

Cost Containment of High-Priced Stores in the California WIC Program

Background

Since 1998, the Department of Health Services WIC Branch has been working on revisions to policies for authorizing and reimbursing grocery stores, in order to ensure fairness and consistency and achieve cost containment. During this period, the WIC program experienced a growing problem — the spread of a new type of store that sells *only* WIC foods, serves *only* WIC participants, and charges significantly higher prices for these foods than other retail food stores. These “WIC-only stores” are able to charge more because they face no competitive pressure to keep their prices low enough to attract non-WIC customers. To read in detail about the impact of high-cost stores on the WIC program, see *WIC-Only Stores and Competitive Pricing in the WIC Program*, by Zoe Neuberger and Robert Greenstein, Center on Budget and Policy Priorities.¹

WIC-Only stores, which now operate in many states, are raising the cost of the WIC Program by substantial amounts. In California, based on May 2004 data showing the share of WIC sales going to WIC-Only stores was 44%, the Center on Budget and Policy Priorities estimates that the federal government is paying about \$37 million a year more for WIC than the program would cost if the WIC foods purchased in WIC-only stores were instead obtained in regular food stores. As of late last year, the WIC-Only store share had risen to 48% of total California WIC redemptions.²

Nationally, the WIC funding level for FFY 2006 is \$5.257 billion, which will likely support current participation this year. But WIC, a “domestic discretionary” program, still faces serious fiscal challenges in Congress, including deep cuts proposed by the Bush Administration in January, and last-minute budget recissions. Absent firm corrective action, the added costs created by high-cost WIC stores create the risk that federal funds will be insufficient to serve all eligible families that apply – and there are still thousands unserved in California.³

The clear fiscal impact of high-cost WIC stores on California WIC’s bottom line has been evident for some time. However, state program administrators have had difficulty instituting vendor cost containment measures through state law and regulations alone. Not only is reform of this system fiendishly complex, but it soon became ensnared in pressure group politics. Four years ago, when California WIC officials sought to institute regulatory reform measures, the WIC-only stores in California, who had formed an association, hired a team of well-connected lobbyists who pressured California policymakers, including Governor Davis, to block those efforts. Draft regulations were informally circulated, but never promulgated.

Without new regulatory authority, California WIC officials were unable to put limitations on authorizing high-cost stores, nor could they implement fair or meaningful reimbursement levels. As a result, the number of WIC-Only stores grew rapidly, and their

percentage of WIC voucher redemptions skyrocketed from 11% in 1997 to over 47% in June 2005 — an alarming trend that caught the attention of Congress during WIC 's reauthorization. New federal laws were enacted, forcing California to freeze new store approvals (with few exceptions) and to get new reimbursement rates in place that will contain vendor costs.

Vendor Cost Containment Provisions in the WIC Reauthorization Bill

Two years ago, the WIC program, along with other child nutrition programs, was reauthorized. President Bush signed the Child Nutrition and WIC Reauthorization Act (P.L. 108-265) on June 30, 2004.⁴

The bill allows WIC-only stores to continue operating and, in fact, to continue to spread. It contains several modest provisions aimed at strengthening the ability of state WIC programs to prevent WIC-only stores from abusing their insulation from normal market forces to charge much higher mark-ups on WIC foods than other stores do, thereby driving up WIC program costs. Specifically, the new law:

- Defines WIC-only vendors as stores for which more than half the annual revenue from food sales consists of WIC sales (or new stores likely to meet those criteria), the so-called “Above 50 Percent Vendors.”
- Requires states to categorize WIC vendors into peer groups. For each peer group, states must establish price criteria, which will be used when assessing vendors' applications for WIC authorization, to make sure that the vendors authorized to participate in WIC charge competitive prices. The state also must limit the amount it will reimburse the vendors in each peer group for specific WIC foods and make sure that prices aren't increased to a level that would prevent the store from being authorized if it were currently being considered. In selecting vendors based on price and limiting reimbursement levels, the state must consider participant access by geographic area.
- **Requires states to ensure that its price criteria and reimbursement limits do not result in higher aggregate food costs if WIC participants redeem their WIC vouchers at Above 50 Percent vendors rather than other vendors.**
- **Requires USDA to certify that a state's price criteria and reimbursement limits do not result in higher average prices at Above 50 Percent vendors than at comparable other vendors.**
- Prohibits Above 50 Percent vendors from providing incentive items or other free merchandise to WIC participants unless the vendor proves to the state that the items were obtained at no cost, except for food or merchandise of nominal value.
- Requires all states to allow participants to redeem WIC food instruments at “any authorized grocer.”
- Requires states to a system in place to address these provisions no later than December 31, 2005.

Federal Regulations and Guidance. To implement the new law, the U.S. Department of Agriculture (USDA) published Interim Final Regulations that took effect on December 29, 2005.⁵ The regulations require California to implement a new vendor authorization and peer group pricing system consistent with federal law and USDA guidance.

Significantly, states will be liable to fiscal sanctions (recoupment) if they fail to achieve cost neutrality between their “Above 50 Percent” and all other vendors. Detailed USDA guidance was issued to states in July 2005.

Lawsuit Dismissed. Implementation was temporary stayed by a federal lawsuit filed in Washington DC on behalf of a group of WIC-Only stores in December 2005. However, in an opinion issued on February 23, 2006, the Court rejected the WIC-only stores’ claims and fully supported USDA’s implementation policies and procedures to date.⁶ Thus, USDA will enforce the new regulations and states are required to comply.

Appropriations Bill Moratoriums. Shortly after the reauthorization bill was signed, the Office of Management and Budget urged Congress to prohibit new WIC-Only Store approvals until states could implement the vendor cost controls required by the new reauthorization law. This resulted in language in the FY 2005 appropriations bill that imposes a nationwide moratorium on any state approvals of any new WIC-Only stores except if necessary to ensure participant access. The President’s 2006 budget proposed to extend this moratorium through the coming fiscal year. The FFY 2006 Agriculture Appropriations bill (signed November 10, 2005) requires states to continue the moratorium until their vendor cost containment systems are implemented.⁷ FFY ’07 appropriators are currently debating a continued moratorium.

California-Specific Vendor Authorization Moratorium. In August 2004, the USDA rescinded its approval of the part of California WIC’s State Plan related to vendor authorization until the program revises its competitive pricing policies to more effectively meet federal cost containment requirements and regulations. In response, the Branch imposed a temporary moratorium on the authorization of new grocers, which will remain in effect pending USDA guidance.⁸

Incentives Curtailed. To gain competitive advantage, many “WIC-Only” stores offered participants incentive items such as extra juice, pots and pans, strollers, and free transportation. The problem with these popular incentives was that WIC food funds were being used to pay for them -- thus driving up costs to the program as a whole. Congress and USDA decided that this was an inappropriate use of taxpayer dollars, so federal guidance tightened up the rules about the types and allowable costs of incentives that are paid for with WIC funds. California implemented this guidance effective December 1, 2005. Stores can now only offer participants a variety of low-cost nutritious foods (tuna, tortillas, fresh produce) and normal customer services -- no more free strollers and rides.⁹

California is Implementing the New Federal Law

Now that federal regulations have been upheld in court, the California WIC program is working quickly to implement a long-awaited revamping of its vendor authorization and reimbursement system. The changes will be rolling out in two phases. One began on June 1st and only impacts certain stores. More comprehensive changes will be implemented on October 1st.

Interim Cost Containment. As an interim cost-control measure, effective June 1, 2006, California lowered the reimbursement rates for all stores that derive more than 50 percent of their total annual food sales revenue from the sale of supplemental foods

obtained with WIC food instruments (the “above-50-percent” vendors, which include WIC-Only and a small number of other grocery stores). For each WIC food item, this new reimbursement rate is derived from the average cost charged by all other WIC retail vendors. No prices will be printed on checks made out to these stores. All other stores will be reimbursed as usual during this period.¹⁰

Full Implementation of Cost Containment. Effective October 1, 2006, California WIC will be establishing peer groups for all authorized vendors and determining separate maximum rates for each peer group. There will no longer be a statewide “Not To Exceed” price printed on any WIC check. At the same time, WIC participants will no longer be asked to choose a single store to shop at. On October 1, all California WIC checks will be redeemable at “Any Authorized Vendor.”¹¹

The Bottom Line

WIC’s mission is to safeguard the health of low-income women, infants and young children who are at nutrition risk – not to subsidize specialized store operators. Because WIC is a capped discretionary program, higher food costs mean that either more federal funds must be provided to serve the same number of participants, or fewer participants can be served. In a scarce funding environment, the new vendor cost containment measures are necessary to protect WIC’s fiscal integrity and allow the program to continue serving vulnerable families.

Over the next year, CWA urges members of the California Legislature to support the WIC Vendor Cost Containment process, and continue careful oversight, in order to ensure that it is not derailed again due to political pressures or bureaucratic snafus. At stake is the fiscal integrity of one of the nation’s most successful public health programs, and the ability of this program to continue to serve hundreds of thousands of low-income families with literally life-saving benefits.

¹ *WIC-Only Stores and Competitive Pricing in the WIC Program*, by Zoe Neuberger and Robert Greenstein, Center on Budget and Policy Priorities, at www.cbpp.org/5-17-04wic.pdf.

² Department of Health Services WIC Branch December 2005 Data.

³ Department of Health Services, WIC Supplemental Nutrition Branch Data, at http://www.wicworks.ca.gov/resources/Method03_CCPA.pdf

⁴ 42 U.S.C § 1786 (h) (11) (B)

⁵ FR, p. 71708-71731, November 29, 2005.
<http://www.fns.usda.gov/wic/regspublished/vendorcostcontainmentinterimrule.htm>

⁶ http://www.calwic.org/docs/federal/courttopinion_nwga.pdf

⁷ Department of Health Services Grocer Alert: *Two Moratoriums on Grocer Authorizations*, http://www.wicworks.ca.gov/grocers/alerts/2004_07_alert.htm

⁸ Ibid.

⁹ Department of Health Services Grocer Alert: *Incentives Offered by 50% Grocers*, at http://www.wicworks.ca.gov/grocers/alerts/2005_12_alert.htm

¹⁰ http://www.wicworks.ca.gov/grocers/alerts/2006_02_alert.htm

¹¹ <http://www.wicworks.ca.gov/grocers/information/aav/coverLetter102005.htm>

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