VIRGINIA EMPLOYMENT COMMISSION

RICHMOND, VIRGINIA

REPORT ON AUDIT

FOR THE YEAR ENDED

JUNE 30, 2002

APA
Auditor of
Public Accounts
COMMONWEALTH OF VIRGINIA

AUDIT SUMMARY

Our audit of the Virginia Employment Commission for the year ended June 30, 2002, found:

- proper recording and reporting of transactions, in all material respects, in the Commonwealth Accounting and Reporting System and in the Employment Commission's Tax and Benefits Systems;

- an internal control matter that we consider a reportable condition; however, we do not consider this to be a material weakness;

- an instance of noncompliance with federal requirements that is required to be reported; and

- adequate corrective action with respect to the audit findings reported in the prior year.

We recommend that the Employment Commission accurately complete financial status reports.

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SELECTED AGENCY INFORMATION

The Employment Commission's mission statement reads: "We provide workforce services that promote maximum employment to enhance the economic stability of Virginia." The Employment Commission accomplishes this goal through the Unemployment Insurance, Job Service, and Workforce Investment Act programs. The Employment Commission also compiles and provides labor market and economic information through the Economic Information Services Division.

The Unemployment Insurance program, established by the Social Security Act of 1935, makes benefit payments to laid-off workers, ensuring that they have minimal income during the course of a job search. The Employment Commission processes and pays benefit claims and resolves any disputed claims through the Commission Appeals division. The Employment Commission also collects employers' taxes used to fund the Trust Fund that pays all benefit claims.

The Wagner-Peyser Act of 1933 created the Job Service program, which aims to provide public employment services to individuals. Such services include referrals for unemployed persons, recruiting for employers looking for qualified employees, and job search skill training.

The Workforce Investment Act is a federal program aimed at reworking the job training process, adult education and literacy, and vocational rehabilitation at the state and local levels. The key elements are the state workforce investment board, local workforce investment boards and their youth councils, and local one-stop delivery systems.

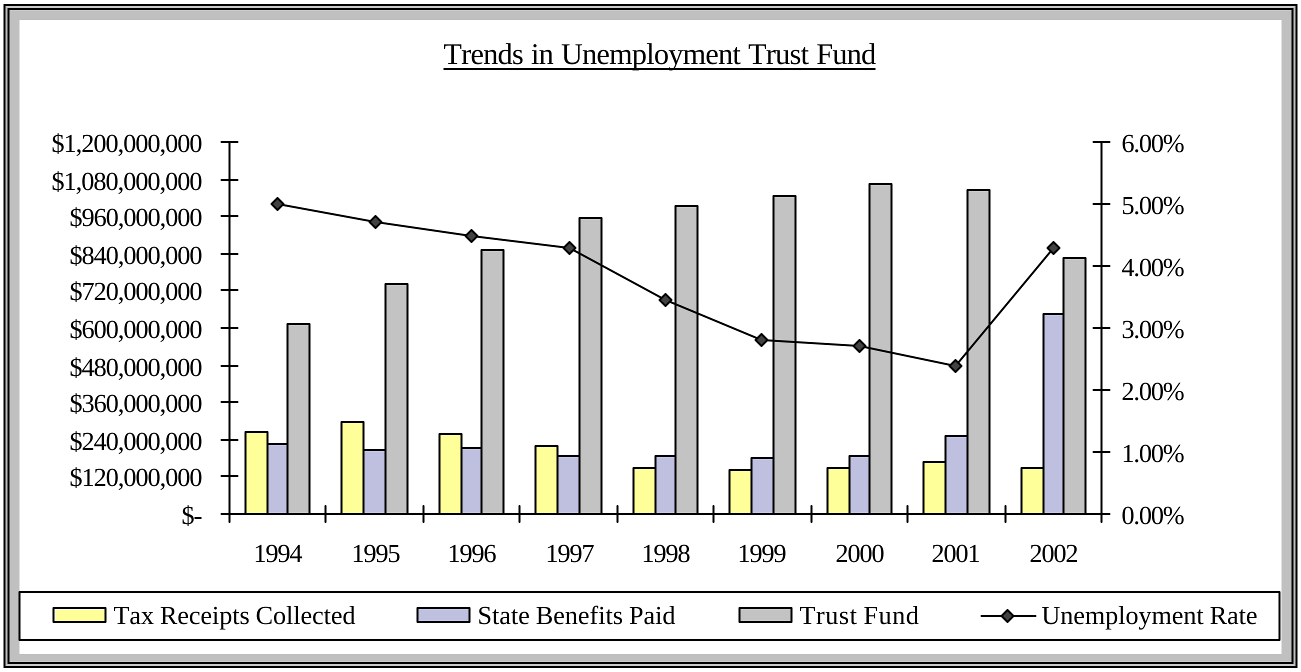
The Employment Commission also accumulates, collects, and reports labor market data through the Economic Information Services division. The data, reported in cooperation with the Bureau of Labor Statistics, provides various information including employment statistics, wages, and layoffs. Staff can compile information upon request or users can arrange access to some data by using the Automated Labor Information on the Commonwealth's Economy system.

UNEMPLOYMENT TRUST FUND

When the Employment Commission collects unemployment taxes from employers, it deposits the collections into the Unemployment Trust Fund for which the Employment Commission is the trustee. The Employment Commission then makes all benefit payments from the trust fund. State law requires that any individual receiving benefits must have earned a minimum amount of total wages in two of the first four of the last five calendar quarters, referred to as the base period. The minimum dollar amount is $2,500. As a result of the events of September 11, 2001, and the downturn in the economy in November 2001, the former Governor issued an Executive Order increasing all unemployment benefits by 37.3 percent. This increased the minimum benefit from $50 to $69 and the maximum benefit from $268 to $368. These higher benefit amounts will remain in effect through January 4, 2003. Legislation enacted in 2002 reduced the increase to 18.65 percent resulting in minimum and maximum benefits of $59 and $318, respectively. These benefit levels are effective from January 5, 2003 to January 3, 2004.

The Employment Commission levies taxes on employers' wages according to rates set by the General Assembly, which reflect the trust fund's solvency. The tax also includes an experience rating based on past claims against an employer's payroll. This rating requires employers with a history of higher claims to pay a greater rate and allows those with fewer claims to pay less. Under current law, employers only pay taxes on the first $8,000 of each employee's wages. For the calendar year 2002, the maximum rate that an employer can be required to pay on those taxable wages is 6.20 percent, while the minimum rate is zero percent. For the fifth consecutive year, benefits paid out have exceeded collections, therefore, reducing the balance in the trust fund to below $1 billion. Since the trust fund is less than 100 percent solvent, the employer tax rates will increase in calendar year 2003 and the minimum and maximum rates will be 0.20 percent and 6.30 percent, respectively. All employers will pay a pool tax of 0.10 percent (included in the minimum and maximum rates), which is used to recover benefits that cannot be charged[8] to a specific employer.

The illustration below presents historical trends, which show the changes in tax collections, benefits payments, the trust fund balance, and the unemployment rate over the past several years.



Year	Tax Collections	Benefits Paid	Collections Over/ (Under) Benefits	Trust Fund Balance*	Trust Fund Solvency**	Unemployment Rate****
1994	$263,715,851	$223,565,168	$ 40,150,683	$ 611,937,629	69.7%	5.0%
1995	295,673,218	208,808,361	86,864,857	743,233,179	79.3%	4.7%
1996	257,770,256	211,074,168	46,696,088	852,342,994	90.5%	4.5%
1997	217,171,263	188,615,553	28,555,710	955,948,173	123.0%	4.3%
1998	145,611,983	187,178,361	(41,566,378)	994,128,995	114.0%	3.4%
1999	143,501,663	181,424,022	(37,922,359)	1,024,275,741	107.0%	2.8%
2000	148,519,732	185,413,314	(36,893,582)	1,065,058,749	101.3%	2.5%
2001	164,694,068	248,503,150	(83,809,082)	1,046,104,532	100.3%	2.6%
2002	149,978,386	644,658,637	(494,680,251)	828,614,632***	82.7%	4.1%

* The trust fund balance also includes interest credited to the account.

** Trust fund solvency is an indicator of the fund's ability to pay benefits during periods of high unemployment as experienced over the past 20 years. The solvency indicator compares the fund's actual balance to the calculated balance needed to pay these benefits for 16.5 months. The formula used to calculate the balance uses historical benefit and wages data. Trust fund solvency does not directly relate to current year tax collections or benefits paid. Since June 1996, the computation of solvency uses a modified accrual basis as stipulated in §60.2-533 of the Code of Virginia.

*** Under the Federal Unemployment Tax Act (FUTA), employers pay the federal government a 0.8 percent tax on the first $7,000 of each employee's wages. This money is used for administration costs of employment security, for extended unemployment compensation, and to fund the federal unemployment account. Each of these three pools has a maximum amount that can be legally retained in the account. When these ceilings are reached, Congress can raise the ceilings or distribute the money to the States' Unemployment Trust Funds. In March 2002, the Employment Commission received a distribution of approximately $214,950,000. The balance in the trust fund includes this distribution. In addition, this balance also includes $33,361,753 of funds reserved for costs other than benefits.

**** This column represents the average unemployment rate for the entire fiscal year.

INTERNAL CONTROL FINDINGS AND RECOMMENDATIONS

Correctly Disburse Temporary Extended Unemployment Compensation

In March 2002, the United States Congress provided temporary extended unemployment compensation (TEUC) benefits to eligible recipients. This Act gave up to 13 additional weeks to individuals who had exhausted their regular Unemployment Insurance entitlement. The federal government fully funds this compensation, so it does not come out of Virginia's Unemployment Trust Fund. The maximum total benefit is equal to 50 percent of the recipients' regular Unemployment Insurance entitlement.

An auditor from the United States Department of Labor reviewed a sample of 50 cases to determine accuracy of payments to claimants and charges to the federal government. Out of that sample, the Employment Commission overpaid nine claimants. The Employment Commission discovered that a programming error caused overpayments to individuals having Unemployment Insurance claims before September 9, 2001, but whose benefit period extended past September 9, 2001. The computer program caused payment of the original TEUC benefit weekly amount plus the 37.3 percent supplement granted by the former Governor without considering the total benefit cap (equal to 50 percent of the recipients' regular Unemployment Insurance entitlement). For example, assume that an individual who filed a claim for benefits prior to September 9, 2001, was eligible to receive $100 a week in regular Unemployment Insurance for a period of 26 weeks and received payment for two of those weeks prior to September 9, 2001. As a result of the Governor's Executive Order, that individual would have received $137 per week for the 24 weeks remaining on his claim. This represents a maximum benefit amount for his state unemployment insurance of $3,488. Under the TEUC program, he was eligible to receive 50 percent of that amount, or $1,744; however, due to the programming error, he received 13 weeks of benefits at $137 per week (the original $100 weekly benefit amount plus the $37 supplement). This resulted in a total pay out of TEUC in the amount of $1,781, or $37 more than was allowable.

The Employment Commission identified 6,265 claims affected and total overpayments of $2,420,040, resulting in an average overpayment of $387 per claim. These overpayments are less than 0.4 percent of the total benefits paid by the Employment Commission during fiscal year 2002. Under TEUC law, the state government can waive overpayments arising from administrative error if the overpayment is not the result of fraud or misrepresentation by the individual and requiring repayment would cause undue hardship. Since the Employment Commission meets both of these requirements, it is possible that the federal government will absorb the overpayments without the Commonwealth incurring any financial liability.

Accurately Complete Financial Status Reports

Under the Workforce Investment Act, the Employment Commission must report financial, participant, and performance data in accordance with instructions issued by the United States Department of Labor (DOL). For activity related to program year 2001, the Employment Commission did not complete a June 30, 2002, quarterly Financial Status Report 9076-A "Workforce Investment Statewide Activities" in accordance with DOL guidelines. The Employment Commission inadvertently used the preliminary "Status of Obligational Authority" reports to compute total federal outlays on the report submitted to DOL instead of the final reports. This resulted in an overstatement of expenses of $977,357. The reporting process requires the preparation of each quarter's reports without reliance on a prior quarter's report. The report for quarter ending September 30, 2002, was prepared accurately.

The Employment Commission does perform a supervisory review of these quarterly reports; however, this overstatement was not detected. During this review, the supervisor should ensure that the individuals preparing the report always use the final financial system. Overstating expenses results in the Employment Commission reporting inaccurate information on Workforce Investment activity to DOL.

Commonwealth of Virginia

Walter J. Kucharski, Auditor

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

January 9, 2003

The Honorable Mark R. Warner
Governor of Virginia
State Capitol
Richmond, Virginia

The Honorable Kevin G. Miller
Chairman, Joint Legislative Audit
and Review Commission
General Assembly Building
Richmond, Virginia

INDEPENDENT AUDITOR'S REPORT

We have audited the financial records and operations of the **Virginia Employment Commission** for the year ended June 30, 2002. We conducted our audit in accordance with Government Audit Standards, issued by the Comptroller General of the United States.

Audit Objectives, Scope, and Methodology

Our audit's primary objectives were to evaluate the accuracy of recording financial transactions on the Commonwealth Accounting and Reporting System and in the Employment Commission's Tax and Benefits Systems, review the adequacy of the Employment Commission's internal control, and test compliance with applicable laws and regulations. We also reviewed the Employment Commission's corrective actions of audit findings from prior year reports.

Our audit procedures included inquiries of appropriate personnel, inspection of documents and records, and observation of the Employment Commission's operations. We also tested transactions and performed such other auditing procedures as we considered necessary to achieve our objectives. We reviewed the overall internal accounting controls, including controls for administering compliance with applicable laws and regulations. Our review encompassed controls over the following significant cycles, classes of transactions, and account balances:

Unemployment Benefit Payments
Taxes and Cash Receipts
Accounts Receivable
Accounts Payable
Federal Grants Management
Expenditures
Payroll and Compensated Absences

We obtained an understanding of the relevant internal control components sufficient to plan the audit. We considered materiality and control risk in determining the nature and extent of our audit procedures. We performed audit tests to determine whether the Employment Commission's controls were adequate, had been placed in operation, and were being followed. Our audit also included tests of compliance with provisions of applicable laws and regulations.

The Employment Commission's management has responsibility for establishing and maintaining internal control and complying with applicable laws and regulations. Internal control is a process designed to provide reasonable, but not absolute, assurance regarding the reliability of financial reporting, effectiveness and efficiency of operations, and compliance with applicable laws and regulations.

Our audit was more limited than would be necessary to provide assurance on internal control or to provide an opinion on overall compliance with laws and regulations. Because of inherent limitations in internal control, errors, irregularities, or noncompliance may nevertheless occur and not be detected. Also, projecting the evaluation of internal control to future periods is subject to the risk that the controls may become inadequate because of changes in conditions or that the effectiveness of the design and operation of controls may deteriorate.

Audit Conclusions

We found that the Employment Commission properly stated, in all material respects, the amounts recorded and reported in the Commonwealth Accounting and Reporting System and in the Employment Commission's Tax and Benefit Systems. The Employment Commission records its financial transactions on the cash basis of accounting, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America. The financial information presented in this report came directly from the Commonwealth Accounting and Reporting System, as well as the Employment Commission's Tax and Benefits Systems.

We noted a certain matter involving internal control and its operation that we consider to be a reportable condition. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of internal control that, in our judgment, could adversely affect the Employment Commission's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial records. The reportable condition is described in the subsection titled "Reporting." We believe that the reportable condition is not a material weakness.

The results of our tests of compliance with applicable laws and regulations disclosed an instance of noncompliance that is required to be reported under Government Auditing Standards. The instance of noncompliance is described in the subsection titled "Reporting."

The Department has taken adequate corrective action with respect to audit findings reported in the prior year.

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.

EXIT CONFERENCE

We discussed this report with management at an exit conference held on January 27, 2003.

AUDITOR OF PUBLIC ACCOUNTS

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