

VIRGINIA EMPLOYMENT COMMISSION

**REPORT ON AUDIT
FOR THE YEAR ENDED
JUNE 30, 2007**

APA

**Auditor of
Public Accounts**

COMMONWEALTH OF VIRGINIA

AUDIT SUMMARY

Our audit of the Virginia Employment Commission for the year ended June 30, 2007, found the following:

- 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;
- internal control matters that require management's attention and corrective action; and
- noncompliance with applicable laws and regulations or other matters that is required to be reported.

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AUDIT FINDINGS AND RECOMMENDATIONS

During the course of the audit, we became aware of several areas in which work was not being completed timely primarily due to either inexperienced staff or staffing shortages. One department has at least six employees with less than one year experience with the Employment Commission. As this agency faces challenges of layoffs, as well as the retirement of an aging workforce, management will need to focus on the effective utilization of available resources to ensure adequate internal controls and compliance with applicable laws and regulations.

Properly Complete Employment Eligibility Verification Forms

The Employment Commission was not properly completing Employment Eligibility Verification forms (I-9) in accordance with guidance issued by the U.S. Citizenship and Immigration Services of the U.S. Department of Homeland Security. The guidance requires the employee to complete, sign, and date Section 1 of the I-9 form on or before the first day of employment. Additionally, the employer or designated representative must complete, sign, and date Section 2 of the I-9 form within three business days of employment.

In our sample of twenty I-9 forms for employees hired during fiscal year 2007, we noted the following noncompliance.

- One form did not have the information regarding the verification documents (document title, issuing authority, document number, and expiration date) completed properly.
- Three forms did not have the employee date on or before the first day of employment.
- Five forms had improperly completed Section 2.
- Five forms did not show the employer verification as completed within 3 business days of the employee's first day of employment.
- The Employment Commission could not provide two employee I-9 forms.

The federal government has increased its enforcement efforts requiring employers to ensure that all new employees are legally entitled to work in the United States. Based upon the number of errors found during audit testwork, we considered this finding to be a significant internal control weakness and non-compliant with federal regulations.

We recommend that the Human Resources Division review the I-9 process, train human resources staff on the requirements of completing I-9 forms, and develop procedures to continuously review the I-9 forms for compliance with federal regulations.

Improve Tax Performance

The U.S. Department of Labor requires the Employment Commission to conduct internal reviews of operations and develop recommendations for improvement. One review, the Tax Performance System Annual Report (TPS Report) identifies findings and recommendations resulting from the Employment Commission's Quality Assurance Department's review of the tax operations within the agency. In the TPS Report for 2006, the Employment Commission failed in five out of the thirteen tax measures identified. Of these five measures, three have not passed for three years consecutively.

The U.S. Department of Labor's primary goal of the TPS Report is to assist state administrators in the improvement of the Unemployment Insurance (UI) program by providing objective information on the quality of existing revenue operations. By consistently not passing these measures, the Employment Commission will have to continually provide corrective action plans to the Department of Labor. In addition, if four or

more tax measures fail in a year or any single function fails three consecutive years, the Employment Commission is also required to submit a corrective action plan for the U.S. Department of Labor's State Quality Service Plan report. This need for improvement relates to a lack of recorded instructions, lack of supervisory review of staff work, and the need for system modernization, among other reasons.

We recommend that the Employment Commission continue to evaluate and pursue opportunities available to increase the quality in all areas of the UI program which, in turn, will improve performance. Some opportunities for improvement include re-evaluating and improving written procedures, ensuring supervisory review of all work performed, and providing adequate training for all levels of staff performing the work. Management should keep staff aware of TPS reviews and recommendations and how their work impacts these reviews. Management should also ensure that all recommendations included in the TPS report are realistic and executable, and that all corrective action plans submitted to the U.S. Department of Labor are compatible.

FOLLOW-UP ON PRIOR AUDIT FINDINGS

Develop Information Security Program

The Employment Commission has made significant progress in developing a comprehensive information security program and addressing many of the information security program findings from last year's audit. We encourage the Employment Commission to continue developing continuity of operations plans.

The completion of these continuity of operation plans is critical in order to restore services to the Citizens of the Commonwealth in the event of a disaster or catastrophe. In addition, the Employment Commission should perform a test of its information technology continuity plans at least annually to assess their adequacy and effectiveness.

As identified in our report last year, untimely deletions of access to both CARS and CIPPS continue to be an area of concern. However, the Employment Commission has established more enhanced communication policies in this area, as well as recently implemented recognition of the removal of such access in the Employment Commission's Employee Separation Checklist.

Assurance of Infrastructure Security

The Employment Commission has addressed our infrastructure finding from last year's audit by taking the appropriate steps to establishing a Memorandum of Understanding and responsibility matrix with the Virginia Information Technologies Agency (VITA).

The Commissioner has responsibility for the security and safeguarding of all of the Employment Commission's sensitive and mission critical electronic information. Over the past four years, the Commonwealth has moved the information technology infrastructure supporting the databases that contain sensitive and mission critical electronic information to VITA, who has an Information Technology Partnership (IT Partnership) with Northrop Grumman. In this environment, VITA and the Commissioner clearly share responsibility for the security of the Employment Commission's information technology assets, systems, and electronic information and must provide mutual assurance of this safeguarding.

While the Employment Commission has addressed the issues in last year's infrastructure finding, the Commissioner and VITA remain responsible for the security and safeguarding of all sensitive and mission critical electronic information. As such, the Employment Commission should receive regular status reports

from VITA on the progress of any identified infrastructure issues. As part of the progress reporting, VITA should provide the Employment Commission with any interim steps they should take if the IT Partnership must delay addressing any issues.

Follow Established Procedures for Field Office Payment Logs

In following up on this prior year audit finding, overall compliance improvement appears to have occurred. We did identify one area of non-compliance with the Field Operations Manual (i.e. manual) in one Field Office where the Local Office Manager's signed date did not match the Field Office Payment Log's date. The Employment Commission has effectively addressed this issue by clarifying this compliance requirement in a documented policy and by performing payment log audits.

Continue Efforts to Improve Entered Participant Data

The Employment Commission performs annual reviews of the Local Areas' compliance with the Workforce Investment Act, Virginia Workforce Council policies, and Local Workforce Investment Board policies. Since 2004, issues regarding Local Areas not fully complying with the Employment Commission's internal guidance to enter participant data into the Virginia Workforce Network Information System (VWNIS) have been occurring. During fiscal year 2007, two out of four Local Area's reviewed contained repeat findings relating to data entry.

We had only four of the sixteen Local Area reports in final form and available to review. The Employment Commission did not have the other reports available due to staffing shortages and the reassignment of staff to perform other functions. The Employment Commission had monitored the remaining Areas but had not finalized the reports at the time of audit review. Untimely, inaccurate, or inconsistent submissions can adversely affect the Local Areas' reported performance to the state and, when summarized by the state, to the U.S. Department of Labor.

Despite the replacement of VWNIS with the Virginia Workforce Connection system, the Employment Commission anticipates continued noncompliance with internal requirements, which will increase the risk of misstating their reports until all Local Areas are utilizing the system fully and accurately. Additionally, the lack of staff resources will inhibit the Employment Commission from finalizing reports and identifying compliance issues timely.

The Employment Commission, under the direction of the Office of the Senior Advisor to the Governor for the Workforce, should continue to conduct compliance testing, require corrective action plans from the Local Areas, and monitor the effectiveness of the Virginia Workforce Connection system. Continued focus in these areas will assist in improving the reporting of accurate performance statistics to the U.S. Department of Labor in accordance with the Workforce Investment Act.

SELECTED AGENCY INFORMATION

The Employment Commission's mission is to promote economic growth and stability by delivering and coordinating workforce services to include policy development, job placement services, temporary income support, workforce information, and transition and training services. 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 makes benefit payments to workers who are unemployed through no fault of their own, ensuring they have minimal income during the course of a job search. The Employment Commission collects unemployment taxes from employers and uses these taxes to pay benefit claims. The tax collections go into the Unemployment Trust Fund for which the Employment Commission is the trustee. The Employment Commission pays all unemployment insurance benefit payments from the Trust Fund.

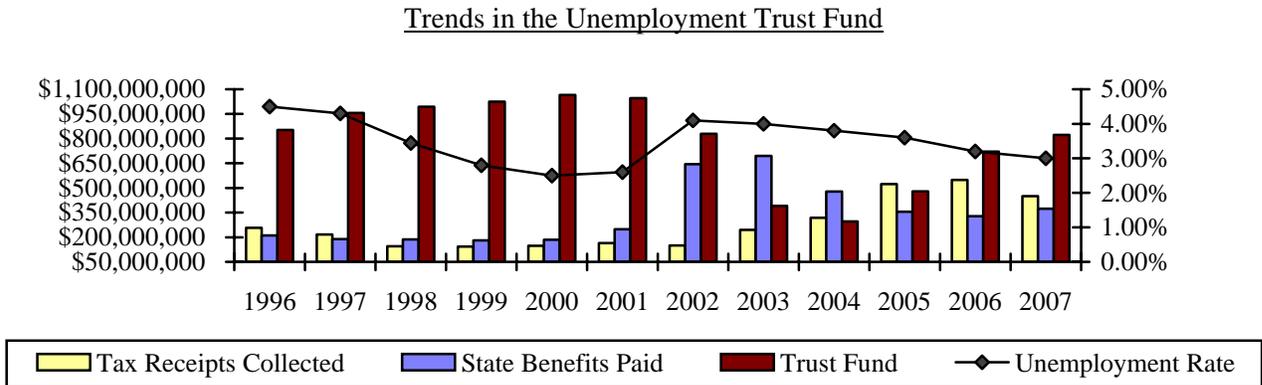
UNEMPLOYMENT TRUST FUND

The Unemployment Trust Fund’s solvency factor applicable for calendar year 2008 decreased to 70.4 percent versus 71.9 percent in calendar year 2007. The solvency factors for calendar years 2004 and 2005 were the only times the factor fell below 50 percent since 1984. Consistent with fiscal year 2006, taxes collected continued to exceed benefits paid, resulting in the Trust Fund balance increasing from \$721 million in the previous year to \$822 million at the end of fiscal year 2007.

As a result of the economic downturn in 2001, the Governor issued, on November 14, 2001, an Executive Order increasing all unemployment benefits by 37.3 percent for a six-month period starting September 9, 2001. In 2002, the General Assembly extended these benefit amounts through January 4, 2003, and, as the economy worked towards recovery, reduced the increased benefit levels over the next year and a half. Since 2004, the General Assembly has passed legislation increasing the minimum and maximum benefit levels. The following chart summarizes these changes in the benefit amounts.

	<u>Minimum Weekly Benefit</u>	<u>Maximum Weekly Benefit</u>
September 9, 2001 - January 4, 2003	\$69	\$368
January 5, 2003 - July 5, 2003	59	318
July 6, 2003 - July 3, 2004	50	316
July 4, 2004 - July 2, 2005	50	326
July 3, 2005 - July 2, 2006	54	330
July 3, 2006 – June 30, 2007	54	347
July 1, 2007 – Present	54	363

The following illustration presents historical trends, which show the changes in tax collections, benefit payments, the Trust Fund balance, and the unemployment rate over the past several years.



Note: The Trust Fund balance also includes interest credited to the account. The unemployment rate represents the average rate for the entire fiscal year.

The Trust Fund's solvency level has an inverse relationship to the amount of employer tax rates. As the Fund's solvency decreases, the tax rates increase. The Employment Commission levies taxes on employees' wages reported by employers according to rates set by the General Assembly. Under current law, employers only pay taxes on the first \$8,000 of each employee's wages. The tax rates imposed on employers consider the Trust Fund's solvency and the employment histories of individual businesses, referred to as the experience rating. This rating requires employers with a history of higher unemployment claims to pay a greater rate and allows those with fewer claims to pay less or nothing at all.

The Unemployment Compensation Act sets the lowest tax rate at zero as long as the Trust Fund solvency remains at or above 100 percent. Since fiscal year end 2002, the Trust Fund solvency has remained below 100 percent; therefore, all employers paid unemployment taxes during calendar years 2003 through 2007. For calendar year 2008, the minimum rate that an employer could be required to pay on taxable wages was 0.12 percent, while the maximum rate was 6.22 percent.

An additional adjustment to the tax rate for calendar years 2003 through 2007 was the inclusion of the pool tax. The pool tax represents a levy to recover benefits not chargeable to a specific employer, known as pool costs. Interest income earned from the Trust Fund can offset the total pool costs when the solvency is above 50 percent. Interest income did not exceed pool costs in fiscal year 2002; therefore, the Employment Commission added a pool tax rate of 0.03 percent to the employer tax rates for calendar year 2003. Because the Trust Fund solvency fell below 50 percent in calendar year 2004, the Employment Commission could not offset the total pool costs and employers paid the full tax rate. The pool tax rate increased to 0.14 percent and 0.22 percent for calendar years 2004 and 2005, respectively. This rate decreased in calendar year 2006 to 0.19 percent, fell to 0.07 percent for calendar year 2007, and will continue to decrease further to 0.02 percent for calendar year 2008.

State law requires a fund-building tax rate of 0.2 percent to the employer tax rates if the fund balance drops below 50 percent, which helps the Trust Fund to remain solvent. The Employment Commission calculated the Trust Fund solvency as 71.9 percent for calendar 2007 and 70.4 percent for 2008. Since the Trust Fund solvency is above 50 percent for calendar years 2007 and 2008, the fund-building tax rate does not need to be included in these respective calendar years.

The following table compares the various taxes for calendar years 2007 and 2008.

	<u>Calendar Year 2007</u>		<u>Calendar Year 2008</u>	
	<u>Tax Rates</u>		<u>Tax Rates</u>	
	<u>Minimum</u>	<u>Maximum</u>	<u>Minimum</u>	<u>Maximum</u>
Tax rate	0.10%	6.20%	0.10%	6.20%
Pool tax	0.07%	0.07%	0.02%	0.02%
Fund-building tax	<u>0.00%</u>	<u>0.00%</u>	<u>0.00%</u>	<u>0.00%</u>
Total	<u>0.17%</u>	<u>6.27%</u>	<u>0.12%</u>	<u>6.22%</u>

The following table lists the projected fund balances and solvency rates for 2008 through 2010.

<u>Year</u>	<u>Projected Fund Balance</u>	<u>Solvency Rate</u>
2008	\$769.8 million	63.6%
2009	\$697.0 million	54.9%
2010	\$714.7 million	54.8%

The Employment Commission expects the fund balance and accompanying solvency rates will decline in the next three years. This decline could trigger a fund building tax rate in the near future if it falls below the 50 percent threshold.

Effective October 27, 2006, the Department of Labor issued a final rule to regarding the statutory confidentiality and disclosure requirements concerning unemployment compensation information. This rule establishes uniform minimum requirements for the payment of costs, safeguards and data-sharing agreements to ensure responsible use when the Employment Commission discloses unemployment compensation information. States have two years from the effective date to adopt conforming legislation. The Employment Commission’s review of this rule and their current procedures determined that no changes were necessary to comply.

WORKFORCE INVESTMENT ACT

The Workforce Investment Act of 1998 (WIA) authorizes funds to provide the employment and training services of various programs and organizations through a system of one-stop career centers. In Virginia, Virginia Workforce Centers provide the services.

Each Virginia Workforce Center provides services required by federal legislation plus services to meet the needs of the local community. Most Employment Commission locations are Virginia Workforce Centers, and there are centers operated by other partner organizations and contractors offering Employment Commission services. Virginia’s system of one-stop career centers is the Virginia Workforce Network. During fiscal year 2006, the Virginia Workforce Centers operated under the guidance of the Virginia Workforce Council and Workforce Investment Boards in seventeen Workforce Investment Areas. Effective July 1, 2006, the Employment Commission, as administrative agency for WIA, received, and on behalf of the Governor, approved a request from local elected officials to combine two local workforce investment areas into a single area.

The Virginia Workforce Council assists the Governor in meeting the workforce training needs of the Commonwealth. This Council serves as the State Workforce Investment Board for the federal Workforce Investment Act. The Council provides guidance on workforce training issues and operation of Virginia Workforce Centers.

The Workforce Investment Boards establish and operate the Virginia Workforce Centers. These Boards provide a forum to assure that workforce training and employment initiatives meet the economic development and business needs of each local area.

Workforce Investment Act Federal Expenses			
	<u>2005</u>	<u>2006</u>	<u>2007</u>
Adult Program	\$ 13,788,000	\$ 11,974,239	\$ 11,666,229
Youth Activities	13,979,784	11,973,139	12,387,822
Dislocated Workers	<u>19,129,872</u>	<u>13,681,019</u>	<u>13,551,689</u>
Total	<u>\$ 46,899,661</u>	<u>\$ 37,630,403</u>	<u>\$ 37,605,740</u>

Note: Programs for adults and dislocated workers seek to improve employment, retention, and earnings of WIA participants and increase their educational and occupational skill attainment. Youth activities seek to increase the attainment of basic skills, work readiness or occupational skills, and secondary diplomas or other credentials.

Effective July 1, 2006, the responsibility for the administration of the WIA programs moved from the Employment Commission to the Governor's Office of Workforce Development and Workforce Council Support (Office). Throughout fiscal year 2007, the transition of the WIA implementation activities occurred between the Employment Commission and the Workforce Development.

The Employment Commission continued to be the fiscal agent for this agency and provided compliance reporting to the Senior Advisor of the Office. This transition will continue throughout fiscal year 2008. Effective July 1, 2008, WIA will transfer to the Virginia Community College System (VCCS). This transfer will include WIA grant administration, fiscal agent responsibilities, and compliance functions and will occur through an Executive Order. The Employment Commission will provide consultation as needed to VCCS during the year that follows.

EMPLOYMENT COMMISSION ADMINISTRATIVE FUNDING

The Employment Commission's funding comes entirely from federal funds, mostly from the Unemployment Insurance, Job Services, and Workforce Investment Act. This funding makes the Employment Commission susceptible to increases and decreases in funding based on the economy. When the economy is poor and unemployment is high, both benefits administered and funding increase. As the economy improves and unemployment decreases, the funding for the Employment Commission also decreases. Thus the Employment Commission's funding reflects the cyclical movement of the economy, requiring the Employment Commission to either increase spending to support increased services or cut costs due to decreased services.

During fiscal year 2007, the Employment Commission requested and received permission from the General Assembly to use approximately \$38.4 million in Reed Act funds for the administration of the Job Service and UI programs. This additional appropriation consisted of \$3.7 million to supplement Wagner-Peyser Job Service programs, \$4.1 million to supplement the administration of the Unemployment Insurance program, and funds to upgrade obsolete information technology systems. Funding of \$28.6 million will be awarded again in fiscal year 2008 under the Reed Act to be used under the direction of the Employment Commission.

Due to continued reduced federal grant funding for fiscal year 2008, layoffs will occur in March 2008. As such, staffing will remain a concern for the Employment Commission.

Information Systems Development

The Employment Commission successfully implemented the Virginia Workforce Connection (which replaced the Virginia Workforce Network Information System) in November 2007. The Employment Commission continues to provide training and support usage. The Employment Commission is in the early planning stages to replace the Virginia Automated Benefits System and the Virginia Automated Tax System and is participating in the Commonwealth's Enterprise Application Initiative for a statewide financial management system.



Commonwealth of Virginia

Walter J. Kucharski, Auditor

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

January 17, 2008

The Honorable Timothy M. Kaine
Governor of Virginia
State Capitol
Richmond, Virginia

The Honorable Thomas K. Norment, 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, 2007. We conducted our audit in accordance with Government Auditing Standards issued by the Comptroller General of the United States.

Audit Objectives

Our audit's primary objective was to evaluate the accuracy of the Virginia Employment Commission's financial transactions as reported in the Comprehensive Annual Financial Report for the Commonwealth of Virginia for the year ended June 30, 2007 and test compliance for the Statewide Single Audit. In support of this objective, we evaluated the accuracy of recording financial transactions on the Commonwealth Accounting and Reporting System and in the Employment Commission's Tax and Benefits Systems, reviewed the adequacy of the Employment Commission's internal control, tested for compliance with applicable laws and regulations, and reviewed corrective actions of audit findings from the prior year reports.

Audit Scope and Methodology

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.

We gained an understanding of the overall internal controls, both automated and manual, sufficient to plan the audit. We considered materiality and control risk in determining the nature and extent of our audit procedures. Our review encompassed controls over the following significant cycles, classes of transactions, and account balances.

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

We performed audit tests we deemed necessary 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. Our audit procedures included inquiries of appropriate personnel, inspection of documents, records, and contracts, and observation of the Employment Commission's operations. We tested transactions and performed analytical procedures, including budgetary and trend analyses.

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 in the Commonwealth Accounting and Reporting System 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. They also report accruals and accrual based financial information to the Department of Accounts, for inclusion in the Commonwealth's Comprehensive Annual Financial Report. The financial information presented in this report came directly from the Commonwealth Accounting and Reporting System and the Employment Commission's Tax and Benefit Systems.

We noted certain matters involving internal control and its operation that require management's attention and corrective action. These matters are described in the sections entitled, "Audit Findings and Recommendations" and "Follow-up on Prior Audit Findings."

The Employment Commission has taken adequate corrective action for two of the four audit findings reported in the prior year. The Employment Commission has not taken adequate corrective action with respect to the prior findings regarding developing their information security program and improving entered participant data.

Exit Conference and Report Distribution

We discussed this letter with management on January 17, 2008. Management's response has been included at the end of this report.

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



AUDITOR OF PUBLIC ACCOUNTS



COMMONWEALTH of VIRGINIA

Virginia Employment Commission

Dolores A. Esser
Commissioner

703 East Main Street

Post Office Box 1358
Richmond, Virginia 23218-1358

January 16, 2008

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' audit report for the year ended June 30, 2007. Your comments and recommendations are appreciated and are given the highest level of importance and consideration as we continue to review and improve our practices and procedures.

In general, we concur with the findings and recommendations identified in your report and as mentioned in the report, we have already taken action to address some of the concerns. We will be developing a corrective action plan to address the audit findings and recommendations.

Again, we appreciate the opportunity to provide the Virginia Employment Commission's comments as part of your office's report of the financial records and operations of the Virginia Employment Commission for the year ended June 30, 2007.

Sincerely,

A handwritten signature in cursive script that reads "Dolores A. Esser".

Dolores A. Esser

VIRGINIA EMPLOYMENT COMMISSION

Dolores Esser
Commissioner

Nick Kessler
Deputy Commissioner

