REVIEW OF
UNEMPLOYMENT BENEFIT OVERPAYMENTS

VIRGINIA EMPLOYMENT COMMISSION

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SUMMARY

The U.S. Department of Labor estimated the Employment Commission unemployment benefit overpayment rate at 14.6 percent for calendar year 2009. Over 2/3 of these estimated overpayments result from questions about the adequacy of the claimant's work search. While the calculation is accurate based on the Employment Commission's requirements, the work search criteria may be outdated, and the systems and funding to improve accuracy may not be available.

The U.S. Department of Labor, for the same period, also calculated an operational overpayment rate of 3.32 percent for Virginia that was lower than all but one of the surrounding states. The operational rate excludes requirements that are not consistent among states to allow for better comparability. This operational rate indicates that Virginia is detecting and pursuing overpayments at a rate better than most of its peers.

Reducing overpayments will require a combination of new systems, personnel, and more timely and accurate information from both claimants and employers. Limitations on funding, repayment of the Trust Fund loan to the federal government, and not adversely increasing administrative costs for employers will all significantly affect the Employment Commission's ability to address overpayments.

This report has a number of recommendations including the potential financial and procedural implications that these recommendations will have on the Employment Commission, employers, and claimants. Because the General Assembly has set the repayment of the federal loan for unemployment benefits as a priority, addressing those recommendations will be difficult.

-T A B L E O F C O N T E N T S-

Unemployment Benefits Claims Process

Introduction

We received a legislative request in February 2010 to analyze overpayment activity at the Virginia Employment Commission (Employment Commission) to determine the amount of overpayments attributable to administrative errors. We were also asked to determine what issues contribute to the administrative errors such as software, lack of training, or improper supervision. The following sections discuss the results of our audit.

The Employment Commission administers the State Unemployment Insurance program which provides unemployment benefits for workers who are unemployed and meet certain eligibility criteria. The Employment Commission processes claims for unemployment benefits by determining if the claimant is eligible and what types of benefits for which they are eligible.

Although the State Unemployment Insurance program is the primary source of unemployment benefits, there are also other types of unemployment benefits that individuals can receive. For example, federal employees as well as military claimants receive benefits under other programs. In addition, over the last few years, the federal government has approved various programs that have extended benefits for individuals who have exhausted their regular State Unemployment Insurance benefits.

The funding for the State Unemployment Insurance program comes from employers based on the number of employees, employees who have filed for unemployment, and the amount of their wages. Additionally, the employer information serves as one of the fundamental pieces of data used to determine if an individual is eligible for benefits. Because of the importance of the employer information to the process, following is a flow chart of this information followed by a brief discussion of some of the issues associated with this information.

Employer Quarterly Report Submission Process

Employers Submit Reports Employers must file tax and wage reports quarterly with the Employment Commission (VEC) 30 days after the end of the quarter. Both the tax and wage reports contain payroll information on all employees for the quarter. Employers may submit quarterly reports in a variety of formats including paper, CD, diskettes, and other electronic means such as iFile and ADP.

The system automatically assesses a $75 penalty on employers for late tax reports; however, VEC waives this penalty in certain situations. However, there are no punitive tools for employers who repeatedly report incorrect information.

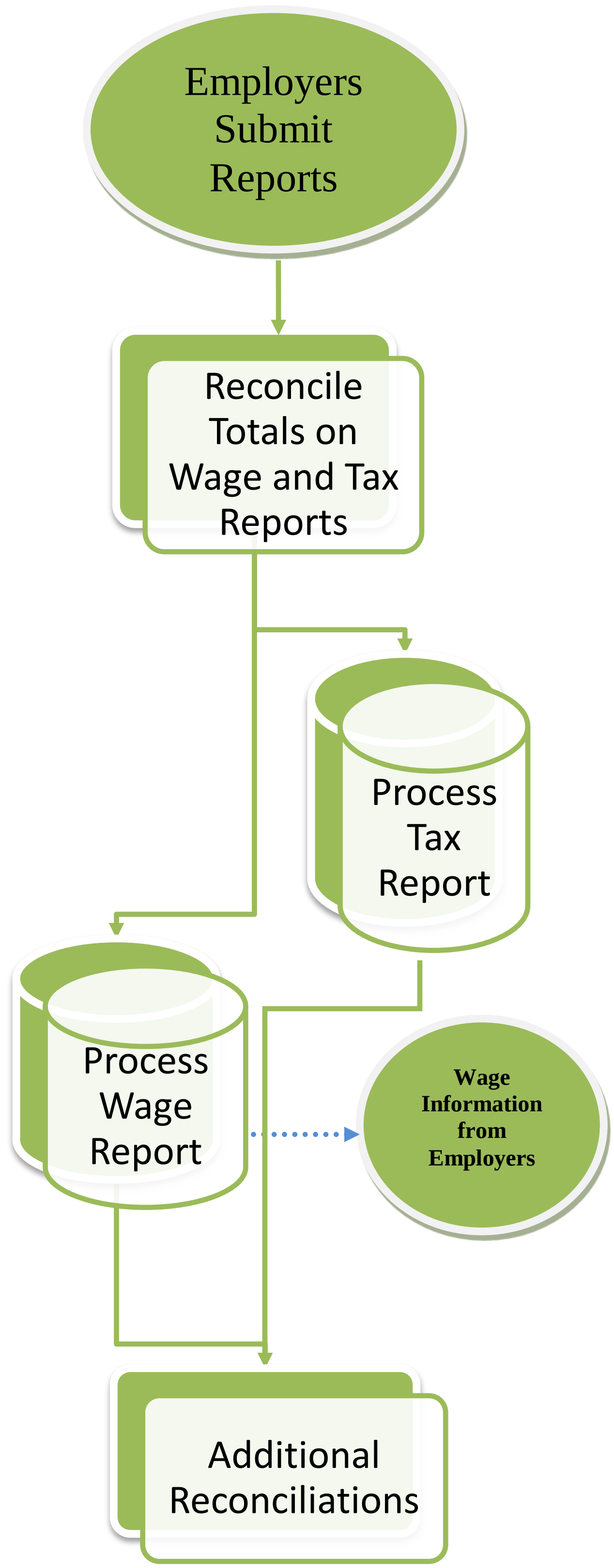
The system identifies employers using electronic submissions and generates a listing of employers submitting paper quarterly reports. VEC mails these employers the required reports to complete and submit. Typically, VEC sends out 120,000 packets. Approximately half the employers use the mailed forms and half create their own forms. VEC tracks information not returned to identify delinquent businesses as well as some businesses that have closed.

Reconcile Totals on Wage and Tax Reports *VEC compares the total payroll amount on the wage report to the total reportable wages on the tax report for paper submissions. When the two do not match, VEC investigates and corrects the information. When the reports match, they are processed through the system.*

Process Wage and Tax Reports VEC automatically processes electronic report submissions and after reconciling in total processes paper report submissions. The system generates wage information for use in checking benefit amounts as shown on the flowchart on page 6.

Additional Reconciliations *VEC performs additional reconciliations based on the submission format of the wage and tax information. They identify variances as a result of incorrect data initially submitted or changes submitted by the employer. VEC investigates and corrects variances over the following thresholds:*

- *For employers with less than 26 employees, they investigate if the wage information is $2,000 more than the tax information, or if the wage information is $25,000 less than the tax information*
- *For employers with more than 26 employees, they investigate if the wage information is $60,000 greater than the tax information, or if the wage information is $75,000 less than the tax information*



Processing Employer Information

The Employment Commission reconciles quarterly wage and tax files from employers to determine if the information is correct. This wage information is the basis for the amount and duration of weekly benefits. As noted above, the Employment Commission has established some thresholds for following up on variances that come up during the reconciliation process.

The reconciliation process will not detect 100 percent of the errors. The thresholds use the number of employees an employer has and the amount of the variance. The Employment Commission designed the reconciliation this way because there are frequently errors in information sent in from employers and it is time consuming to research and resolve all errors. They investigate the variances that meet the threshold and follow up with employers to correct the information.

The Employment Commission sometimes processes employer wage information without having the tax report on file or even though they are aware the tax and wage information do not match. The information may not match if the wage information is incomplete, if it is being amended by the employer or it is within the thresholds discussed above. In these cases, the Employment Commission has not performed the reconciliation and identified any variances. This occurs because the employer wage file is an essential data source for determining an individual's eligibility for benefit payment and the federal government has imposed a time requirement to make the payment.

Example:

An employer incorrectly submitted two separate quarters (second and fourth quarters of 2007) of wage information as wages for the fourth quarter 2007. The staff detected the difference; however, they needed the information to process claims and began using this incorrect data.

Using this incorrect data during 2008 and 2009, the Employment Commission overpaid individuals drawing unemployment benefits from this employer. The Employment Commission as a result over paid 154 individuals $222,000 in unemployment benefits.

Although errors of this nature can occur, Employment Commission staff did not follow up to correct the error in a timely manner. Since this error occurred, the Employment Commission implemented new procedures in Spring 2009 for processing employer information.

- Employment Commission staff developed additional process documentation which incorporate the staff's knowledge and expertise. In addition, they have implemented additional training to make staff more aware of the repercussions of errors and made some system modifications to better identify potential errors.

- Employment Commission staff meet quarterly to review any changes in the processes, review the outcomes, and work together to deal with date submission problems and make the employers more aware of how the process works.

- The Employment Commission received a Supplemental Budget Request to procure a server and software to allow bulk upload of wages. This new process will allow for employers to label the date of the submitted file as well as required fields using either an MMREF, ICESA or an excel spreadsheet upload. In addition, this upload will allow employers using QuickBooks software to electronically transmit files which will reduce the potential for error and reduce the need for mailing media.

Eligibility Requirements

The Employment Commission determines eligibility using both monetary and non-monetary requirements as discussed below. Each claimant must meet both monetary and non monetary requirements to receive their initial unemployment benefits payment.

The Employment Commission has a relatively short time period to obtain the information and make eligibility determinations. The federal government requires the Employment Commission to pay unemployment benefits within 14 days of the first eligible week, allowing a one week waiting period.

For example, an individual files a claim with an effective date of October 3 which falls into the benefit week ending October 9. The first week subsequent to the week of the claim is a one week waiting period, so the 14 day requirement starts at the end of the following week on October 16. In this example, the Employment Commission must have completed all work so that Employment Commission can pay the unemployment benefit by October 28. This requires the Employment Commission to process unemployment claims and make eligibility determinations in a fairly short time period and delays in getting information, either from the claimants or the employers, can impact how well the process works.

Monetary Eligibility – The claimant must have earned sufficient wages to be eligible for unemployment benefits. The amount of wages earned helps determine the weekly benefit amount as well as the length of time you can receive benefits based on the provisions of the Code of Virginia. Generally, to be eligible for benefits, an individual must have earned at least $2,700 in two quarters (combined) of the base period, which is the first four of the last five completed quarters prior to the date of the claim.

Non monetary Eligibility – A claimant must have lost their job due to no fault of their own.

In addition to these requirements, a claimant must also meet certain weekly requirements to continue to receive unemployment benefits. Generally, a claimant must be willing to perform work, be available for work, and make at least two job contacts every week. Not all states have work search requirements and the Employment Commission will waive these requirements in certain circumstances, such as short term layoffs where the claimant has a scheduled return-to-work date. The claimant must also accept all offers of suitable work and register for work with the Virginia Workforce Connection System. These same requirements apply once a claimant starts collecting federal extended benefits except three job contacts are required in the last tier of extended benefits. One additional requirement is the claimant must report any wages and earnings from any source every week.

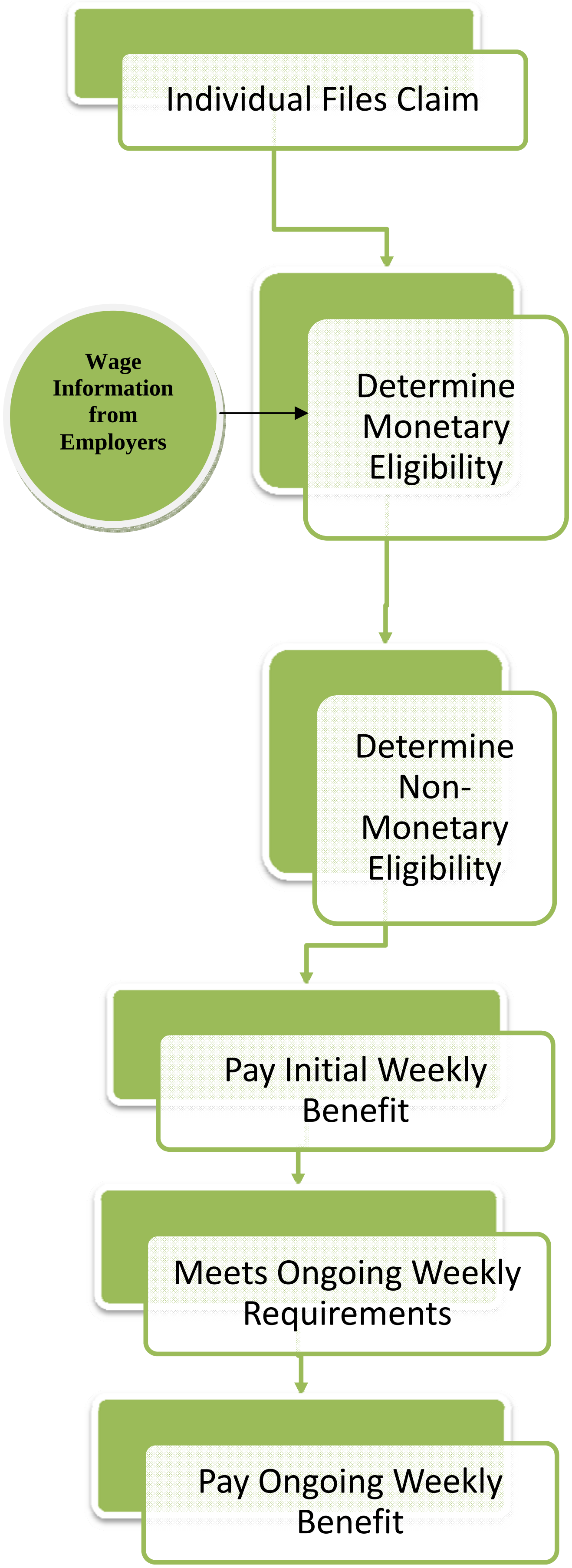
A claimant is eligible to receive their state unemployment benefits for up to a year from the effective date of their claim. If a claimant has exhausted his benefits, and files a new benefit claim, he is not eligible for a new claim until after expiration of the benefit year ending date on the first claim. A claimant can never draw benefits twice from the same wages. If a claimant files a second claim after the expiration of the benefit year ending date on the first claim without having worked 30 days or 240 hours with an employer, the Employment Commission considers this claim a "double-dip" and the claimant is not eligible.

How the Eligibility Determination Process Works

To determine eligibility, the Employment Commission uses information provided by the claimant as well as information from their employer. The Virginia Automated Benefits System (VABS) is the Employment Commission's primary system for processing and paying unemployment benefit claims.

There are several different processes that occur, some simultaneously, when a claimant submits a claim for unemployment benefits. These processes involve multiple parties and each party has important responsibilities in the process and must perform their task in a timely manner in order for the process to work correctly. We have included a flowchart on the following page to illustrate the steps in the process at which the Employment Commission performs various edits and procedures to help ensure the accuracy of the data.

Unemployment Benefit Claims Process



Individual Files Claim An individual can file a claim either on line, over the phone, at a local office, or by mail. The individual provides name, address, social security number, and employer information for the last 18 months. The individual also provides information on the reason for separation from the job and their availability to work.

VEC matches name, social security number, and the date of birth to Department of Motor Vehicle (DMV) records to verify the validity of the information.

Determine Monetary Eligibility Using the social security number, VEC pulls wage information for the individual over the last five quarters to determine if they meet the monetary eligibility requirements to receive benefits. VEC pulls this information from quarterly wage files sent from employers unless the individual is a federal or military employee or had out of state wages. If this is the case, VEC pulls this information from a national database.

VEC generates a monetary determination letter and sends it to the individual. The letter shows employer and wage information for the last four quarters as well as estimated benefits. The letter asks the individual to contact VEC if any of the information is incorrect.

Determine Non-Monetary Eligibility VEC determines if the individual is eligible for benefits by making sure the reason for separation from their job is a lack of work (e.g., not eligible if they were fired). If this claim is not the individual's first unemployment claim, VEC also makes sure the individual has met the applicable paid work requirements of 30 days/240 hours.

VEC sends the employer a Wage and Separation Report so they can confirm the individual's reason for separation. The employer must return this report within nine days. If the employer does not return the report in this time frame, VEC assumes the reason for separation given by the individual is correct. If the employer returns the Report and the reason for separation is anything other than lack of work, VEC assigns the case to a Deputy who conducts interviews or hearings and makes an eligibility determination.

Weekly Requirements *VEC continues to pay weekly benefits if the individual meets the weekly eligibility requirements. Individuals must be available to work and actively seek work each week. Individuals must provide information weekly to VEC on their work search activities and to confirm their work availability. They must also report any other wages and earnings during the week. The individual can provide this information over the phone, Internet or on a form.*

As shown in the flowcharts, the eligibility determination process involves multiple parties and information from the claimant as well as the employer. Another factor that impacts the eligibility determination process is the relatively short time period the Employment Commission has to obtain the information and make eligibility determinations. As a result, there are several points in the process where incorrect or untimely data can affect the accuracy as well as the validity of the benefit claim.

The Employment Commission performs a number of edits and verifications before paying a benefit claim to ensure benefit payments are accurate and to prevent errors or irregularities. The flowcharts on the previous pages show these edits and verifications and we list them here.

1. When a claimant initially applies, the Employment Commission performs the following verifications of a claimant's identity and information.

    - Verifies the name, social security number, date of birth, and gender as well as any pension income information against the Social Security Administration records.

    - Verifies the claimant's name, social security number and date of birth with Department of Motor Vehicle (DMV) records.

    If any of this information does not match and the Employment Commission cannot determine the reason, the Employment Commission sends a letter to the claimant asking them to report to a local office with proof of identity. The Employment Commission will not process their claim until they have a valid social security number.

    If the individual is not a U. S. Citizen, the Employment Commission verifies their Alien Registration Number against Homeland Security records. If the verification comes back showing the claimant is not legally able to work in the United States or Homeland Security returns no confirmation, the Employment Commission assigns the case to a Hearings Officer for investigation.

2. VABS checks to make sure the claimant is eligible for benefits if they have previously received benefits. A claimant is not eligible for a new claim until after expiration of the benefit year ending date on the first claim. The Employment Commission will not process the new claim unless the claimant meets this requirement.

3. VABS generates a Monetary Determination Letter which shows all of the employers and wages for the four quarters of the base period as well as estimated benefits (weekly benefit amount and how long they would receive them). If any of the information is incorrect, the Employment Commission asks the claimant to contact them.

4. VABS also generates a Wage and Separation Report for the employer to confirm the reason for separation given by the claimant, and a request to return this information within nine days. The system only generates this report if the claimant indicates lack of

work as the reason for separation. If employer does not return the report, the Employment Commission assumes the information from the claimant is correct and they do not contact the employer.

5. VABS generates a letter to reimbursable employers letting them know that there is a claim and their percentage of wages in the base period and their total "potential" charge if the claimant receives all the benefits. The letter instructs these employers to contact the Employment Commission if the information is not correct or they are disputing the charges.

6. The Employment Commission reconciles quarterly wage and tax files from employers to determine if the information is correct. This wage information is the basis for the amount and duration of weekly benefits. The Employment Commission has established some thresholds for following up on variances that come up during the reconciliation process.

   The reconciliation process will not detect 100 percent of the errors. The thresholds use the number of employees an employer has and the amount of the variance. The Employment Commission designed the reconciliation this way because there are numerous errors and it is time consuming to research and resolve all errors. They investigate the variances that meet the threshold and follow up with employers to correct the information.

Once a claimant meets the eligibility requirements and receives their initial benefit payment, they must meet weekly eligibility requirements to continue to receive benefit payments. The claimant receives a letter after their initial weekly benefit to remind them of their responsibilities and what they need to do in order to continue to receive their benefits.

In order to meet the weekly requirements, the claimant has to contact the Employment Commission and provide information on their job search activities and availability for work. While the requirement for adequate work search is set forth in the <u>Code of Virginia</u>, the Employment Commission has responsibility for defining adequate work search and what information the claimant needs to provide. The claimant must provide the name, address, and contact information for each job search contact that week including what the result was. The claimant can contact employers either in person, through the Internet, or by fax. The Employment Commission does not consider responses to blind ads or telephone calls to employers adequate to meet the work search requirements.

Claimants can provide their weekly information via the voice response system, the Internet, or a Continued Claim for Benefits form. The Employment Commission transfers this information into VABS. The Employment Commission does not confirm this information unless the case is under review for some reason. If the claimant has not provided the weekly information, their benefit payments stop immediately.

Improper Payments and How They are Detected

Many of the verification procedures above rely on either the claimant or the employer submitting information to the Employment Commission. If either the claimant or employer submits the required information late, incorrect, or not at all, this can impact the eligibility process and can result in an improper payment. For purposes of this report, an improper payment describes a situation where an eligible individual does not receive a benefit, an ineligible individual receives a benefit, or an individual is eligible but receives the wrong benefit payment amount.

Unemployment benefit improper payments can occur for a variety of reasons, and the Employment Commission uses different methods to detect improper payments. For example, if an employer reports a change in wages earned during a quarter and an individual is receiving a benefit payment, VABS will generate a report of changes in wages earned and any effect that the change would have on a benefit payment. These reports go to the Monetary Determination Unit to review and determine if the change in benefits is correct.

Employment Commission staff receive questions from employers and other individuals about individuals receiving benefit payments and follow up on these specific cases. If the staff determines there are questions about an individual receiving benefits, they will take appropriate action to either stop or adjust the payment depending on the results of their review.

One other tool the Employment Commission uses to detect improper payments is quarterly statements sent to all employers that list employees who are receiving benefits. Employers refer to this letter as a charge statement or a billing statement, depending on how the employer pays their unemployment taxes. The Employment Commission asks employers to review these statements and report any incorrect information, or any individuals they do not believe should be on their statements or individuals they have rehired. The Benefit Payment Unit receives these comments and follows up to determine if a claimant's benefit or the employer's charges requires adjustment.

Overpayments are improper payments where the individual receives too much in benefits. While underpayments do exist, once they are detected the Employment Commission adjusts the individual's benefit amount and gives them the amount underpaid to date. For the remainder of this report we will deal only with overpayments of benefits to individuals and the processes to detect, correct, and collect these amounts.

Benefit Payment Control Unit

The Employment Commission has a unit devoted to detecting and addressing overpayments called the Benefit Payment Control Unit. This unit, in the Central Office, has a staff of ten employees who work with twelve investigators located throughout the state to assist in investigating overpayments. The Unit's workload has increased significantly over the last few years with the overall increases in activity. The Unit has added four investigator positions, but they are still handling about twice the number of cases. To meet the increased caseload, the Unit has changed processes to be more efficient and staff must work overtime.

The primary duties of the Benefit Payment Control Unit include the following.

- Reviewing benefit claims and detecting overpayments
- Establishing the amount of any overpayment and recovering the funds
- Instituting procedures to prevent future overpayments

The Benefit Payment Control Unit has a number of different tools and processes developed over time to address the more common methods that individuals use to receive benefit payments they do not deserve. Most of these tools include automated cross matches between various data sources to identify possible exceptions for follow up. We discuss the most significant detection tools below, the New Hire Reporting Cross Match and the Wage Tax Reports Cross Match. Both of these cross matches occur at the federal level so the match includes wage and payroll information from all states. Both of these matches address situations where the claimant finds a job but does not inform the Employment Commission and therefore continues to collect benefits. The Employment Commission has a three year time frame which allows them to file charges related to benefit overpayments for up to three years from the date of the payment.

New Hire Reporting Cross Match

One of the most effective tools that the Employment Commission has for detecting overpayments is the New Hire Reporting Cross Match. The U.S. Department of Labor mandated that all state employment agencies perform this match starting in 2009, but the Employment Commission has participated since 2005. The Employment Commission performs this match on a weekly basis.

This match relies on new hire reporting information collected in Virginia as well as other states. Section 63.2 – 1946 of the Code of Virginia and federal law requires employers to report newly hired and re-hired employees to a state and federal directory within 20 days of their hire date.

In Virginia, the Division of Child Support Enforcement in the Department of Social Services operates the New Hire Reporting Center (Center). They collect new hire information from Virginia employers and maintain this in the Virginia State Directory of New Hires. The Center provides information from the Virginia State Directory to the National Directory of New Hires maintained by the U.S. Department of Health and Human Services (HHS).

Each week, the Benefit Control Payment Unit sends a list of all benefit claimants from the past seven weeks to HHS. The Employment Commission uses seven weeks because they estimate this will give them the best coverage for detecting overpayments. HHS matches information in the National Directory of New Hires against the Employment Commission's list of claimants and reports individuals who appear on both lists to the Employment Commission for follow up. If someone appears on both lists, there is a possibility the individual has gotten a job and has not reported this; therefore, they have continued to receive unemployment benefits. The Benefit Payment Control Unit follows up on this to determine whether an actual overpayment occurred.

Wage Tax Reports and the Claims Wage File Cross Match

Weekly, the Employment Commission also sends information on all claimants who received benefits that week to HHS. The information sent excludes all new hire matches already identified. The Employment Commission also sends information on all wages reported by employers to HHS on a quarterly basis.

HHS matches the claimant files against the wage files from Virginia as well as other states quarterly to identify individuals who are on both lists. This cross match is designed to catch claimants who have new jobs but whose employers did not report them as new hires. This match detects claimants not detected by the New Hire Reporting Cross Match. The results of the cross match go to the Benefit Payment Control Unit for follow up.

Benefit Payment Control Unit staff review the cross match results, as well as other cases referred to them, and prioritize cases for review and follow up. Managers assign cases a priority level and internal procedures set time frames for each investigation depending on the priority level. For example, case specific complaints receive a priority 1 assignment that set a 30 day timeframe for research and follow-up.

Benefit Payment Control Unit staff and investigators research individual cases to identify which instances are true overpayments. When the Unit detects a potential overpayment, VABS generates a letter to the claimant to let them know the case is under review and may request additional information. VABS will automatically stop benefit payments in ten days unless they receive additional information from the claimant or employer. For example, if the claimant came up in the New Hire Cross Match, the claimant must provide information on their new employer, when they started work and how much they have earned. Benefit Payment Control Unit staff will also contact the employer and request additional information while researching the case.

If the Benefit Payment Control Unit staff determines that there has been an overpayment, they establish an overpayment on VABS, giving each overpayment case class, cause, and detection codes. VABS then also generates a notice to the claimant notifying them of the overpayment and the amount of money owed to the Employment Commission with information on their appeal rights.

The Unit manager uses a Case Assignment System to track and monitor caseloads and compliance with established timeframes. Regional managers review caseload reports on a monthly basis that show each investigator’s work load (cases assigned, completed, outstanding, and delinquent). Unit staff and investigators have had difficulty meeting the established timeframes for following up on cases due to the increased caseloads over the last several years.

The following caseload information shows activity in the Benefit Payment Control Unit for the eleven months ended September 30, 2010. These cases result from various matches of potential overpayments or referrals to the Unit for other reasons.

Summary of Caseload Activity as of September 30, 2010

Beginning Number of Cases Outstanding	17,673
New Cases	42,095
Cases Completed	(38,758)
Cases Outstanding at September 30	21,010

Of the cases outstanding as of September 30, approximately 11,000 are delinquent, meaning the Unit has not completed its investigation within the established timeframes. The cases outstanding represent potential overpayments under research by the Unit, but they have not yet been established as an overpayment. The Employment Commission has stopped benefit payments while the case is under review. Of these cases outstanding, the Unit estimates that half will be overpayments.

Quality Control Programs

The Employment Commission also has a Quality Assurance Unit which performs several federally mandated quality control programs including the Benefit Accuracy Management (BAM) Program and the Benefit Timeliness Quality (BTQ) Program. The BTQ program focuses on timeliness of payments and whether hearings officers' decisions appear appropriate. The BAM program focuses on the accuracy of unemployment benefits paid and claims denied. This program covers state unemployment benefits as well as unemployment compensation for federal employees and ex-members of the military, but does not cover extended federal benefits.

Under the BAM program, the Quality Assurance Unit selects a sample of benefits paid every week based on an algorithm provided by the U.S. Department of Labor (Labor) designed to select a statistically valid sample. Examiners review the cases to ensure that the Employment Commission properly processed the unemployment claims. The federal government establishes the samples sizes and sets the guidelines for reviewing cases and evaluating errors. BAM investigators will review all the eligibility requirements related to that week including verifying work search activities reported by the claimant.

If the Quality Assurance Unit identifies errors during the BAM process, they refer the individual cases to other Units in the Employment Commission for correction or Benefit Payment Control Unit staff to establish overpayments. Both the U.S. Department of Labor and the Employment Commission use BAM results to identify system wide problems for correction and future error prevention.

The Quality Assurance Unit sends their sample results to the Labor who generates an annual report, called the BAM report. This report includes results for a calendar year, summarizes the sample results, and projects these results onto the universe of all claims paid during the year. Using this information, Labor also calculates a BAM "operational rate" which excludes certain eligibility requirements which are not consistent among states, and therefore allows states to compare their performance. Labor also reports the operational rate and how this relates to the amount of overpayments a state has established.

If the Employment Commission does not meet certain criteria set by Labor, they prepare an action plan to address the issues and improve their performance. These corrective action plans are included in the State Quality Service Plan. Labor has requested that states analyze their BAM data to better identify root causes for overpayments and strategies to reduce overpayments. Labor has instructed States to consider this information as they develop their State Quality Service Plans for 2011.

Recovering Overpayments

The Code of Virginia requires that individuals who improperly receive unemployment benefits must repay them. If the reason for the overpayment is an administrative error, the Code of Virginia allows more flexibility in how the Employment Commission can arrange repayment of benefits.

As discussed above, the Benefit Payment Control Unit staff establishes an overpayment on VABS, which generates a notice to the claimant. The notification resembles a bill although it is not an official bill. The following month, the claimant does receive the first 'official' bill. If there is no response from the claimant, the Employment Commission sends past due notices at 30 days and 60 days. If there is no activity on the account after 90 days, the Benefit Payment Control Unit transfers the account to the Accounts Receivable Section for further collection efforts.

The Accounts Receivable Section sends a notice to the claimant stating they are 90 days past due and their account will either go to a collection agency or to the Attorney General's Office for further action. The Employment Commission sends accounts with balances less than $3,000 to a collection agency. If the account balance is over $3,000, the Employment Commission transfers the account to the Attorney General's Office for further collection efforts. The Employment Commission also uses other methods for trying to collect overpayments, including Tax Debt set off and offsetting any future unemployment benefits.

If a claimant's account is over two years old, the Employment Commission considers the account uncollectible and writes it off. In this case, the Employment Commission writes off the account by moving it to inactive status which could allow for future collection. There are some situations where the Employment Commission will completely discharge an account and take it off of the system. This occurs for accounts that are over seven years old and situations where the claimant has died or declared bankruptcy.

There are numerous actions that can impact this process and extend the collection notice period. For example, claimants can appeal the Employment Commission decisions. Another action that impacts the process is the claimant setting up a payment plan, in which case the Employment Commission will send monthly bills until the claimant settles the account in full.

Analysis of Overpayment Information and Recoveries

As part of our review, we analyzed the overpayment data from the Virginia Automated Benefit System (VABS) for fiscal years 2008 through 2010. This data reflects the accounts and amounts of actual overpayments detected and recorded in each of these years and includes all types of benefits. At any point in time, the Employment Commission may not have detected some overpayments.

The following table shows total benefits paid and total overpayments found for each of the last three fiscal years. Various extended federal benefit programs went into effect in fiscal year 2009 and continued into fiscal year 2010. As an example, for fiscal year 2010 the $40 million in overpayments represents approximately $29 million in the Unemployment Insurance Program benefits and $11 million in various federal extended benefits.

Summary of Benefits and Overpayments by Fiscal Year

	2008	**2009**	**2010**
Unemployment Benefits Paid	$435,433,784	$1,121,257,378	$1,880,184,481
Overpayments Established	$ 14,114,585	$ 21,935,643	$ 40,155,024
Percentage of Overpayments Established	3.24%	1.96%	2.19%

Source: Data obtained from VEC through the Virginia Automated Benefits System

As we discussed earlier in this report, the unemployment benefit claims process relies on information from claimants and employers and there are several points in the process where inaccurate information can result in an overpayment. We analyzed the overpayment data to determine what were the types of overpayments established, what caused the overpayments, and how the Employment Commission detected the overpayments.

Cause of Overpayments

There is a class code, a cause code, and a detection code for each overpayment established in VABS. We determined that analyzing the overpayment data by cause codes would be the most effective way to get a better understanding of the cause of overpayments in general. There are almost 40 different cause codes. We analyzed fiscal year 2010 overpayment data and summarized our analysis below. Based on the data we reviewed, the average amount of an overpayment established in 2010 was $1,165.

Summary of Overpayments by Cause – Fiscal Year 2010

Cause Code in VABS	Number of Overpayment Cases	Dollar Value of Overpayments	Percentage of Overpayment (based on $)
Unreported wages	15,964	$11,424,608	28%
Non-monetary determination	5,615	13,097,377	32%
Incorrect reason for separation	4,787	8,378,092	21%
Miscellaneous	1,905	2,020,979	5%
Error in computing amount	1,537	731,085	2%
Other	4,663	4,502,883	12%
Totals	**34,471**	**$40,155,024**	**100%**

Source: Data obtained from VEC through the Virginia Automated Benefits System

As shown above, over 80 percent of the overpayments in fiscal year 2010 fall into three causes – unreported wages, non-monetary determination, and incorrect reason for separation. To better understand these causes, we discuss each in more detail below with examples of how these overpayments could occur.

The "*Unreported Wages*" cause generally means that the claimant had wages they did not report. The New Hire Cross Match is the usual detection method of overpayments of unreported wages.

In discussing this overpayment with Employment Commission staff, they stated that sometimes this occurs because there is confusion over when benefits payments stop. Some claimants do not understand they are no longer eligible for unemployment benefits on the day they start a new job, not the day of their first paycheck.

Example:

A claimant gets a new job but continues to call in each week to give information on work search and work availability as if they have not gotten a job. The Employment Commission makes the benefit payment to the individual because they have met the weekly requirements. The claimant subsequently shows up on the New Hire Cross Match, which detects the overpayment.

The "*Non-Monetary Determination*" overpayments cause is a code normally used by the Benefit Payment Control Unit until they finish their investigation and determine the more specific reason for the overpayment. The Benefit Payment Control Unit normally changes this code to another code when they complete the investigation. Based on our review of prior year's overpayment data, the Benefit Payment Control Unit reclassifies the majority of overpayments in this category to "*Incorrect Reason for Separation*."

The "*Incorrect Reason for Separation*" cause is for overpayments where the claimant was not eligible due to an incorrect reason for separation. These types of overpayments can occur for multiple reasons. One common situation is when an employee provides an incorrect reason for separation and the employer does not provide information in time for the Employment Commission to stop benefit payments. Another situation is shown below:

Example:

The claimant files a claim and indicates they lost their job due to lack of work. The Employment Commission sends a Wage and Separation Notice to the employer to confirm the reason provided by the claimant. The employer returns the notice indicating the claimant lost their job for misconduct. The Employment Commission schedules a fact finding hearing to gain more information, but the employer is not available for the hearing and does not participate. As a result, the Employment Commission makes the eligibility determination based on the information provided by the claimant. The employer subsequently appeals the decision and provides additional information, causing the Employment Commission to reverse the eligibility decision and establish an overpayment.

The "*Miscellaneous*" cause occurs when a change in wage information affects the length of time a claimant can receive benefits. VABS reports that the benefit payment exceeds the period authorized. Again, the Benefit Payment Control Unit researches these accounts and they may be subsequently reclassified to another cause code. We discuss the "*Error in Computing Amount"* cause later in this report in the section "*Additional Analysis of Overpayments Due to Administrative Errors*."

<u>*Overpayments Sample*</u>

We selected a sample of 50 fiscal year 2010 overpayment cases for review to meet several objectives. First, we wanted to obtain a better understanding of the situations resulting in overpayments at the individual case level. We also wanted to gain a better understanding of the documentation the Employment Commission maintains on individual overpayment cases and to determine consistency of overpayments coding. Below is a summary of the cases we reviewed. While we selected some of our cases randomly, we did include certain high dollar overpayments in our sample for review. As a result, the average dollar amount of overpayments in our sample is higher than the average overpayment amount cited earlier in this report.

Summary of Overpayments Sample

# of Overpayment Cases Reviewed	50
Average Dollar Amount of Overpayment	$2,761
Average # of Weeks Overpaid	8.6 weeks

We reviewed the cause codes in VABS as well as additional documentation in VABS and discussed some cases with staff from the Benefit Payments Controls Unit. We found that, overall, the cause codes in VABS appeared reasonable based on our review of the documentation for the cases. In our sample of 50 cases, we determined the following causes for the overpayments.

Summary of Overpayment Sample by Cause – Fiscal Year 2010

Cause Code in VABS	**Number of Cases**	**Dollar Value of Overpayments**	**Percentage of Overpayments (based on $)**
Unreported Wages	15	$24,701	18%
Non Monetary Determination	11	36,175	27%
Incorrect Reason for Separation	8	41,044	30%
Error in Computing Weekly Wage Amount	6	5,224	4%
Other	10	30,891	21%
Total	50	$138,035	100%

The causes of overpayments in our sample reflected similar trends as we saw in the analysis on all overpayments established in fiscal year 2010. The difference in the percentage of overpayment cases due to "*Error in Computing Weekly Amount*" is due to the fact that we selected our sample to obtain adequate coverage of overpayments classified as Administrative Errors to ensure we adequately addressed issues related to the legislative request.

Class of Overpayments

In addition to assigning each overpayment a cause code, Benefit Payment Control Unit staff also classifies each overpayment with a class code. The table shows the value of overpayments by class.

Summary of Overpayments by Class – Fiscal Years 2008 - 2010

	2008	2009	2010
Class of Overpayment	**Dollar Value of Overpayments**	**Dollar Value of Overpayments**	**Dollar Value of Overpayments**
Criminal Fraud	$ 5,556	$ -	$ -
Dismissed	92,503	27,186	1,240
Administrative Error	260,817	864,646	1,696,464
Administrative Fraud	2,557,515	2,639,283	4,646,279
Java (Reversal)	5,307,591	6,863,666	4,992,144
Non-Fraud	5,034,894	10,221,533	26,055,878
Pending Criminal Fraud	852,179	1,314,179	2,762,209
Statute of Limitations	3,530	5,150	-
(blank)	-	-	810
Total	**$ 14,114,585**	**$ 21,935,643**	**$ 40,155,024**
Unemployment Benefits Paid	**$435,433,784**	**$1,121,257,378**	**$1,880,184,481**
Overpayments as a percentage of Benefits Paid	**3.24%**	**1.96%**	**2.19%**

The Benefit Payment Control Unit assigns each account a Blank class while under review or pending a correction. The Unit then reclassifies the account based on its review into one of the following classes.

Criminal Fraud - When a claimant knowingly and willfully makes false statements (minimum of three) resulting in an overpayment amount that is determined to be prosecutable by the applicable locality.

Dismissed - The claimant is prosecuted for fraud and the judge dismisses the case. This can happen because of inadequate evidence or because the judge lets the claimant consent to the acts committed and works out a payment plan in return for a dismissal.

Administrative Error (Agency Fault) - The Employment Commission had the information needed to make the correct determination and failed to look at the documentation appropriately.

Administrative Fraud – The claimant knowingly and willfully makes false statements (minimum of three) resulting in overpayments that do not meet the requirements for prosecution.

Java - A reversal of a written determination to award benefits. When a payment is questionable, a deputy will hear the individual circumstances and apply the applicable provisions of law to determine a claimant's qualification to receive weekly benefit payments. Many times, either the claimant or employer will appeal this decision if they do not agree with the decision. A "Java" overpayment occurs when the appeal causes a reversal of the decision which results in an overpayment of benefits. Java comes from the original court case of this matter.

Example: A claimant states they lost their job without just cause and the deputy decides this is correct. The employer then appeals the decision and brings more evidence to the table to support the misconduct of the employee. The new facts cause a reversal of the original decision and therefore the claimant was overpaid benefits.

Non-Fraud - The claimant makes false statements but there is no evidence to suggest that it was a deliberate attempt to conceal information.

Pending Criminal Fraud - The claimant is under investigation for criminal fraud awaiting trial.

Statute of Limitations - The overpayment was discovered after three years and is not prosecutable.

Employment Commission Actions Other than Recovery

Other than just recovering the overpayment, the Employment Commission takes other actions against individuals that improperly receive benefits. For those individuals where the overpayment is the result of a process such as a change in a hearing decision or a misunderstanding of the eligibility criteria, the Employment Commission limits itself to only recovery of the overpaid amount. The claimant can continue to receive benefits and repay the overpayment through a deduction in their weekly benefits payments. These cases are in the classes "Administrative Error Agency Fault", "Java", and "Non-Fraud".

"Java" and "Non-Fraud" overpayments have increased in both account volume and amount during the recession and reflect the increased activities of the Employment Commission. The "Non-Fraud" class has specifically increased as a result of the number of claimants who are unfamiliar with the process.

"Criminal Fraud," "Administrative Fraud," "Pending Criminal Fraud," and "Dismissed" represent accounts the Employment Commission is actively pursuing. The Employment Commission's investigators work with both the Attorney General's Office and local Commonwealth's Attorneys to convict individuals who have knowingly and deliberately attempted to obtain benefits to which they are not entitled. "Criminal Fraud" and "Dismissed" class cases represent matters which have gone or are going before the courts for misdemeanor consideration.

"Administrative Fraud" is a class of cases which would not result in a misdemeanor prosecution, but do include circumstances in which an individual has knowingly and deliberately attempted to obtain benefits they should not receive. In these cases, the Employment Commission identifies these individuals on VABS, and they cannot receive any future benefits until they have made restitution of the benefits received.

Overpayments Due to Administrative Errors

During our review, we also performed additional analysis on overpayments established that were classified by the Employment Commission as "Administrative Errors." The Employment Commission generally uses this class of overpayment when the Employment Commission has correct information but does not interpret it correctly and an overpayment results. This was an area of interest in the legislative request that we received. We analyzed the overpayment data for overpayments that were classified as administrative errors as shown below.

Summary of Overpayments due to Administrative Errors (Agency Fault) by Fiscal Year

	2008	**2009**	**2010**
Total Overpayments	$14,114,585	$21,935,643	$40,155,024
Overpayments due to Administrative Errors	$ 260,818	$ 864,646	$ 1,696,464
Percentage of Overpayments due to Administrative Errors	1.85%	3.94%	4.22%

Source: Data obtained from VEC through the Virginia Automated Benefits System

Overall, this type of overpayment has increased over the last several years which is more than likely due to the increased workload at the Employment Commission. Although these types of overpayments account for less than five percent of all overpayments in fiscal year 2010, we further analyzed the administrative errors classification for more information on causes of these types of overpayments and present the data below.

Summary of Overpayments due to Administrative Errors by Cause - Fiscal Year 2010

	Number of Overpayment Cases	**Dollar Value of Overpayments**
Administrative Errors Due to:		
Error in Computing Claim Amount	782	$ 730,489
Payment During Ineligible Period	143	253,883
Pending Determination	176	348,176
Other	283	363,916
Totals	**1,384**	**$1,696,464**

Source: Data obtained from VEC through the Virginia Automated Benefits System

The most common cause of administrative errors was "*Errors in Computing Claim Amount*." The Employment Commission uses this classification if it incorrectly calculates a claimant's weekly or maximum amount because there were errors in the wage information. More than half of the administrative errors were of this type so we reviewed several cases in our sample to better understand how this type of error occurs.

Example:

A claimant applies for unemployment benefits, meets eligibility requirements and begins receiving unemployment benefits. This eligibility determination uses quarterly wage information received from the employer. Subsequently, the Employment Commission identifies an error in the wage information used as the basis for the eligibility determination and corrects the error; however, this results in a new benefit amount and an overpayment because the claimant was receiving too much in benefits.

In the example above, the wage information originally sent in by the employer was not correct and the Employment Commission did not detect this error before making the benefit payment. Although the Employment Commission has controls in place to detect errors, they may not detect all errors.

For example, the reconciliation of the quarterly wage and tax information should detect errors in the wage information; however, the reconciliation process will not resolve 100 percent of errors. The process uses thresholds and other parameters to test the information and detect errors; however, these are tests are not full audits of the information, so will allow errors to occur.

Another situation that can occur is the claimant did not review the monetary determination letter and did not contact the Employment Commission to notify them of any errors. This control is dependent on the claimant reviewing the information and contacting the Employment Commission with any errors.

While the amount of errors may represent a significant amount, the methods to eliminate or reduce the number of errors further could add significant costs and administrative time for the Employment Commission, claimants, and employers. Reducing these errors would require the Employment Commission to receive both more timely and accurate data which will add costs to the employers to supply the information. Making sure that the data is completely accurate and without error before making a benefit payment would delay the delivery of benefits and violate the federal regulation over the timeframe. Overall, the number of overpayments due to administrative errors is not large in relation to total payments, and the cost of obtaining better information to reduce the number would be excessive.

Analysis of Overpayment Recoveries

Claimants who receive unemployment benefits for which they are not entitled must repay the Employment Commission. We reviewed the Employment Commission's receivable balances related to benefit overpayments for the past three years. Amounts presented below are <u>net</u> of estimated uncollectible accounts.

Amounts Due to VEC for Overpayments - As of June 30

Fiscal Year	Gross Receivables for Overpayments	Estimated Uncollectible	Ending Balance
2008	$19,709,043	$14,584,692	$5,124,351
2009	$25,006,106	$19,004,640	$6,001,466
2010	$41,879,533	$32,008,527	$9,871,006

Source: VEC Quarterly Receivable Summary

The benefit overpayments due to the Employment Commission over the last three years have increased which reflects the increased volume of benefits paid out during this period. We further analyzed the overpayment activity related to fiscal year 2010 and summarized it below.

Summary of Accounts Receivable Activity for Overpayment

Beginning Accounts Receivable for Overpayments at 7/1/09	$25,006,106
Additions – new overpayments established	38,667,025
Collections on overpayments	(13,053,157)
Amounts written off	(8,740,441)
Ending Accounts Receivable for Overpayments at 6/30/10	$ 41,879,533
Less: Amounts Estimated to be Uncollectible	($32,008,527)
Net Accounts Receivable for Overpayments at 6/30/10	$ 9,871,006

Source: VEC Quarterly Receivable Summary

We reviewed the Employment Commission's aging of these accounts and over half of these balances are over 6 months old. The Employment Commission estimates they recover 40 to 50 percent of overpayments. This estimate appears reasonable based on collection statistics over the last several years; however, the percentage collected has decreased over that last two years which could be due to increased workload and the number of cases for collection. In addition, emphasis at the federal level in recent years has focused more attention on the establishment of overpayments than the collection of overpayments. As a result, the Employment Commission has focused resources on the overpayment establishment process and this may have negatively impacted collection efforts.

Fiscal Year	Overpayments Established	Overpayments Collected	Percentage Collected
2008	$14,114,585	$ 6,322,892	44.79%
2009	$21,935,643	$ 8,586,708	39.15%
2010	$40,155,024	$13,053,157	32.51%

Source: VEC Quarterly Receivable Summary

There are several factors that affect the Employment Commission's ability to recover overpayments. First, some individuals remain unemployed or file bankruptcy and do not have the financial means to repay the amounts. The appeals process can also affect collection efforts. If an overpayment has occurred but the claimant appeals the case, collections efforts cannot start until the resolution of the case. Also, if a claimant moves to another state, the Employment Commission's ability to collect the overpayment is limited.

Analysis of Benefit Accuracy Measurement Reports

The Benefit Accuracy Measurement (BAM) program report is a measure of the Employment Commission's performance, which media and legislators often use. The federally mandated program examines performance of the unemployment insurance benefit system, both for individual states and nationally. The BAM program is the only method the Employment Commission currently uses to generate information on estimated overpayments.

As discussed earlier in this report, the Employment Commission has a Quality Assurance Unit in the Central Office that has responsibility for this program. This Unit tests a weekly sample of unemployment benefits paid to ensure the Employment Commission staff are properly checking the eligibility requirements, and the Unit forwards these sample results to the U.S. Department of Labor (Labor). Using the sample results, Labor prepares the BAM annual report on a calendar year basis. The most recent report available for our review was for calendar year 2009 which the Employment Commission received in May 2010, and we show the summarized results below.

Summary of BAM Report Statistics – Calendar Year 2009

	Percentage (based on dollars)	Estimated Dollar Value *
Proper Payments	85.3%	$969,579,855
Overpayments	14.6%	165,852,703
Underpayments	.1%	1,136,569
Total	100.0%	$1,136,569,127

**Projections based on calendar year 2009 UI benefit payments*

The BAM statistics above use a sample of 368 cases, as determined by Labor; the sample size in previous year was 480 cases but the Employment Commission requested and received approval to decrease the sample size for 2009 due to resource issues. Labor uses a statistical basis for sample selection and evaluation meaning they are 95 percent confident that the error rates listed above are within +\- 3.7 percent.

The BAM report shows a projected overpayment rate of 14.6 percent, which is significantly different from the percentage of overpayments established by the Employment Commission. As shown earlier in this report, overpayments established in VABS were approximately two percent for both fiscal years 2009 and 2010. While these two sets of data use different timeframes and do not measure the same thing, there should be a correlation between the estimated percentage of actual overpayments and the percentage of detected and established overpayments.

To further understand the BAM statistics, it is necessary to review the sample results by cause. Labor establishes these causes and they differ slightly from other cause codes in VABS and presented in this report. Below is the breakdown of the 14.6 percent overpayment rate from the BAM report by cause to show the specific errors that resulted in overpayment errors in the sample.

BAM Overpayment Rate by Cause – Calendar Year 2009

Cause	Percentage (based on dollars)	Estimated Dollar Value
Work Search Issues	9.7%	$110,189,810
Separation Issues	1.8%	20,447,595
Benefit Year Earnings Issues	1.5%	17,039,661
Other Eligibility Issues	.7%	7,951,841
Other Issues	.7%	7,951,841
Base Period Pay Issues	.2%	2,271,955
Total	14.6%	$165,852,703

Two thirds of the overpayments in the sample were due to work search errors in meeting the weekly eligibility requirements. These requirements are that the claimant being willing and available to work and they make at least two work search contacts. As part of their review, BAM examiners determine if the claimant met the weekly job search requirements and they follow up with both the claimant and relevant employers to confirm this information.

There are various situations that can occur which result in the classification of work search errors as overpayments. Frequently, the BAM examiners cannot confirm the work search information for a number of different reasons and if this occurs, the BAM examiner classifies this as an overpayment.

To better understand the specific errors, we reviewed the calendar year 2009 BAM sample cases classified as overpayments. We reviewed the Error Summary Reports for each case to determine the cause assigned to the overpayment and the individual circumstances documented by the reviewer in making the determination.

There were 43 payments that were determined to be overpayments due to work search errors. These payments totaled $10,661 based on the amount they received that week. We reviewed these cases and found the following based on the dollars overpaid:

- ✓ *Forty-seven percent were situations where the claimant said they made their job contacts that week via telephone. The Employment Commission does not consider telephone contact adequate job search. As a result, the BAM examiner does not confirm any job contact information provided by the claimant and these payments are considered overpayments*

- ✓ *Thirty-seven percent were situations where the claimant did not provide enough information for the BAM examiner to confirm the job contacts. As an example, the claimant did not provide a phone number or address for the employer. The BAM* *examiner cannot confirm the job contacts that week and considers the benefit as overpayments.*

- ✓ *Twelve percent were situations where the claimant said they did not make any job contacts or the BAM examiner contacted the employer who said the claimant did not contact them. In both cases, the BAM examiner considers this an overpayment because claimant did not meet the job search requirement.*

- ✓ *Four percent were various other situations.*

Given the situations found in the overpayments above, it is possible a claimant may have satisfied the intent of the work search requirement (i.e., they did look for a job), but their benefit payment is determined to be an overpayment because they did not meet the Employment Commission's requirements for documentation or method of job search. The burden of meeting the weekly work search requirement falls on the claimant and they are advised when they apply that the Employment Commission may audit their claim and they need to retain documentation for one year.

Another issue that impacts BAM data reported is the extrapolation of the overpayment error rate onto the total population of benefits. BAM estimates a total overpayment amount by multiplying the overpayment percentage determined in the sample by the total population of unemployment benefits. There are some types of claimants included in the total benefits populations, who are not required to meet certain eligibility requirements. An example is seasonal employees or short term layoffs do not require claimant to do a job search.

Other examples include certain industries or certain areas of the state where the Employment Commission has granted a waiver to the work search requirement. In the BAM report, Labor applies the error rate to the entire population of benefits with no allowance for these types of situations. This can result in overstating the amount of estimated overpayments, but there is not sufficient data to determine how much this amount might be.

One final issue that can impact the BAM data is the recent extended federal benefit programs. The current BAM program focuses on the benefit accuracy of benefit payments under the state's unemployment insurance program and does not include extended federal benefits. Federal guidelines exclude the extended benefit programs from the BAM samples. The BAM program only covers permanently authorized programs. Federal guidelines do not include the extended benefit programs, since they are temporary and inclusion of these payments in the BAM reviews would require extensive reprogramming to both federal and state systems.

As a result, Labor does not extrapolate overpayment error rates onto the total population of benefits but just includes the state unemployment insurance program benefits and not extended benefits. This lack of federal and state reprogramming of the BAM reviews would limit the usefulness of the information for trying to determine estimated total overpayments across all benefit programs.

BAM Operational Rate

Labor also calculates a BAM "operational rate" using the sample results which allows states to compare their performance. The operational rate is the overpayment rate that excludes certain eligibility requirements which are not consistent among states. These include requirements for work search, employment service (ES) registration, base period wage issues and miscellaneous causes such as benefits paid during a period of disqualification. While most states have some sort of work search requirement, there are significant differences in who must meet the requirement, how many contacts are necessary and the contact methods the claimant can use. As an example, Virginia is one of only four states where telephone contact with an employer does not meet adequate work search requirements.

The BAM operational rate for Virginia as well as other states in our region is in the chart below. Labor computes the operational rate quarterly to allow states to measures their performance throughout the year. The operational rates shown below use the BAM statistics for federal fiscal year 2009, which is October 2008 through September 2009.

BAM Operational Overpayment Rate – Federal Fiscal Year 2009

Delaware	7.07%
Maryland	3.07%
Pennsylvania	6.20%
Virginia	3.32%
West Virginia	2.19%

Using the operational rate above, Labor also computes a rate of established overpayments. Labor uses information reported by the Benefit Payment Control Unit on established overpayments to determine a percentage of established overpayments based on the estimated overpayments from the operational rate. The rate of overpayments established computed for Virginia for the same time period was 67.4 percent, which indicates better performance than the other states in the region. Labor considers 50 percent to be the acceptable level for performance for establishing overpayments.

The BAM operational rate statistics on established overpayments are consistent with what we calculated earlier in the report. Although the time periods for the two sets of data are slightly different, when you apply the overpayment established percentage above (67.4 percent) to the BAM operational rate, you get a 2.23 percent rate for established overpayments from total benefits. This is consistent with our fiscal year 2010 calculation of 2.19 percent earlier in the report.

Projections for Fiscal Year 2010

The Employment Commission tests benefit payment samples throughout the year but Labor does not calculate the official rates until the end of the calendar year. Using the calendar year 2009 BAM error rate, we calculated estimated overpayments and overpayments established for fiscal year 2010. We considered only the Unemployment Insurance Program and did not estimate overpayments for federal extended benefits; benefits paid for federal extended benefits totaled approximately $925 million in fiscal year 2010.

Estimated Overpayment Information for Fiscal Year 2010

	UI Program
Unemployment Benefits Paid	$953,969,661
Estimated Overpayment (including work search requirement)	$139,279,571
Estimated Overpayments (excluding work search requirement)	$46,744,513
Overpayments Established	$29,177,925
Percentage of Overpayments Established to Estimated Overpayments (including work search requirement)	21%
Percentage of Overpayments Established to Estimated Overpayments (excluding work search requirement)	62%

**Estimated based on Benefit Accuracy Measurement Overpayment error rates calculated for calendar year 2009. These error rates are documented in the section entitled* "Analysis of Overpayment Information in BAM Reports."

Operational Matters

Financial

Historically, the Employment Commission has received 100 percent of its administrative funding from an administrative allowance, which federal law allows, grants for employment services, and a portion of interest and penalties. The level of funding is also a function of the unemployment rate in the Commonwealth. As the rate of unemployment increases so does the level of funding and the reverse is also true. During the years prior to 2009, the Commonwealth experienced very low levels of unemployment and the Employment Commission underwent a series of staff reductions and office closings to address these reductions.

Although the unemployment rate has risen, the increase in funding lags the unemployment increases. The current recession found the Employment Commission implementing a staffing reduction, therefore forcing management to set funding priorities as to which function received funding. Management placed emphasis of making timely payment of benefits its priority; however, they did increase their detection efforts as noted earlier in the report.

Implementing any recommendations in this report that require resources will require management to reallocate resources and re-set priorities. We believe these choices may have policy considerations that both the Governor and the General Assembly may wish to review before the Employment Commission implements a change.

The last major financial consideration facing the Employment Commission is the repayment of the loan from the federal government for unemployment benefits. While an increase in employer taxes will repay most of the loan principal, payment of interest will need to come from interest and penalties that the Employment Commission collects and is a source of discretionary funding for administrative cost that may not be available.

Technology

The Employment Commission's primary systems are over 25 years old and limit management's abilities to obtain timely information and react to changes in the environment. The systems also limit how the Employment Commission interacts with both employers and claimants.

The Employment Commission does have two system development initiatives that will replace its older systems. These two projects are the Financial Management Systems Project and the Unemployment Insurance Modernization Project (UI Mod).

The Financial Management Systems Project is a modern, integrated financial management system to replace their outdated mainframe batch system. The total cost of the project is $4.7 million, including $1.5 million coming from the Employment Commission's penalty and interest fund. The UI Mod project will replace VATS, VABS, and the Wage Record System. UI Mod will support payment of benefits to unemployed workers, collection of taxes from employers, and the accumulation of wage data. The total budget for UI Mod is $58.5 million with $49.1 million coming from the Reed Act funds and the remaining $9.4 million coming from the Employment Commission's penalty and interest fund.

Virginia Information Technologies Agency has approved the initial planning phase of the Financial Management Systems Project and the development phase of the UI Mod project; however with making repaying the federal loan a priority, the Employment Commission is not sure if the penalty and interest funding will be available for these projects, therefore jeopardizing the successful implementation of both projects.

Business Cycle

As noted earlier, the Employment Commission's funding is a direct reflection of the unemployment rates, which reduce funding in times of low unemployment, but do not necessarily change in time to address increases in unemployment. Employment Commission management needs to maintain a fine balance between having adequate staff and modern systems to address this fluctuating situation.

Controlling overpayment rates requires both experienced staff and modern systems, however, as the unemployment rate changes the number of staff does not need to remain constant. No one can reasonably predict either the severity or duration of any business cycle, however, the Employment Commission should consider developing some contingency plans to allow it to react to increases in the unemployment rate and, more importantly, to set minimum staffing levels or rotational training plans to allow the Employment Commission to not lose its expertise.

Findings and Observations

Benefit Eligibility Process

- The Employment Commission has a number of controls in the eligibility determination process designed to prevent overpayments. These controls rely on information submitted by both claimants and employers. As a result, the timeliness and accuracy of this information impacts the effectiveness of these controls. Improving both timeliness and accuracy will require new systems within the Employment Commission and require the Employment Commission to enforce reporting requirements by both claimants and employers.

- Approximate two thirds of the overpayment errors in the Benefit Accuracy Measurement (BAM) reviews relate to the weekly work search requirements. The work search requirement is difficult to enforce and there are several different issues for consideration related to these errors.

  - The Employment Commission could implement procedures to verify weekly work search requirements. Currently, there are no procedures to verify or confirm this information unless the case is part of the BAM sample. Verification would require additional staff and this staff would need to contact employers to confirm the information or have claimants obtain information from the employers when they do the work search, which would put an additional requirement on employers.

  - Generally, the Employment Commission disqualifies any work search done by telephone. The current policy is a claimant must contact employers in person and they can send resumes or applications through the Internet or fax.

    Virginia is one of only four states that do not allow telephone contact as adequate work search. Of the 14.6 percent overpayment error rate in the BAM statistics, 4.5 percent of the rate relates to errors for claimants who claimed they did a work search using the telephone. This type of work search may be valid as businesses have adopted more sophisticated telecommunication systems for handling normal business transactions, including initial personnel contacts. The Employment Commission may want to review their adequate work search policy and consider whether any revision is necessary.

- Overall, the majority of established overpayments in fiscal year 2010 were due to two main causes – unreported wages by the claimant and incorrect reasons for separation. While the individual cases and situations may differ across the population of overpayments, these two main causes account for an estimated 75 - 80 percent of all overpayments.

  - The majority of overpayments occur when the claimant gets a new job and does not tell the Employment Commission and continues to receive benefit payments. The Employment Commission relies primarily on various detection tools to identify these overpayments.

- The second major reason for overpayments is where the claimant gives an incorrect reason for separation from their job. The Employment Commission has a control in place so that the employer can confirm the reason for separation. However, there are a number of things that can happen that affect the effectiveness of this control. Examples are that employers do not submit documentation timely or sometimes not at all until after the Commission makes a benefit payment. Improving the timeliness of employer responses could place additional costs on the employers.

- Employment Commission staff have to spend a significant amount of time resolving errors in wage information sent in from employers. They have to process a considerable amount of data so it will be available for the eligibility determination process in a timely manner. An average quarter may involve wage information from 188,000 employers. Although the Employment Commission sends out and provides on the internet specific instructions to employers on how to submit the information via various media types, many times employers do not follow the instructions and Employment Commission staff have to spend time resolving issues and errors with the data.

  Also, a high percentage of employers continue to submit information on paper forms that increase the risk of data entry errors. The Employment Commission has no punitive tools for employers who consistently send in incorrect information, and employers object to other measures, such as automating information, because of the cost to them. This situation may improve with the increased options for sending electronic information, however, the long term resolution is the replacement of the existing systems and abandonment of paper forms except for the smallest employers.

Overpayment Detection and Monitoring

- The Employment Commission could increase staffing in the Benefit Payment Control Unit if they wanted to increase the amount and timeliness of establishing overpayments. The Benefit Payment Control Unit, which has responsibility for the detection, establishment, and recovery of overpayments, does not currently have the staff to handle the increased caseload and there is a backlog of cases. Although the Employment Commission stops benefit payments when the Unit identifies a potential overpayment, the Commission cannot establish an overpayment or begin recovery actions until the case undergoes review and a determination. To increase the staffing of this Unit will require the Employment Commission to shift resources from other areas.

- The Benefit Payment Control Unit does not have current documented policies and procedures for their overpayment detection and recovery processes. This Unit has a critical function at the Employment Commission as they are responsible for the detection, establishment, and recovery of overpayments. As a result, during our review of overpayments, we relied primarily on verbal discussion with the Unit's staff to gain an understanding of their process and VABS functions. Further, the schedule for the current Unit director includes working on the Unemployment Insurance Modernization Project (UI Mod) over the next several years. The lack of documented policies and procedures could affect the ability of this Unit to effectively function in his absence.

- The Employment Commission may want to consider developing some new mechanisms to analyze and report overpayment information for internal management purposes. The Benefit Accuracy Measurement (BAM) program is the only method the Employment Commission uses to generate information on estimated overpayments. We believe there are some issues in the BAM data which limit its usefulness for analyzing benefit overpayments. First, Labor computes the overpayment error rates from annual samples that could overstate the rate because of how Labor evaluates the sample results that may cause statistical variations. In addition, Labor computes the estimated dollar value of overpayments for the entire population even though not all claimants in the population have the same requirements. Also, Labor does not consider extended federal benefit payments in the computation, only the state unemployment insurance payments.

Other Matters

- Overpayments caused by administrative errors account for approximately four percent of all overpayments. Most of these types of errors are in the wage information sent in from employers that the Employment Commission procedures do not detect.

- There is an increased emphasis on improper payments, like unemployment benefit overpayments, at the federal level. Recent efforts at the federal level focus on more analysis to aid in identifying the root causes of improper payments so they can address these causes, or determine if a cost effective solution may not exist.

  As the Employment Commission moves forward with system development projects to replace VABS, they need to consider the need to analyze overpayment data and how to best record this information in their new system. The current classification system in VABS to classify overpayments limits the ability of the user to analyze overpayment activity to determine root causes. While the federal government sets some classifications to allow standardization among states, we believe the Employment Commission has some flexibility with regard to overpayment classifications to better use this information.

Commonwealth of Virginia

Walter J. Kucharski, Auditor

Auditor of Public Accounts
P.O. Box 1295
Richmond, Virginia 23218

November 19, 2010

The Honorable Robert F. McDonnell
Governor of Virginia

The Honorable Charles J. Colgan
Chairman, Joint Legislative Audit
and Review Commission

We have performed a **Review of Overpayments at the Virginia Employment Commission** in conjunction with our fiscal year 2010 audit of the Employment Commission and are pleased to submit our report herein. We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

<u>Audit Objectives</u>

We received a legislative request to perform this work and we had the following objectives for this review:

- To fully understand the unemployment benefit claims process to include the Employment Commission's procedures for identifying and classifying overpayments, the process for recouping overpayments, and the BAM reporting process;
- Analyze overpayment activity for fiscal years 2008, 2009 and 2010 to identify trends and reasons for overpayments;
- Review the calendar year 2009 BAM report to try to identify why overpayment amounts reported here are significantly different than overpayments established by the Employment Commission;

- Analyze the accounts receivable activity related to overpayments; and

- Identify any weaknesses or areas for improvement and make recommendations to address these.

Audit Scope and Methodology

We gained an understanding of the unemployment benefit claims process and how overpayments can occur, how they are detected and how they are recovered. We obtained this understanding through interviews with Employment Commission staff, review of documentation, and analysis of data. We analyzed overpayment data, as well as individual cases, obtained from the Employment Commission's automated benefit payment processing system, the Virginia Automated Benefit System (VABS). We also analyzed accounts receivable data related to overpayments.

Conclusions

Overall, we found that the Employment Commission has a number of different processes in place to minimize overpayments, but these processes are reliant on information from both the claimants and employers. While there are opportunities to reduce benefit overpayments, these could result in significant cost increases for employers as well as the Employment Commission. We have summarized our observations and conclusions in the section entitled "Findings and Observations."

Exit Conference and Report Distribution

We discussed this report with Management on November 30, 2010. Management's response to the report is included in the section entitled "Agency Response." We did not audit management's response and accordingly, we express no opinion on it.

This report is intended for the information and use of the Governor and General Assembly, management, and the citizens of the Commonwealth of Virginia and is a public record.

AUDITOR OF PUBLIC ACCOUNTS

LCW/clj

COMMONWEALTH of VIRGINIA

Virginia Employment Commission

John R. Broadway
Commissioner

703 East Main Street

Post Office Box 1358
Richmond, Virginia 23218-1358

December 7, 2010

Mr. Walter J. Kucharski
Auditor of Public Accounts
Post Office Box 1295
Richmond, Virginia 23218

Dear Mr. Kucharski:

Thank you for the opportunity to review and respond to the Auditor of Public Accounts' report on the Review of Unemployment Benefit Overpayments.

We are always looking for opportunities to improve processes and welcome your analyses and observations. Your findings and observations are appreciated and are given the highest level of importance and consideration as we continue to review and improve our practices and procedures in addressing benefit overpayment issues.

Your report contains a significant amount of information. We will thoroughly analyze each area of your report in the detail necessary to formulate sound comprehensive directions and approaches to further reduce unemployment benefit overpayments where possible. Please be assured we will work diligently over the coming months to address areas of necessary improvements to ensure the best possible outcomes for our claimants, employers, and other stakeholders.

Again, we appreciate the opportunity to provide comments as part of your office's report on the Review of Unemployment Benefit Overpayments of the Virginia Employment Commission.

Sincerely,

John R. Broadway
Commissioner

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VIRGINIA EMPLOYMENT COMMISSION

John R. Broadway
Commissioner

Dr. Robert P. Leber
Deputy Commissioner