VIRGINIA EMPLOYMENT COMMISSION

RICHMOND, VIRGINIA

REPORT ON AUDIT

FOR THE YEAR ENDED

JUNE 30, 2000

APA
Auditor of Public Accounts
COMMONWEALTH OF VIRGINIA

AUDIT SUMMARY

Our audit of the Virginia Employment Commission for the year ended June 30, 2000, found:

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

- internal control matters that we consider reportable conditions, but not material weaknesses; and

- no material instances of noncompliance with applicable laws and regulations tested that are required to be reported.

We recommend that the Commission:

- eliminate inappropriate access to automated systems' production data files;

- update the Business Impact Analysis and Risk Assessment; and

- reevaluate physical security procedures at field offices.

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

Commonwealth of Virginia

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

Walter J. Kucharski, Auditor

January 30, 2001

The Honorable James S. Gilmore, III
Governor of Virginia
State Capitol
Richmond, Virginia

The Honorable Vincent F. Callahan, Jr.
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, 2000. We conducted our audit in accordance with Government Auditing Standards, issued by the Comptroller General of the United States.

Audit Objective, 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 Commission's Tax and Benefits Systems, review the adequacy of the Commission's internal control, and test compliance with applicable laws and regulations.

Our audit procedures included inquiries of appropriate personnel, inspection of documents and records, and observation of the Department'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 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 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 Commission properly stated, in all material respects, the amounts recorded and reported in the Commonwealth Accounting and Reporting System and in the Commission's Tax and Benefit Systems. The Commission records its financial transactions on the cash basis of accounting, which is a comprehensive basis of accounting other than generally accepted accounting principles. The financial information presented in this report came directly from the Commonwealth Accounting and Reporting System as well as the Commission's Tax and Benefits Systems.

We noted certain matters involving internal control and its operation that we consider to be reportable conditions. 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 Commission's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial records. Reportable conditions, entitled "Eliminate Inappropriate Access to Automated Systems' Production Data Files," "Update Business Impact Analysis and Risk Assessment," and "Reevaluate Physical Security Controls at Field Offices" are described in the subsection titled "Internal Control Findings and Recommendations." We believe that none of the reportable conditions is a material weakness.

The results of our tests of compliance with applicable laws and regulations disclosed no instances of noncompliance that are required to be reported under Government Auditing Standards.

This report is intended for the information 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 30, 2001.

AUDITOR OF PUBLIC ACCOUNTS

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INTERNAL CONTROL FINDINGS AND RECOMMENDATIONS

Eliminate Inappropriate Access to Automated Systems' Production Data Files

Personnel assigned to the Computer Operations section have inappropriate write access to all production data files for the Tax, Benefits, and federal automated systems. Production data files process information regarding such critical areas as employer taxes, the employee wages master file, daily transaction file, and unemployment compensation payments. Individuals with write access to files can change or delete critical information. Computer Operations do not need write access to production files to perform their job duties.

The Commission should eliminate write access to production data files for those employees whose job responsibilities do not require such access. This would lessen the risk of unauthorized changes that could render the data unreliable.

Update Business Impact Analysis and Risk Assessment

The Business Impact Analysis and Risk Assessment Plan identifies all data processing systems as well as any risks or threats to these systems. The Commission's plan, completed in November 1997, does not address such risks as natural disasters or improper disposal of documents (paper, diskettes, etc.) The Commission replaced its network during 1998 but has not yet updated their business impact analysis and risk assessment. COV ITRM Standard SEC2000-01.1 requires business impact analyses and, if necessary, updates to risk assessments, when an agency undergoes changes in information technology systems or their environments.

The Commission is updating the Business Impact Analysis and Risk Assessment. The Commission should finish updating the plan as soon as possible to ensure adequate security of critical and sensitive data, and compliance with Department of Technology Planning standards.

Reevaluate Physical Security Measures at Field Offices

We visited five field offices to review the Commission's overall level of physical security. In three of the five offices visited, we found that essential computer equipment like routers were stored in rooms with unrestricted access. Unlimited access to computer equipment poses a potential threat of misuse, damage, or theft. Field offices should store essential computer equipment in areas with access restricted to only personnel whose duties require them to maintain the equipment.

We also found that for several field offices, all employees had keys to the building allowing undetected access during all hours. The issuance of keys gaining entrance to field offices should be limited to the manager and only to other individuals for specified purposes such as back-up access or operations outside of normal business hours. Limiting keys to buildings helps reduce the risk of loss of equipment by theft or other unauthorized actions.

Finally, we found that most offices visited did not have enhanced security measures such as security cameras or emergency alarm systems connected to local police.

The Commission should reevaluate their physical security needs at all field offices to ensure the security of critical equipment as well as the safety of employees.

SELECTED AGENCY INFORMATION

The Virginia Employment Commission's mission statement reads: "We provide workforce services that promote maximum employment to enhance the economic stability of Virginia." The Commission accomplishes this goal through the Unemployment Insurance and Job Service programs. The 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 Commission processes and pays benefit claims, and resolves any disputed claims through the Commission Appeals division. The 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 Commission 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.

WORKFORCE INVESTMENT ACT OF 1998

The Workforce Investment Act (WIA), passed on August 7, 1998, makes major changes in the delivery of employment and training programs 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 General Assembly established the Virginia Workforce Council to assist the governor in meeting workforce-training needs in the Commonwealth. In addition, the Council serves as the State Workforce Investment Board and oversees workforce-training issues for the Virginia Community College System. The Virginia Workforce Council created the Virginia Workforce Strategy to direct the workforce development efforts of state agencies and to guide legislative and budgetary policy decisions.

Under the provisions of the Workforce Investment Act, the Virginia Workforce Council has divided the state into seventeen local service delivery areas. Each area has a board, appointed by local elected officials, that will include representatives of business, education, labor organizations, community organizations, economic development agencies, and each of the one-stop partners. One-stop partners include the Department of Rehabilitative Services, the Department for the Visually Handicapped, the Virginia Employment Commission, area agencies on aging, and redevelopment and housing authorities. In most areas one chief local-elected official will serve as the fiscal agent for all Workforce Investment Act funding. As such, they will receive funds from the Commission and be responsible for the legal use of those funds in accordance with the Workforce Investment Act. The local boards, in partnership with local-elected officials in each area, will be responsible for:

- Developing a five-year plan for the local workforce investment program;

- Designating eligible providers of services;

- Negotiating performance measures for local employment and training activities;
- Overseeing the local one-stop delivery system and programs; and
- Assisting in the development of a statewide employment statistics system.

Under the Workforce Investment Act, there are three established levels of services for adults and dislocated workers:

- Core services – the initial effort to place workers in jobs
- Intensive services – provided to unemployed workers who cannot obtain employment through core services and employed workers who need additional assistance to remain employed
- Training services – only available to individuals who are unable to obtain or retain employment through intensive services.

Core services are need-driven whereas training services are eligibility driven. In some cases intensive services are need-driven. In other cases, they are eligibility driven.

The Workforce Investment Act will also provide enhanced services for youth. Subgroups of local boards will plan youth activities. These subgroups will not have voting authority in board meetings. Members of the subgroups will have experience working with youth. Youth services under the Workforce Investment Act provide for ten program elements, including tutoring, internships, and summer employment opportunities. For this year, many local boards elected to have summer program activity. Under the current plan, states received pre-awards in April 2000 of 25 percent of the youth program funds, if they elected to participate in a summer youth program.

The Workforce Investment Act also mandates that states establish one-stop delivery systems in each local service delivery area, which will directly deliver core employment services such as job search assistance and career counseling. The local centers will also provide customers access to more intensive services such as case management, short-term prevocational services, and training. The Workforce Investment Act allows in addition to the one delivery center, a network of affiliated centers.

The Workforce Investment Act program implementation date was initially July 1, 2000. However, because states did not have adequate time to meet all of the requirements, full implementation will occur by June 30, 2001.

The Governor designated the Commission as the lead agency in implementing the WIA within Virginia. The Commission will oversee the development of the one-stop centers and coordinate the delivery of various agencies' services to customers. Other agencies that may be involved with WIA programs include the Departments of Rehabilitative Services, Social Services, and Education.

The Commonwealth of Virginia has substantially implemented the Workforce Investment Act. Most of the seventeen local areas have approved strategic plans, or are awaiting Commission approval. In addition, the Commission has approved performance measures and one-stop operators for most of the local areas. The Commission expects to have full program implementation before the June 30, 2001, deadline.

Unemployment Trust Fund

When the Commission collects unemployment taxes from employers, it deposits the collections into the Unemployment Trust Fund, for which the Commission is the trustee. The 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. State law also dictates the minimum and maximum weekly benefit amounts that an individual can receive.

The 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. The maximum rate that an employer can be required to pay on those taxable wages is currently 5.58 percent, while the minimum rate is 0 percent.

Unemployment Compensation Law Changes

In 1997, the General Assembly increased the maximum weekly benefit payment and decreased the minimum weekly rate. The law also decreased the minimum qualifying earnings. A summary of the changes follows.

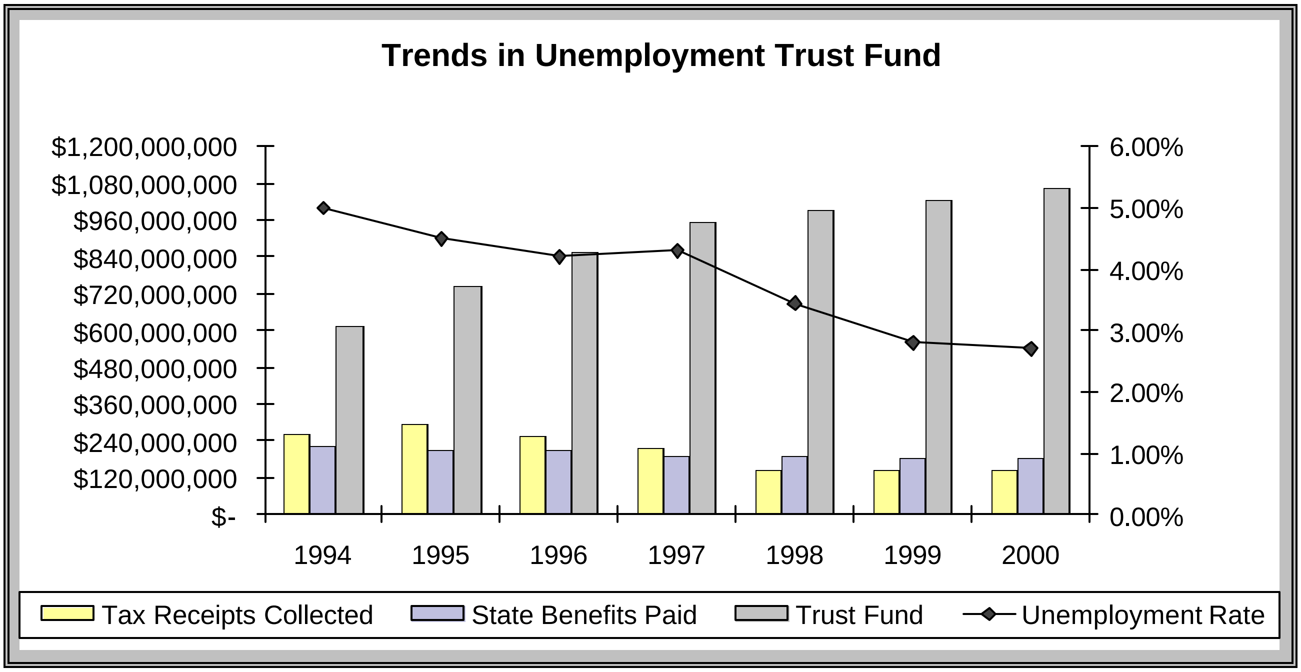
	Weekly Benefit		Minimum
Year	Maximum	Minimum	Qualifying Earnings
1997	$ 226	$ 60	$ 3,000
1998	228	55	2,750
1999	230	50	2,500
2000	268	50	2,500

In 2000, for example, an eligible individual who earned at least $2,500 in the base period would receive a weekly benefit ranging from a minimum of $50 to a maximum of $268.

In response to falling unemployment and an increasing balance in the Unemployment Trust Fund, the General Assembly revised the formula used to determine the trust fund balance factor in 1997. This resulted in lower employer tax rates for two years. However, as the Trust Fund solvency has decreased, the maximum employer tax rate has increased. The table below shows the change in the tax rates.

	Maximum Tax
Prior to July 1, 1997	6.20% or $496 per employee
From July 1, 1997- December 31, 1999	5.40% or $432 per employee
As of January 1, 2000	5.58% or $447 per employee

The balance in the trust fund continues to rise, and for the third consecutive year, benefits paid out exceed collections. The interest that the fund earns offsets the deficit in tax revenue and causes the fund's balance to grow. The illustration below presents historical trends, which show the changes in tax collections, benefits payments, 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%	2.7%

* 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 twenty 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.

At June 30, 2000, the Trust Fund was 101.3 percent solvent, which represents a decline from 107 percent in the previous year. The percentage decline is a direct result of the continuing decrease in employer tax rates.