indicates its intention to do so in its State Plan, and § 246.12(j)(2), which states that the State agency must conduct routine monitoring visits. May the State agency delegate routine monitoring to another State agency?

Answer: Yes, provided the other State agency is acting as a contractor. During routine monitoring visits, a contractor must follow the contracting State agency's rules and procedures and also use its food instruments. Nevertheless, we strongly recommend that routine monitoring be conducted by the State agency or delegated to its local agencies. During the comment process on the proposed rule, many State agencies indicated that routine monitoring serves several important program purposes, including surveying the types of errors that occur during food instrument transactions, preventing such errors in the future through vendor training, and strengthening relationships between vendors and the State or local agency by having a presence in their stores. For these reasons, a vast majority of State agencies that commented on the proposal supported retaining a routine monitoring requirement. For routine monitoring to be effective in strengthening relationships between State/local agencies and vendors, it has to be conducted by State or local agency personnel.

Question 2: Under § 246.12(j)(2), may the State agency count compliance buys conducted on non-high-risk vendors or those conducted above the 5% compliance investigation requirement towards its routine monitoring requirement?

Answer: No. The routine monitoring requirements in § 246.12(j)(2) and the compliance investigation requirements in § 246.12(j)(4) are totally separate requirements. A vast majority of those who commented on the proposed rule opposed the 10% compliance investigation requirement, because of the program costs that would be necessary to meet the proposed requirement, and also opposed eliminating the routine monitoring requirement, because routine monitoring serves an important program purpose. Some commenters indicated that routine monitoring is a preventative measure that helps the State agency build positive relationships with its vendors, whereas compliance investigations are a punitive measure that result in adversarial relationships with vendors. In its comment letter, the National Association of WIC Directors suggested that the proposal be modified so that 10% of vendors are monitored with at least half subject to

compliance investigations. We accepted this compromise but revised it to establish separate 5% requirements for routine monitoring and compliance investigations to ensure that the vendor monitoring requirements maintain a balanced approach. These monitoring requirements are minimum requirements; the State agency may exceed them as it deems appropriate.

Question 3: Clarify what exactly is required by § 246.12(j)(4)(i) with regards to an Indian Tribal Organization (ITO) State agency counting compliance investigations conducted by a geographic State agency?

Answer: If the geographic State agency is acting as a contractor, the ITO State agency may count its contractor's compliance investigations, which must be conducted in accordance with the ITO State agency's rules and procedures and use its food instruments. In addition, the contractor's investigators must be available to testify during administrative or judicial review proceedings regarding vendor sanctions that result from violations detected during such compliance investigations. If the geographic State agency is not acting as a contractor, the following two conditions must be met for an ITO State agency to count compliance investigations conducted by a geographic State agency on shared vendors. First, the ITO State agency must establish a State agency sanction in accordance with § 246.12(l)(2)(iii). Second, the ITO State agency and the geographic State agency must enter into an information-sharing agreement that addresses how the geographic State agency will provide the ITO State agency with information and documentation regarding the compliance investigations conducted on and mandatory sanctions imposed upon shared vendors.

Question 4: Under § 246.12(j)(4), may the State agency count a compliance investigation conducted by another State agency on a non-high-risk vendor toward its 5% compliance investigation requirement?

Answer: Yes, provided the following three conditions are met. First, the State agency has identified less than 5% of its vendors as high-risk vendors. Second, the State agency has a State agency sanction in accordance with § 246.12(l)(2)(iii). Third, the two State agencies have an information-sharing agreement regarding compliance investigations and mandatory sanctions of shared vendors. If these conditions are met, the State agency may count compliance investigations conducted by another State agency on non-high-risk vendors as investigations conducted on randomly selected vendors as permitted under § 246.12(j)(4)(ii).

Question 5: If during a compliance buy the vendor refuses to participate in the transaction (i.e., does not traffic or sell an unauthorized item), may the State agency still count the attempted transaction toward the 5% compliance investigation requirement (and on the TIP report)?

Answer: Yes, provided the compliance investigator documents the attempted transaction in accordance with § 246.12(j)(6).

Question 6: If a State agency conducts a review of a vendor's redeemed food instruments and the vendor's receipts (not inventory records) and imposes a sanction against the vendor based on this review, may the State agency count this review toward the required 5% compliance investigation requirement?

Answer: Yes, provided reviews of redeemed food instruments and vendor receipts provide sufficient evidence to support the imposition of mandatory sanctions against vendors. However, when such a review does not result in the imposition of a vendor sanction, the State agency must conduct compliance buys or an inventory audit to complete its compliance investigation in accordance with § 246.12(j)(4).

Question 7: Under § 246.12(j)(4), may the State agency count toward its 5% compliance investigation requirement compliance buys conducted by the Food Stamp Program (FSP) Compliance Branch that do not use WIC food instruments?

Answer: No. The State agency may only count compliance investigations conducted by the FSP Compliance Branch when WIC food instruments are used. Although we strongly encourage the State agency to coordinate its compliance efforts with its FSP counterparts, this coordination should focus on the efficient use of the limited resources available for compliance activities. For example, if the FSP Compliance Branch intends to investigate a retailer that has been identified as a high-risk vendor in the WIC Program, rather than investigating that vendor, the State agency should select another high-risk vendor on which to conduct a compliance investigation.

Question 8: Food Stamp Program (FSP) documentation requirements regarding compliance buys differ from WIC Program requirements. What does the State agency need to do to count a WIC compliance investigation conducted by the FSP Compliance Branch toward the 5% compliance investigation requirement?

Answer: For the State agency to count a compliance investigation conducted by the FSP Compliance Branch toward its 5% compliance investigation requirement, the following two conditions must be met. First, the State agency must obtain a copy of the FSP documentation of a completed compliance investigation in which FSP investigators used WIC food instruments during the compliance investigation. Second, the State agency either has identified the vendor as a high-risk vendor or has identified less than 5% of its vendors as high-risk vendors.

Question 9: Define what a "Federal, State, and local law enforcement agency" refers to in § 246.12(j)(4)(i)?

Answer: Generally, Federal, State, and local law enforcement agencies are those that enforce laws through the investigation and prosecution of violators. Federal law enforcement agencies include the USDA Office of the Inspector General, the Secret Service, the Federal Bureau of Investigations, the Internal Revenue Service, and the Justice Department. State and local law enforcement agencies include State and local police departments and State Attorneys' General, district attorneys', and local prosecutors' offices.

Question 10: Under § 246.12(j)(4)(i), do law enforcement agencies have to use WIC food instruments during their investigations of high-risk vendors for the State agency to count such investigations toward its compliance investigations requirement?

Answer: Yes, generally law enforcement agencies must use WIC food instruments during their investigations for the State agency to count the investigation toward its 5% compliance investigations requirement. However, in situations in which law enforcement authorities do not use WIC food instruments but their investigations provide sufficient evidence to support either the imposition of vendor sanctions or the termination for cause of vendor agreements, the State agency may seek approval from its FNS regional office to count such investigations toward its compliance investigations requirement.

Question 11: How does the State agency conduct vendor monitoring on military commissaries when nonmilitary personnel are neither permitted to enter commissaries nor transact food instruments?

Answer: As noted in the first paragraph of the answer to Question 3 of Section E, FNS has a Memorandum of Understanding (MOU) with the Department of Defense regarding military commissaries as WIC Program vendors. Under the MOU, the State agency is prohibited from conducting on-site monitoring reviews (i.e., compliance buys and routine monitoring visits) of commissaries, "except

upon invitation by the constituted military authority." However, the MOU permits the State agency to review food instruments submitted for redemption by commissary vendors prior to payment. If food instruments are found to contain errors or omissions, payment may be denied unless or until further justification or correction is provided by the submitting commissary. If the State agency identifies a possible problem, it should write the commanding officer of the installation requesting repayment, investigation, or other appropriate action. The commanding officer or his/her designee must take necessary action and promptly reply to the State agency, including repayment if appropriate. If the State agency wishes to further pursue problem resolution, it should refer the case to its FNS regional office. Since commissary vendors are not subject to on-site monitoring reviews, the number of commissary vendors may be subtracted from the State agency's total number of vendors when calculating the 5% routine monitoring and compliance investigation requirements.

Question 12: How does FNS recommend the State agency conduct compliance investigations in remote areas, where everyone knows everyone else?

Answer: In areas where the State agency determines that compliance buys would be ineffective, we recommend that the State agency conduct inventory audits to determine whether the vendors' redemptions are consistent with their documented inventories of supplemental foods.

Question 13: Regulations at § 246.12(j)(4) provide that a compliance investigation may be closed when two compliance buys are conducted in which no program violations are found. Often, the first two compliance buys of a compliance investigation find only minor violations of the vendor agreement, which do not warrant further compliance buys. Does the State agency have the discretion to close a compliance investigation when no serious vendor violations that would trigger a mandatory sanction are found during the first two compliance buys?

Answer: Yes, the State agency may consider a compliance investigation complete when two compliance buys have been conducted in which no serious vendor violations that would trigger a mandatory sanction are detected. Although compliance investigations typically are targeted to test vendors' willingness to commit serious vendor violations, we understand that minor violations also may be detected during compliance investigations. In our references to "no program violations" in §§ 246.12(j)(4)(i) and (j)(4)(ii), our intent was that the State agency be able close a compliance investigation if no serious vendor violations are detected during two compliance buys.

Question 14: May a State agency use as high-risk criteria the number of participant complaints and a designated number of accumulated sanction points?

Answer: Yes. Regulations at § 246.12(j)(3) allow a State agency to use such criteria ***in addition to*** the FNS criteria. However, any criteria that a State agency uses in lieu of the FNS criteria must be statistically based. Neither the number of participant complaints nor the number of sanction points accumulated is a statistically-based criterion. Non-statistically-based State criteria used in conjunction with FNS criteria also should be fair (i.e., do not unfairly target any particular group of vendors) and have a logical association with a vendor's risk status. All State agency-developed criteria must be approved by FNS.

Question 15: Can a State agency supply WIC food instruments and WIC identification (ID) cards/folders to the Office of the Inspector General (OIG) for use in conducting compliance investigations?

Answer: Yes. The State agency should provide food instruments and ID cards or folders to the OIG for the purpose of conducting compliance investigations. We believe it is in the interest of the State agency to cooperate with an OIG investigation of potential WIC fraud or abuse. Findings from an investigation could assist the State agency to sanction an abusive vendor. In addition, under section 246.12(j)(4) of the regulations a State agency may count the OIG investigation of a high-risk vendor toward meeting the minimum requirement for compliance investigations.

I. Vendor Violations and Sanctions

Question 1: Under § 246.2, why is there a distinction with respect to intent between a participant violation and a vendor violation?

Answer: As noted in the first paragraph of the WIC Program's authorizing legislation (42 U.S.C. 1786, Section 17(a)), improving the health of program participants is paramount to the mission of the WIC Program. A vast majority of participants are infants and children, who are unable to commit program violations. Disqualifying these participants for unintentional program violations committed by their parents, caretakers, or proxies would significantly compromise the mission of the Program. Similarly, we believe that disqualifying pregnant, postpartum, and breastfeeding women participants for unintentional program violations would also compromise the mission of the Program. Consequently, we clarified in § 246.2 that a participant violation is "any intentional action of a participant, parent or caretaker of an infant or child participant, or proxy that violates Federal or State statutes, regulations, policies, or procedures governing the Program." This definition is consistent with program legislation at 42 U.S.C. 1786, Section 17(f)(14), which requires participant claims only in cases of intentional program violations.

Studies have shown that each year vendor violations, whether intentional or not, result in the loss of tens of millions of dollars of program funds. Because WIC is a grant program, such losses mean that fewer participants may be served. As discussed in the preamble to the WIC/FSP Vendor Disqualification final rule (64 FR 13315-13316), vendor sanctions are not criminal; they are imposed in order to protect the integrity of the WIC Program. If stores consistently overcharge customers for purchases, customers take their business elsewhere regardless of whether the overcharges are intentional or inadvertent. Likewise, the WIC Program should not tolerate vendors whose practices repeatedly result in direct losses to the Program. To address the vendor community's concerns about receiving sanctions based on a single, inadvertent error committed by a cashier, we require a pattern of violations to trigger most mandatory sanctions.

Vendors are not program participants. Rather, vendors are authorized to provide program benefits to participants. Consequently, program requirements for vendors differ from those for participants. Whereas a pattern of violations, whether intentional or not, is required to trigger most mandatory vendor sanctions, a single, intentional violation is required to trigger a mandatory participant sanction. We believe this distinction is consistent with the mission of the WIC Program.

Question 2: How may the State agency prohibit vendors from giving diapers and other incentive items to participants to entice them to shop at their stores?

Answer: WIC regulations do not give State agencies clear authority to prohibit vendors from providing incentive items to participants. FNS will seek to establish authority via regulations for State agencies to prohibit vendors from providing incentive items solely to WIC participants, because this has been a recurring issue. State agencies that are concerned about the impact of incentives on WIC food costs should establish appropriate price limitations in accordance with § 246.12(g)(3) of the WIC regulations to ensure that only the actual costs of foods are paid through the WIC Program. Vendors whose prices are not within established limits risk losing WIC authorization.

Question 3: Under § 246.12(h)(5), is the State agency required to include all vendor sanctions in its sanction schedule or is the State agency only required to include the mandatory sanctions specified in §§ 246.12(l)(1)(i)-(l)(1)(iv)? Requiring all vendor sanctions be included in the sanction schedule would remove all State agency flexibility, when experience has taught us that no two cases are alike.

Answer: Yes. The State agency must include all vendor sanctions in its sanction schedule. Regulations at § 246.12(l)(2) state in part: "The State agency may impose sanctions for vendor violations that are not specified in paragraphs (l)(1)(i) through (l)(1)(iv) of this section as long as such vendor violations and sanctions are included in the State agency's sanction schedule." To prevent the occurrence of vendor violations, vendors must be aware of what actions the State agency considers to be vendor violations and what the penalties are for committing such violations.

Question 4: Under § 246.12(h)(5), is the State agency required to identify in its sanction schedule the "pattern" of vendor violations necessary to trigger a sanction?

Answer: No. The State agency is not required by Federal regulations to identify the patterns of violations used to trigger sanctions, because this information represents a significant aspect of the State agency's investigative techniques. Generally, the State agency's use of patterns is based on the severity, frequency, and nature of the vendor violations. Typically, the patterns of violations will provide sufficient evidence to uphold the State agency's sanctions upon administrative review. We recommend that the State agency seek legal counsel

from its State's Attorney General's or General Counsel's office prior to identifying in its sanction schedule the patterns used to trigger sanctions.

Question 5: Under § 246.12(l)(1)(iii)(C), may the State agency establish more than one pattern to substantiate a sanction for vendor overcharges (e.g., one pattern of two incidences of vendor overcharges of $1.00 or more and a second pattern of six incidences of vendor overcharges of less than $1.00)?

Answer: Yes. As noted in the *Overcharging* section of the preamble to the WIC/Food Stamp Program Vendor Disqualification final rule (64 FR 13315, 3/18/99), "… the evidence necessary to establish a pattern is influenced by both the severity and number of the incidences of a violation." The *Mandatory WIC Vendor Sanctions* section of the preamble (64 FR 13314) provides the following example: "… if a vendor overcharged $20 on a gallon of milk, the number of incidences required to demonstrate a pattern of the violation would be less than for a vendor who overcharged 5¢ on a gallon of milk. It is therefore left to the discretion of the State agency to determine the number of incidences that reflect a pattern, based on the type and severity of violation."

Although the State agency may establish multiple patterns for substantiating a sanction, the State agency is prohibited under § 246.12(l)(2) from establishing State agency sanctions that set lower thresholds for the same violations covered by the mandatory sanctions in § 246.12(l)(1). The *Routine Monitoring and Compliance Investigations* section of the preamble to the WIC Food Delivery Systems final rule further states: "In situations in which the State agency is unable to establish the level of evidence necessary to support a sanction, we recommend that the State agency issue a warning to the vendor identifying the vendor violations found and recommending corrective actions, such as additional training. Providing the vendor with a warning that violations are occurring puts the vendor on notice and also provides support for sanctions in the event that additional violations are uncovered during future compliance investigations" (65 FR 83268).

Question 6: Under § 246.12(l)(2), if the State agency disqualifies a vendor for a State agency-established sanction, is the State agency required to terminate the vendor agreement?

Answer: Yes. Regulations at § 246.12(l)(9) require that "when the State agency disqualifies a vendor, the State agency must also terminate the vendor agreement." This provision applies to both mandatory and State agency-established sanctions that result in the disqualification of a vendor. During disqualification periods, stores are not authorized to transact and redeem food instruments. It is through termination of the vendor agreement that the State agency formally terminates a

store's vendor authorization and prohibits it from transacting and redeeming food instruments.

Regulations at § 246.12(h)(3)(xxi) further clarify that "… the vendor will have to reapply in order to be authorized after the disqualification period is over. In all cases, the vendor's new application will be subject to the State agency's vendor selection criteria and any vendor limiting criteria in effect at the time of the reapplication." As noted in section 2.d. of the preamble to the WIC Food Delivery Systems final rule (65 FR 83251), the State agency may develop a streamlined system for accepting reapplication information, provided the system ensures that stores provide updated information regarding the vendor selection criteria and their current ownership and management.

Question 7: Under § 246.12(l), may a vendor be disqualified when its management and the State agency are working together on an investigation? For example, the State agency provides food instruments to the vendor at the request of its management to conduct in-house investigations. During an in-house investigation, a cashier commits a serious vendor violation, and the vendor terminates the cashier's employment.

Answer: No. Unlike compliance investigations conducted by program representatives, in-house investigations are conducted by vendor representatives, who are not in the position to testify against their employers to support the imposition of vendor sanctions. Like routine monitoring, in-house investigations are a preventative measure taken by vendors to improve their program compliance. The purpose of in-house investigations is for the *vendor* to survey the types of food instrument errors and vendor violations that occur during WIC transactions and to take appropriate actions to reduce the number of such errors and violations in the future. Although in-house investigations serve a similar program purpose as routine monitoring visits, in-house investigations may not be counted by the State agency toward its 5% routine monitoring requirement.

Question 8: A formal definition of trafficking is not included in § 246.2. How is trafficking defined?

Answer: Trafficking is a general term used to describe the commercial exchange of goods. However, the term is also used to refer to the illegal commercial exchange of goods (e.g., trafficking in drugs or stolen property). Although the term "trafficking"is not included in § 246.2, it has been commonly used in the WIC Program for years to refer to the illegal exchange of food instruments for cash. Under § 246.12(l)(1)(ii)(A), the term "trafficking" is used parenthetically to

refer to "buying or selling food instruments for cash," which also reflects the term's meaning in § 246.12(l)(1)(i).

Question 9: Under § 246.12(l), may a vendor be disqualified for a vendor violation committed by a cashier while on his/her break or after work? For example, the cashier tells the compliance investigator to meet her/him in the parking lot during his/her break or at the end of his/her shift. While off duty in the parking lot, the cashier provides cash to the investigator in exchange for food instruments. Trafficking occurred, but it was not in the store and it was on the cashier's own time.

Answer: As always, vendor sanctions must be based on evidence. Whether a State agency may sanction a vendor for violations committed by employees on breaks, after work, or off premises will depend on whether the evidence is sufficient to uphold a vendor sanction upon administrative or judicial review. Consequently, we recommend that the State agency seek advice from its Attorney General or General Counsel's office on a case-by-case basis to determine if the level of evidence collected during a compliance investigation is sufficient to support a vendor sanction. In some cases, the State agency may have imposed vendor sanctions for such violations in the past, and precedents have been established as to the level of evidence necessary to support various vendor sanctions.

Some vendor violations that trigger mandatory sanctions (e.g., overcharging or charging for supplemental foods not received) cannot occur outside of a WIC transaction. Other vendor violations, especially trafficking, may occur anywhere. Whenever a vendor's owners, officers, or managers commit vendor violations that warrant a mandatory sanction, regardless of when or where such violations occur, the State agency must sanction the vendor. When an employee (e.g., a non-managerial cashier) commits violations on the vendor's premises (i.e., in the store or its parking lot) that warrant a mandatory sanction, we believe the State agency also must sanction the vendor. However, to address situations in which an employee commits violations off premises, we believe the appropriate action is to send the vendor a warning letter indicating that one of its employees has committed the following vendor violations and that such violations may affect the vendor's continued authorization in the Program. In addition, when appropriate, the State agency should refer the employee to Federal, State, or local authorities for prosecution under applicable laws.

Question 10: On occasion, a cashier commits a serious vendor violation during a compliance buy, but for some reason (e.g., the vendor suspects the transaction was a compliance buy), the vendor never submits the food instrument for redemption. May the State agency impose a sanction under § 246.12(l) based on a vendor violation committed during a transaction for which the vendor never submits the food instrument for redemption?

Answer: Yes, except for the overcharging and the charging for supplemental foods not received violations, which require the vendor to submit the food instruments for redemption to substantiate the violations. Most of the other violations that trigger mandatory sanctions only require that the vendor provide unauthorized items (e.g., cash, credit, alcohol or tobacco products, non-food items, or unauthorized food items) in exchange for food instruments to commit the violation. These violations occur at the time of the vendor exchanges the unauthorized items for food instruments rather than at the time the vendor submits the food instruments for redemption.

Question 11: During a compliance investigation, the vendor overcharges $0.50 during the first compliance buy, undercharges $1.00 during the second compliance buy, and does not commit a vendor violation during the third compliance buy. Under § 246.12(l)(1)(iii)(C), what discretion does the State agency have regarding the detection of vendor overcharges and the imposition of mandatory sanctions?

Answer: In order to sanction a vendor under § 246.12(l)(1)(iii)(C), the State agency must establish a pattern of overcharging to trigger the three-year, mandatory sanction. The above example of only one overcharge violation does not provide sufficient evidence to trigger a mandatory sanction for a pattern of overcharging. Regulations at §§ 246.12(j)(1)(i) and (j)(1)(ii) permit the State agency the discretion to consider a compliance investigation complete "when two compliance buys have been conducted in which no program violations are found." Consequently, the State agency may close the investigation in the above example because undercharging is not a vendor violation. Depending on the type of overcharging detected, the State may want to issue a warning to the vendor. For example, if the vendor failed to enter the purchase price at the time of the transaction, then submitted the food instrument for redemption with the $0.50 vendor overcharge, the State agency may want to warn the vendor about both the overcharge violation and the violation of the State agency's purchase price procedures. Such warnings put vendors on notice that vendor violations have been detected and to take corrective actions to prevent such violations. In addition, warnings may be used to support future sanctions when subsequent compliance investigations detect continued program noncompliance.

Question 12: If an item is accidentally scanned twice, is the vendor violation a vendor overcharge or an incidence of charging for supplemental food not received by the participant?

Answer: The type of vendor violation committed by a vendor is always based on the evidence. In this case, the type of vendor violation depends not only on what the vendor charged the Program but also on what supplemental foods were obtained by the participant. If the vendor submits a food instrument for redemption that includes a supplemental food item that was neither listed on the food instrument (e.g., in excess of the quantity listed on the food instrument) nor obtained by the participant, then the vendor has committed a vendor overcharge (§ 246.12(l)(1)(iii)(C)), which would be consistent with a cashier accidentally scanning an item twice. However, if the participant obtained the excess supplemental food item, then the vendor has committed a vendor violation of providing unauthorized food items in exchange for food instruments (§ 246.12(l)(1)(iv)), because this vendor violation includes charging for supplemental food items provided in excess of those listed on the food instrument. Further, if the participant was authorized to receive a particular quantity of a supplemental food (e.g., 12 cans of infant formula) and obtains fewer items (e.g., 11 cans of infant formula) and the vendor submits the food instrument for redemption charging the Program for the total authorized quantity (e.g., 12 cans of infant formula), then the vendor has committed a vendor violation of charging for supplemental foods not received by the participant (§ 246.12(l)(1)(iii)(E)).

Question 13: During a compliance investigation, the vendor commits vendor overcharges, and after the vendor submits the food instruments for redemption, the State agency makes price adjustments to the food instruments. If the State agency imposes a sanction on the vendor for the vendor overcharges the vendor's attorney argues during the administrative review that the State agency already corrected the errors by making price adjustments; therefore, there is no reason to sanction the vendor. Is the State agency precluded from imposing a sanction when it makes price adjustments to food instruments or allows the vendor an opportunity to justify or correct food instruments that contain vendor overcharges?

Answer: First of all, we want to clearly distinguish the term "price adjustment" from the term "vendor claim." When a vendor, *in accordance with the vendor agreement*, submits a food instrument for redemption that exceeds the State agency's price limitations, the action taken by the State agency to adjust the purchase price of the food instrument so it complies with the appropriate price limitation is a *price adjustment*. This action, which was required by the William

F. Goodling Act of 1998 (P.L. 105-336), ensures that vendors do not raise their prices to levels that would otherwise make them ineligible for vendor authorization. The amount of a price adjustment corresponds to the amount the vendor charged above the maximum price allowed under the State agency's price limitations and does not necessarily correspond to the amount of a vendor overcharge.

Conversely, when a vendor, *in violation of the vendor agreement*, submits a food instrument for redemption that contains a vendor overcharge, the action taken by the State agency in response to the vendor overcharge is a vendor claim. Regulations at § 246.12(h)(3)(ix), which specify the federal requirements for all vendor agreements, state: "When the State agency determines the vendor has committed a vendor violation that affects the payment to the vendor, the State agency will delay payment or establish a claim. The State agency may delay payment or establish a claim in the amount of the full purchase price of each food instrument that contained the vendor overcharge or other error. The State agency will provide the vendor with an opportunity to justify or correct a vendor overcharge or other error. The vendor must pay any claim assessed by the State agency. In collecting a claim, the State agency may offset the claim against current and subsequent amounts to be paid to the vendor. *In addition to denying payment or assessing a claim, the State agency may sanction the vendor for vendor overcharges or other errors in accordance with the State agency's sanction schedule*" (emphasis added).

Payment of a vendor claim, even through a pre-edit offset, does not absolve the vendor of the vendor overcharge violation. Vendor claims and vendor sanctions are not mutually exclusive. Payment of vendor claims should act as a warning to the vendor that it has committed vendor violations and needs to take corrective action to eliminate such violations in the future. In situations in which vendor claims are assessed through denial of payment (i.e., returning rejected food instruments to vendors) by a pre-edit system, we strongly recommend that the State agency issue a formal warning to the vendor that vendor overcharges have been detected and that continued noncompliance may result in a vendor sanction.

The argument that paying claims or fines absolves one from violations or crimes is not a valid argument. Drivers who pay fines for speeding still receive points against their licenses in accordance with the schedule established for such violations, and when a driver's accumulated points exceed a certain threshold, his or her driver's license is revoked. In the same manner, a vendor that commits vendor overcharges must pay its vendor claims to continue its authorization; however, when the State agency establishes a pattern of vendor overcharges, the

State agency must sanction the vendor in accordance with the vendor agreement's sanction schedule.

Question 14: Under § 246.12(l), in addition to disqualifying a vendor's owner, may the State agency disqualify a store location?

Answer: No. Under § 246.12(l), sanctions are imposed against a vendor, which is accountable for the vendor violations committed its owners, officers, managers, agents, and employees. As indicated in § 246.12(h)(3)(xxi), a vendor agreement is not a license or property interest that can be sold or transferred. Accordingly, a vendor sanction is only associated with a vendor and is not associated with a property or store location. In the event the store is sold, the new owner may not be prevented from applying for vendor authorization. However, if the State agency determines that the store was sold by its previous owner in an attempt to circumvent a vendor sanction, the State agency is required under § 246.12(g)(5) to deny vendor authorization to the new owner.

Question 15: Under § 246.12(l), may a new store owner pay a previous owner's civil money penalty to avoid the previous owner's sanction?

Answer: No. The civil money penalty is only associated with the previous owner. When the store is sold, the previous owner's vendor agreement must be terminated, because a vendor agreement is not a license or property interest that can be sold or transferred (§ 246.12(h)(3)(xxi)). To become a vendor, the current owner must apply for vendor authorization. Unless the State agency determines that the store was sold by its previous owner in an attempt to circumvent a vendor sanction, the sanction imposed against the previous owner should not affect the new owner's ability to receive vendor authorization.

Question 16: Under § 246.12(u)(5), "when appropriate," the State agency must refer vendors, home food delivery contractors, and participants who violate program requirements to Federal, State, or local authorities for prosecution under applicable statutes. What guidance can FNS provide the State agency to assist in determining when such cases must be referred to law enforcement authorities?

Answer: Regulations at § 246.23(d) state: "*Penalties*. In accordance with section 12(g) of the National School Lunch Act, whoever embezzles, willfully misapplies, steals or obtains by fraud any funds, assets or property provided under section 17 of the Child Nutrition Act of 1966, as amended, whether received directly or indirectly from USDA, or whoever receives, conceals or retains such funds, assets or property for his or her own interest, knowing such funds, assets or property

have been embezzled, willfully misapplied, stolen, or obtained by fraud shall, if such funds, assets, or property are of the value of $100 or more, be fined not more than $10,000[1] or imprisoned not more than five years, or both, or if such funds, assets or property are of a value of less than $100, shall be fined not more than $1,000 or imprisoned for not more than one year, or both." This provision establishes $100 of program funds as the threshold between a misdemeanor and a felony. However, State and/or local laws regarding fraud and abuse committed against Federal programs vary widely.

We recommend that the State agency seek advice from its State's Attorney General or General Counsel's office regarding thresholds of program loss and types of evidence necessary to seek prosecution under applicable State laws. In addition, we recommend that local agencies seek similar advice from local prosecutors about applicable local laws. If during the course of a WIC Program investigation, information is developed that indicates fraud and abuse in excess of $1,000 or other major criminal activity, including large scale vendor trafficking in food instruments, firearms or narcotics, or involvement by organized crime elements, the State agency should immediately advise its FNS regional office, which will refer the case to the appropriate USDA Office of the Inspector General (OIG) regional office. In such cases, the State agency should hold further investigative action in abeyance, pending USDA OIG action. In such instances, the FNS regional office will notify the State agency of whether USDA OIG intends to assume the investigation. If USDA OIG does not assume the investigation, the State agency should refer the case to State and/or local law enforcement authorities for investigation and/or prosecution under applicable State or local laws.

Question 17: Must the State agency wait until all appeal actions have been taken and resolved before taking adverse action against a vendor?

Answer: No. The Child Nutrition Act of 1966, 42 U.S.C. 1786, Section 17(o)(2)(B) and Section 246.18(a)(2) of the regulations require the State agency to make denials of authorization and permanent disqualifications imposed under § 246.12(l)(1)(i) for trafficking convictions effective on the date of receipt of the notice of adverse action. The State agency must make all other adverse actions effective no earlier than 15 days after the date of the notice of adverse action and no later than 90 days after the date of the notice of adverse action or, in the case of an adverse action that is subject to administrative review, no later than the date the vendor receives the review decision. Reciprocal WIC disqualifications based on a

[1] FNS is revising the regulations to reflect a legislative change that increased the maximum penalty to $25,000. Final WIC Policy Memorandum #2002-7 instructs State agencies to begin applying the new penalty limit now.

FSP disqualification are not subject to administrative or judicial review under the WIC Program as stated in § 246.12(l)(1)(vii).

Question 18: Under § 246.12(l)(1)(v) and (vi), may the State agency apply a second, third or subsequent mandatory sanction for a period that exceeds the term of the vendor's agreement?

Answer: Yes. The second, third and subsequent mandatory sanction provisions are not restricted to a single agreement period, and depending on the type of violation, may extend well beyond the length of the vendor agreement. These provisions are intended to serve as a strong deterrent to fraudulent and abusive behavior by vendors.

Question 19: May a State agency sanction a vendor based on denial of authorization under the Food Stamp Program (FSP) due to lack of business integrity or other reasons?

Answer: No. Being denied authorization by the FSP is not a vendor violation in the WIC Program. However, if the State agency has established FSP authorization as a selection criterion, denial of FSP authorization would mean that the vendor does not qualify for WIC authorization. Section 246.12(h)(3)(xxiv) requires the vendor to comply with the vendor selection criteria, and any changes to the criteria, throughout the agreement period. Consequently, although a WIC State agency may not sanction a vendor for a FSP denial, the State agency may terminate the vendor agreement for cause when a vendor no longer meets selection criteria.

Question 20: May a State agency use a formula other than that contained in § 246.12(l)(1)(x) to calculate the amount of a civil money penalty (CMP)?

Answer: A State agency must use the formula in § 246.12(l)(1)(x) to calculate the amount of a CMP imposed in lieu of a disqualification for a violation that is subject to a mandatory sanction. The State agency may use a different formula to calculate the amount of a CMP for a State-established sanction. However, as indicated in § 246.12(l)(2)(i), the amount of the CMP may not exceed $10,000 for each violation and $40,000 for violations investigated as part of a single investigation.

Question 21: Can a State agency establish a policy requiring vendors to purchase infant formula only from licensed wholesalers and retailers?

Answer**:** The WIC regulations do not prohibit this practice. FNS is aware that State agencies are seeking various means to deter the theft and potential resale of infant formula through the WIC Program. The theft and resale of formula is a law enforcement issue. However, a State agency may take reasonable steps toward ensuring that authorized vendors only purchase supplemental foods, including infant formula, from legitimate sources. FNS advises that a State agency planning to establish a policy in this area work with the State Attorney General or General Counsel's office.

Question 22: Can vendors transact WIC food instruments outside of the authorized retail location?

Answer: No, vendors must transact WIC food instruments within the store. Several State agencies have raised this question in connection with the delivery of supplemental foods to participants' homes. Vendors that offer delivery services for customers may deliver WIC foods after the transaction has been completed in the store. The delivery is not a part of the WIC transaction; and the WIC Program bears no responsibility for the customer's use of delivery services or associated costs.

Several provisions of the WIC Food Delivery Systems rule indicate that WIC transactions in retail purchase food delivery systems are inherently in-store transactions. These include the following:

(a) The regulations differentiate between a retail food delivery system, home delivery system, and a direct distribution system. Each system represents a distinct means of providing supplemental foods to WIC participants. Although a State agency might use more than one type of food delivery system at the same time, the operational requirements and procedures for each system remain separate and distinct.

(b) A vendor is authorized by the vendor agreement to provide supplemental foods in a specific store location, and only in that location. The vendor also receives training to perform in-store transactions only. Thus, vendor personnel may not arbitrarily decide to operate as a home food delivery system contractor by transacting food instruments in a participant's home.

(c) Location is critical to vendor selection. Therefore, a change in location will result in termination of the vendor agreement under §246.12(h)(3)(xvii) of the WIC regulations, unless the State agency determines that the change in location qualifies as a short distance and is permissible.

State agencies have the discretion to include in the vendor agreement a requirement that the vendor must transact WIC food instruments inside the authorized store location, along with a sanction for violation of this requirement. The mandatory sanction in § 246.12(l)(iii)(D) of the regulations for a pattern of receiving, transacting and/or redeeming food instruments outside of authorized channels would apply to violations of this provision in the vendor agreement.

J. Administrative Review of State Agency Actions

<u>Question 1</u>: How do Federal regulations impact State administrative procedures acts (State APAs) when there is a conflict between them? For example, although § 246.18(e) requires that State agency administrative review procedures must provide that review decisions under both the full and abbreviated review procedures are the final State agency action, some State APAs grant more than one level of State administrative review.

<u>Answer</u>: Generally, where there is a conflict between Federal and State or local laws, the Federal law has supremacy over the State or local law, meaning the State or local law as written is void on its face and unenforceable. Federal law includes not only Federal legislation and statutes but also program regulations. Regulations at § 246.3(c)(1) state: "Each State agency desiring to administer the Program shall annually submit a State Plan and enter into a written agreement with the Department for administration of the Program in the jurisdiction of the State agency in accordance with the provisions of this part." If the State agency identifies a conflict between its State APA and program regulations at § 246.18(e), the State must comply with the program regulations as written, since its procedures are void and unenforceable pursuant to the Supremacy Clause of the U.S. Constitution. Further, the State should seek to amend its State APA to comply not only with Federal law but also its Federal/State agreement.

Before amending its State APA, the State agency should examine its State's administrative review system to determine whether the multiple levels of review represent separate administrative reviews or simply a process of approving its review decisions. For example, some States have administrative review processes that permit vendors to immediately appeal a review decision, prior to the issuance of a written review decision, to a higher level for concurrence. This higher-level review only consists of a reexamination of the review decision and the evidence presented during the administrative review and *does not* provide for another administrative review in which the State agency and vendor must present witnesses and evidence again. This type of higher level review is permissible under § 246.18(e), provided that: (1) only one written review decision is issued; (2) the written review decision is the final State agency action; and (3) the written review decision is issued within the 90-day timeframe required by § 246.18(c)(3).

Question 2: The administrative review procedures in § 246.18 only refer to "vendors," does this mean that vendor applicants with no previous WIC authorization history have no rights to administrative review for denials of authorization?

Answer: No. All vendor applicants, whether previously authorized vendors or not, are entitled to an administrative review for denials of authorization under § 246.18(a)(1).

Question 3: Previous regulations at § 246.12(f)(2)(xxiii) provided that the vendor agreement is "null and void" if the ownership changes, which meant the vendor was not entitled to an administrative review, because the State agency did not take an adverse action against the vendor (i.e., terminate the vendor agreement for cause), rather the ownership change simply rendered the vendor agreement null and void. Instead of the previous "null and void" provision, why does § 246.12(h)(3)(xvii) require the State agency to terminate the vendor agreement for a change in vendor ownership or location or a cessation of business? Further, why does § 246.18(a)(1)(ii)(E) provide vendors with an administrative review for termination of a vendor agreement because of such changes?

Answer: A majority of those who commented on the WIC Food Delivery Systems proposed rule recommended changes to proposed § 246.12(h)(3)(xvii) because it did not reflect actual business practices. Commenters from both State agencies and the vendor community indicated that stores' decisions to change ownership, business structure, or location, or cease operations are typically confidential to maintain customers and employees. Providing adequate advance notice of such changes to the State agency also may be prohibited by sales contracts or union agreements. Consequently, more often than not, such changes are not reported in advance. Although termination of the vendor agreement for *reported* changes in vendor ownership, business structure, or location, or cessation of operations may not seem like an adverse action, termination of the vendor agreement for *unreported* changes, especially changes in business structure, is certainly considered an adverse action by affected businesses. Due to the complexities of business structures, State agencies and vendors often disagree with what constitutes a change in ownership and what constitutes a change in business structure. Rather than resolving all such disputes in the courts, we believe it is in the best interests of the Program (i.e., ensuring adequate participant access) to provide vendors with at least an abbreviated administrative review to present evidence that such changes do not warrant termination of the vendor agreement.

We accepted several recommendations from commenters to modify proposed § 246.12(h)(3)(xvii). These modifications included clarifying that the State agency has the discretion to determine: the length of the required advance written notice of vendor changes, whether a change in location qualifies as a short distance, and whether a change in business structure constitutes a change in ownership. Only one commenter suggested that we retain the "null and void" language from previous regulations. We did not accept this comment for the reasons noted above. A State agency commenter noted that it verifies through its Secretary of State's business division whether a vendor change represents a change in ownership or a change in business structure. We highly recommend that State agencies seek such external verification of vendor changes that will result in the termination of vendor agreements.

Question 4: Under § 246.18(a)(1)(ii)(E), when a vendor agreement is terminated because of a change in ownership, who has appeal rights, the previous owner or the current owner?

Answer: Regulations at § 246.18(a)(1)(ii)(E) state in part: "The State agency must provide abbreviated administrative reviews to vendors that appeal the following adverse actions, unless the State agency decides to provide full administrative reviews for any of these types of adverse actions: (E) termination of an agreement because of a change in ownership…." A vendor may disagree with the State agency's determination that a change, whether reported or not, represents a change in ownership. When a vendor appeals the State agency's termination of the vendor agreement because of a change in ownership, the State agency must provide the vendor with an administrative review, regardless of whether the State agency considers the vendor to be a previous owner or a new owner.

Question 5: Under § 246.18(a)(1), are vendor applicants who are denied program authorization due to a State-established selection criterion entitled to a full or an abbreviated administrative review?

Answer: The State agency has the discretion to establish whether a full or abbreviated administrative review is to be provided for denials of vendor authorization due to its State agency-established vendor selection criteria. In determining which type of administrative review was appropriate for the mandatory selection criteria, we considered the range of issues that may be subject to vendor appeal for each selection criterion. For selection criteria in which the issue on appeal is a narrow one, we provided for an abbreviated administrative review. For example, the only fact at issue in a denial of authorization due to the vendor selection criterion for current Food Stamp Program disqualification or civil money penalty for hardship is whether the information used by the State agency to

deny authorization to the vendor applicant is accurate. When we determined that a vendor may raise a broad range of issues regarding a selection criterion, we provided for a full administrative review. For example, for denials of authorization due to the competitive price selection criterion, the vendor may raise a variety of issues, including its peer group assignment, the prices used by the State agency, or whether the selection criterion was applied correctly.

Question 6: Because § 246.18(b)(7) only provides the vendor with the opportunity to examine "the evidence upon which the State agency's action is based," is the vendor now required to request access to its entire vendor file under the State's Open Records or Freedom of Information Act, which allow a vendor access to its entire vendor file?

Answer: Regulations at § 246.18(b)(7) establish minimum requirements for the State agency's full administrative review procedures. Consequently, the State agency has the discretion to restrict the access of the vendor or its attorney to only the evidence upon which the State agency's action is based and to require the vendor or its attorney to request further access to the vendor's case file through the State's Open Records or Freedom of Information Act. Conversely, the State agency may provide the vendor full access to the vendor's case file as part of the State agency's full administrative review procedures. However, the State agency should not provide vendors with access to investigative information contained in the vendor's case file, including how the State agency established the vendor's high-risk status, where the State agency's investigative techniques are exempted from release by State Open Records or Freedom of Information Act requests. To determine what information to provide to vendors under its full administrative review procedures, we recommend that the State agency seek advice from its State Attorney General or General Counsel's office.

Question 7: Under § 246.18(a)(1)(i), is the State agency required to provide a full administrative review when a vendor appeals a civil money penalty (CMP) issued in lieu of a reciprocal WIC disqualification?

Answer: Yes. Section 246.18(a)(1)(i)(D) states that a full administrative review must be provided for the imposition of a fine or a CMP in lieu of disqualification.

K. Definition of Proxy

Question 1: Under the definition of "proxy" in § 246.2, may a non-parent, non-caretaker proxy bring an infant or child in for recertification?

Answer: Yes, provided the caretaker proxy provides written authorization from the infant or child's parent, legal guardian, or other individual who is legally responsible for the infant or child.

Question 2: Under the definition of "proxy" in § 246.7(l)(1), may the State agency continue its practice of permitting both parents of an infant or child participant to be designated as authorized representatives, rather than requiring one parent be designated as the authorized representative and the other parent be designated as a proxy?

Answer: Yes. Both parents of an infant or child participant may be designated as authorized representatives. The State agency may need to develop specific policy and procedures to address child custody cases.

L. Dual Participation Provisions

Question 1: Under §§ 246.7(l)(1)(i) and (l)(1)(ii), what types of systems does FNS deem appropriate for the detection and prevention of intrastate and interstate dual participation?

Answer: The type of system that is appropriate for a State agency to detect and prevent dual participation will depend on the State agency's needs and circumstances. Many factors influence which type of system is appropriate for the State agency, including: whether an Indian Tribal Organization (ITO) State agency operates within the State agency's jurisdiction; whether a Commodity Supplemental Food Program (CSFP) agency operates within the State agency's jurisdiction; and whether the State's borders make interstate dual participation likely or unlikely. The State agency must assess its own circumstances and develop a system that meets its needs.

The FNS Southwest Regional Office's (SWRO) Dual Participation Program Integrity Workgroup issued guidance to assist State agencies in the development of systems to detect and prevent both intrastate and interstate dual participation. The resource guide, entitled "Best Practices: A Guide to Preventing and Resolving Dual Participation in the WIC Program," contains a variety of effective policies and procedures used by SWRO State agencies. The guide also contains a sample interstate dual participation agreement, as well as recommended procedures for determining when to impose participant claims and sanctions. First issued in August 1999, the guide was updated in October 2001. State agencies are encouraged to obtain a copy of the 2001 guide by contacting their FNS regional office.

Question 2: Under the interstate dual participation requirements in § 246.7(l)(1)(ii), how does FNS define other factors that "make it likely" that participants travel regularly between local service areas located across State agency borders?

Answer: Factors that "make it likely" that participants travel regularly between local service areas include: public transportation systems that operate across State borders; the lack of geographic barriers separating local service areas; the proximity of local agencies or clinics of bordering State agencies; or the authorization of common vendors by bordering State agencies. This list is not intended to be exhaustive. We recommend that each State agency consult with its FNS regional office and neighboring State agencies to determine the need for a written agreement for the detection and prevention of dual participation.

Question 3: Does the 120-day timeframe for follow-up action on instances of suspected dual participation specified in § 246.7(l)(1)(i) also apply to the interstate dual participation provisions in § 246.7(l)(1)(ii)?

Answer: Yes. The 120-day timeframe for follow-up action applies to all instances of suspected dual participation.

Question 4: Under § 246.7(l)(1), is the State agency required to collect participant claims for improperly issued benefits when the dual participation was not intentional?

Answer: No. Although regulations at § 246.7(l)(1)(iii) require immediate termination from participation in one of the programs for all cases of dual participation, regulations at § 246.7(l)(1)(iv) only require the State agency to collect participant claims "in cases of dual participation resulting from intentional misrepresentation."

M. Participant Violations, Claims, and Sanctions

Question 1: Under § 246.23(c)(1)(i), for participant claims, what does FNS consider the "full value" of program benefits that have been obtained or disposed of improperly as the result of a participant violation? Does the State agency have the discretion to use either the total purchase price of such food instruments, the post-rebate food cost, or the food cost plus the NSA costs for certification, nutrition education, etc.?

Answer: To calculate the amount of a participant claim under § 246.23(c)(1)(i), the State agency must use either the total purchase price of food instruments or the total post-rebate food cost of program benefits obtained or disposed of improperly as the result of a participant violation. Although the actual costs of program benefits improperly obtained may include Nutrition Services and Administration (NSA) costs for nutrition education and breastfeeding promotion, it is inappropriate to include such costs in a participant claim. The "rights and obligations" statement that must be signed by the applicant, parent, or caretaker under § 246.7(i)(10) contains the following statement: "I understand that intentionally making a false or misleading statement or intentionally misrepresenting, concealing, or withholding facts may result in paying the State agency, in cash, *the value of the food benefits improperly issued to me* and may subject me to civil or criminal prosecution under State and Federal law" (emphasis added). The formula used by the State agency to calculate participant claims must be applied consistently throughout the State agency's jurisdiction.

Question 2: In addition to § 246.23(c)(1), what guidance can FNS provide the State agency to assist in determining when further collection actions for participant claims would no longer be cost-effective?

Answer: Under § 246.23(c)(1), for each participant claim, the State agency is required to issue a letter to the participant demanding repayment of the full value of program benefits that have been obtained or disposed of improperly as the result of a participant violation. In addition, the State agency must develop standards for determining when claims collection actions beyond the initial demand letter are necessary based on a cost-benefit analysis. To establish its standards, the State agency should determine what additional actions it may take to successfully collect participant claims, analyze the costs associated with these actions, and develop standards, such as dollar thresholds, that establish when the State agency will take further claims collection action. For more specific guidance, we recommend that the State agency refer to Attachments DP-7 and DP-8 of the "Best Practices: A Guide to Preventing and Resolving Dual Participation

in the WIC Program," which is referenced in the answer to Question 1 of Section L. of this document.

Question 3: Under § 246.23(c)(1)(i), may the State agency require participants to pay claims for food instruments transacted after their expiration dates before paying vendors for such food instruments?

Answer: No. Although regulations at § 246.12(j)(3) require that at least during the initial certification visit each participant, parent or caretaker must "receive an explanation of how the local food delivery system operates," it is ultimately the vendor's responsibility to ensure that a food instrument is valid before transacting it. Under § 246.12(h)(3)(iv), the vendor is assigned the responsibility to "accept a food instrument only within the specified time period." Consequently, under the vendor agreement, transacting a food instrument before or after its specified period is a vendor violation. Under § 246.12(h)(3)(ix), the State agency must deny payment of or establish vendor claims for the full value of such food instruments. In addition, we recommend that the State agency counsel the participant, parent, or caretaker involved in such transactions about using food instruments within their valid dates.

Question 4: In addition to establishing a claim against the vendor, is the State agency required under § 246.23(c)(1)(i) to establish a claim against a participant for a food instrument transaction in which the participant committed a participant violation?

Answer: Yes. Regulations at § 246.23(c)(1)(i) state in part: "If the State agency determines program benefits have been obtained or disposed of improperly as the result of a participant violation, the State agency must establish a claim against the participant for the full value of such benefits." Regulations at § 246.2 clarify that a *participant violation* includes "exchanging food instruments or supplemental foods for cash, credit, non-food items, or unauthorized food items, including supplemental foods in excess of those listed on the participant's food instrument…." In addition to issuing a participant claim, regulations at § 246.12(u)(2) state: "Except as provided in paragraphs (u)(2)(i) and (u)(2)(ii) of this section, whenever the State agency assesses a [participant] claim of $100 or more…or assesses a second or subsequent claim of any amount, the State agency must disqualify the participant for one year."

Question 5: What recourse does the vendor have when a participant, who attempts to transact an expired food instrument and the vendor refuses to accept the food instrument, takes the supplemental food items and leaves the expired food instrument on the vendor's counter?

Answer: The vendor should contact local law enforcement authorities, report the incident as shoplifting, and provide authorities with information pertaining to the incident. The vendor should not submit the food instrument for redemption because it may be used as evidence by local law enforcement authorities in their investigation and prosecution of the perpetrator involved in the shoplifting incident. If it is store policy, the vendor may refuse service to the perpetrator in the future.

In addition to contacting local law enforcement authorities, the vendor should report the incident to its State or local agency. During the next office visit, State or local agency personnel should counsel the participant, parent/caretaker, or proxy on the proper use of food instruments and the penalties for participant violations. In the event that the vendor is unable to recover the value of the stolen supplemental foods through the disposition of the shoplifting case, the State agency may, at its discretion, pay the vendor for the expired food instrument in accordance with § 246.12(k)(5).

Question 6: Under § 246.12(u)(2), does the disqualification period imposed for a participant sanction only apply to the participant's current certification period or does it extend beyond this period?

Answer: A disqualification period is a set amount of time, such as one year, and has no relationship to a participant's certification period. The disqualification period begins when the participant's benefits are discontinued and extends until the disqualification period expires.

Question 7: Under § 246.12(u)(2), after a participant's disqualification period has expired, may the participant reapply and be certified for program benefits, even though full restitution has not been made?

Answer: Yes. After a participant's disqualification has expired, the participant may reapply and be certified for program benefits, even though full restitution has not been made.

Question 8: To address egregious situations, such as when a parent has been convicted for WIC fraud, may the State agency prohibit a participant or parent/caretaker from receiving further program benefits until either full restitution is made or a repayment plan is agreed upon?

Answer: No, unless the prohibition is part of the participant or parent/caretaker's conviction or plea agreement.

Question 9: Can a State agency sanction a participant for altering the WIC food instrument and obtaining more supplemental foods than prescribed by the local agency, if the State agency's pre-payment edit system detected the alteration and rejected the food instrument?

Answer: Yes. Altering a WIC food instrument and obtaining supplemental foods in excess of the quantities prescribed by the WIC clinic are participant violations, irrespective of whether the State agency pays the vendor for the supplemental foods that were improperly obtained. Section 246.23(c)(1) of the WIC regulations requires the State agency to assess a claim for the full value of benefits improperly obtained, which in this instance means the value of the supplemental foods that were in excess of those originally prescribed. Under § 246.12(u)(2), a State agency must impose a mandatory disqualification for up to one year whenever it assesses a claim of $100 or more for benefits improperly obtained, except as indicated in paragraphs (u)(2)(ii) and (u)(2)(iii). However, because altering a food instrument is also a vendor violation, the State agency should review the situation carefully, examining available data to determine whether the violation is attributable to the participant and/or to the vendor before issuing a claim.

After reviewing the rejected food instrument, the State agency should decide whether the vendor should have been able to detect the alteration and, possibly, whether the amount of supplemental foods provided was consistent with the alteration. Examination of information imprinted on the back of the food instrument is particularly important for this reason. The State agency should look for a pattern of abuse involving the same participant, the same vendor, and even the same cashier if possible. Compliance investigations may be needed to corroborate or to decipher a suspicious pattern suggested by existing evidence.

When a participant has repeated violations and the claim amount is substantial and unpaid, the State agency may want to check with State and/or local law enforcement authorities to see whether referral for prosecution under

§ 246.12(u)(5) is appropriate. To minimize the likelihood of food instrument alterations, a State agency should consider writing out the quantities of supplemental food items prescribed on the food instrument, e.g., using “five cans of concentrate infant formula” rather than “5 cans of concentrate infant formula.”

N. Miscellaneous Provisions

Question 1: Do §§ 246.26(e) and (f) supersede State Freedom of Information and/or Open Record laws?

Answer: As a condition of participating in the WIC Program, State agencies agree to comply with Federal requirements for the Program, including the vendor/retailer confidentiality provisions at §§ 246.26(e) and (f). If a State Freedom of Information/Open Records law conflicts with these provisions, the State agency must take whatever steps are necessary to modify or obtain an exception from the law. In some cases, there may not be a conflict because the State law already provides an exception from the disclosure requirement to address such confidentiality provisions.

Question 2: Do the confidentiality provisions found in § 246.26(e) only cover currently authorized vendors and not vendors who have been disqualified from the Program? Information, such as the reasons why a particular vendor was disqualified, is used: to discuss issues with participants involved in vendor violations (e.g., about the connection between unauthorized foods and anemia), to train other vendors (e.g., about the connection between vendor violations and sanctions), and to provide reports to the public and media about the reasons why particular vendors have been disqualified.

Answer: The confidentiality protections in § 246.26(e) extend to all vendors, regardless of whether they are currently authorized or not. However, only information that individually identifies a vendor is protected from disclosure. Thus, State agencies may use vendor information as part of case studies for participant or vendor training as long as any information identifying an individual vendor is redacted (i.e., altered or removed).

Question 3: Under § 246.26(e), is all vendor information, except for name, address, and authorization status, considered to be confidential information?

Answer: Yes. Regulations at § 246.26(e) state: "Confidential vendor information is any information about a vendor (whether it is obtained from the vendor or another source) that individually identifies the vendor, except for vendor's name, address, and authorization status." Aggregate data that does not individually identify vendors is not considered confidential information.

Question 4: Under § 246.26(e), may the State agency provide information to vendors about the other vendors in its peer group (name, address, authorization status, and peer group)?

Answer: No. The State agency may provide vendors the definitions for its peer groupings and aggregate data about the number of vendors in each peer group, but it is prohibited under § 246.26(e) from providing information to vendors that identifies the peer groupings of other individual vendors.

Question 5: Under § 246.26(e), is price information regarding authorized vendors confidential during the administrative review process when a vendor appeals its denial of authorization due to the competitive price vendor selection criterion?

Answer: Price information regarding individual vendors is confidential information under § 246.26(e) and may not be provided to vendor applicants during administrative reviews. The State agency should present aggregate or anonymous price information to demonstrate that it correctly applied its competitive price vendor selection criterion when it denied authorization to the vendor applicant. If vendor-specific price information is requested by the hearing officer, the State agency may provide such information to the hearing officer, who is permitted under § 246.26(e)(1) to view confidential vendor information. We recommend that the State agency seek legal counsel from its State's Attorney General or General Counsel's office to determine what type of price information is appropriate for presentation during administrative reviews.

Question 6: Under § 246.26(e), may the State agency provide a vendor with data regarding its own redemptions?

Answer: Yes. The State agency may provide a vendor with vendor-specific data about its own operations.

Question 7: Under § 246.26(e), is vendor-specific gross redemptions data considered confidential vendor information? Under some States' laws, vendor-specific gross redemptions data is not considered confidential vendor information because this information is generated by the State agency, not provided to the State agency by the vendor, and is considered public information as it relates to the accountability of public funds.

Answer: Yes. As noted in § 246.26(e), any information (other than vendor's name, address, and authorization status) that individually identifies a vendor is confidential, whether it is obtained from the vendor or another source. That

includes gross redemption data generated by the State agency. See the above answer to Question 1 of this section for information on how to deal with State Freedom of Information/Open Records laws that may conflict with this requirement.

Question 8: How do the confidentiality requirements in § 246.26(e) affect the sharing of confidential vendor information between State agencies?

Answer: Regulations at § 246.26(e) state in part: "Except as otherwise permitted by this section, the State agency must restrict the use or disclosure of confidential vendor information to: (1) Persons directly connected with the administration or enforcement of the WIC Program or the Food Stamp Program who the State agency determines have a need to know the information for purposes of these programs. These persons include personnel from its local agencies and other WIC State and local agencies and persons investigating or prosecuting WIC or Food Stamp Program violations under Federal, State, or local law." Consequently, the State agency may provide confidential vendor information to personnel from other State and local agencies provided such personnel are directly connected with the administration or enforcement of the WIC Program.

Question 9: Can a vendor require participants to leave their WIC vouchers as a "deposit" when ordering exempt infant formulas?

Answer: Under 7 CFR 246.12(h)(3)(iii), the vendor agreement must require a vendor to offer program participants, parents or caretakers of infant or child participants, and proxies the same courtesies offered to other customers. If the vendor does not require non-WIC customers to leave a deposit for exempt infant formula orders, it may not require WIC participants to leave their food instruments as a deposit.

Requiring a participant to leave a food instrument with a vendor, for any reason, prior to the WIC transaction should be discouraged, unless the vendor agreement specifically permits and governs this practice. Vendors may not establish their own rules for WIC transactions, even if their rationale is to prevent financial loss due to the failure of customers to return to the store to purchase formula that was ordered for them. Requiring a participant to relinquish a food instrument prior to the WIC transaction also exposes the participant to the risk of loss or theft of the food instrument and may increase the potential for fraud or abuse by vendors.

O. Implementation of the Final Rule

Question 1: May the State agency wait until the end of the current vendor agreement period before implementing the required changes from the final rule?

Answer: Yes, provided the required changes are fully implemented by October 1, 2002. On October 18, 2001, FNS published a final rule that extends the implementation date for the WIC Food Delivery Systems final rule from February 27, 2001 until October 1, 2002. We extended the implementation date to provide State agencies with additional time to implement the final rule, to promote more effective and efficient implementation of the new requirements, and to make the implementation date correspond with the beginning of the Federal fiscal year.

We recognize that implementation methods vary among State agencies. For example, a State agency for which all vendor agreements are scheduled to be renewed in May 2002 might decide to wait until then to implement the new vendor requirements. This way the State agency could make the necessary changes without having to amend current agreements. Another State agency that enters into agreements on a rolling basis may decide to amend the agreements as new ones are entered into, provided that agreements are in place for all vendors by October 1, 2002, even if it means amending some agreements prior to that date. Another approach is to send a notice to all vendors informing them of the new provisions and offering them the option to either agree to the amendments or to terminate their agreements. The extended implementation period should give State agencies sufficient lead time to plan for an orderly replacement of any vendors that terminate their agreements because they do not agree to the new provisions.