



STATE OF NORTH CAROLINA

EMPLOYMENT SECURITY COMMISSION

STATEWIDE FEDERAL COMPLIANCE AUDIT PROCEDURES

FOR THE YEAR ENDED JUNE 30, 2011

OFFICE OF THE STATE AUDITOR

BETH A. WOOD, CPA

STATE AUDITOR

EMPLOYMENT SECURITY COMMISSION

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AUDITOR'S TRANSMITTAL

The Honorable Beverly Eaves Perdue, Governor
Members of the North Carolina General Assembly
Mr. J. Keith Crisco, Secretary, Department of Commerce
Mrs. Lynn R. Holmes, Assistant Secretary, Division of Employment Security

We have completed certain audit procedures at the Employment Security Commission, currently known as the Division of Employment Security within the Department of Commerce, related to the State of North Carolina reporting entity as presented in the *Single Audit Report* for the year ended June 30, 2011. Our audit was performed by authority of Article 5A of Chapter 147 of the *North Carolina General Statutes*.

In the *Single Audit Report*, the State Auditor presents the results of tests of internal control and compliance with laws, regulations, contracts, and grants applicable to the State's major federal programs. Our audit procedures were conducted in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*.

Our audit objective was to render an opinion on the State of North Carolina's, and not the Commission's, administration of major federal programs. However, the report included herein is in relation to our audit scope at the Commission and not to the State of North Carolina as a whole.

The audit findings referenced in the report are also evaluated to determine their impact on the State's internal control and the State's compliance with rules, regulations, contracts, and grants. If determined necessary in accordance with *Government Auditing Standards* or the OMB Circular A-133, these findings are reported in the State's *Single Audit Report*.

North Carolina General Statutes require the State Auditor to make audit reports available to the public. Copies of audit reports issued by the Office of the State Auditor may be obtained through one of the options listed in the back of this report.

A handwritten signature in cursive script that reads "Beth A. Wood".

Beth A. Wood, CPA
State Auditor



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**REPORT ON COMPLIANCE WITH REQUIREMENTS THAT COULD HAVE A
DIRECT AND MATERIAL EFFECT ON EACH MAJOR PROGRAM AND ON
INTERNAL CONTROL OVER COMPLIANCE
IN ACCORDANCE WITH OMB CIRCULAR A-133**

Mr. J. Keith Crisco, Secretary, Department of Commerce
Mrs. Lynn R. Holmes, Assistant Secretary, Division of Employment Security
and Management of the Department of Commerce and Division of Employment Security

Compliance

As part of our audit of the State of North Carolina's compliance with the types of requirements described in the *OMB Circular A-133 Compliance Supplement* that could have a direct and material effect on each of its major programs for the year ended June 30, 2011, we have performed audit procedures at the Employment Security Commission. Our report on the State of North Carolina's compliance with requirements that could have a direct and material effect on each major program and on internal control over compliance in accordance with OMB Circular A-133 is included in the State's *Single Audit Report*. Our federal compliance audit scope at the Employment Security Commission included the following:

- CFDA 17.225 - Unemployment Insurance
- Employment Service Cluster
 - CFDA 17.207 - Employment Service / Wagner-Peyser Funded Activities
 - CFDA 17.801 - Disabled Veterans' Outreach Program (DVOP)
 - CFDA 17.804 - Local Veterans' Employment Representative (LVER) Program
- Workforce Investment Act (WIA) Cluster
 - CFDA 17.258 - WIA Adult Program
 - CFDA 17.260 - WIA Dislocated Workers
 - CFDA 17.278 - WIA Dislocated Worker Formula Grants

The audit results described below are in relation to our audit scope at the Commission and not to the State of North Carolina as a whole.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the

**REPORT ON COMPLIANCE WITH REQUIREMENTS THAT COULD HAVE A
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United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination of the Commission's compliance with those requirements.

The results of our audit procedures at the Employment Security Commission disclosed instances of noncompliance that are required to be reported in accordance with OMB Circular A-133 and which are described in findings 1, 2, and 4 in the Audit Findings and Responses section of this report.

Internal Control Over Compliance

Management is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered internal control over compliance with the requirements that could have a direct and material effect on a major federal program to determine the auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of internal control over compliance.

A *deficiency in internal control over compliance* exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. A *material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. A *significant deficiency in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

**REPORT ON COMPLIANCE WITH REQUIREMENTS THAT COULD HAVE A
DIRECT AND MATERIAL EFFECT ON EACH MAJOR PROGRAM AND ON
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Our consideration of the internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be deficiencies, significant deficiencies, or material weaknesses, and therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined above. However, we consider the deficiencies described in findings 1, 3, and 4 in the Audit Findings and Responses section of this report to be significant deficiencies in internal control over compliance, as defined above.

Management's responses to the findings identified in our audit are included in the Audit Findings and Responses section of this report. We did not audit the responses, and accordingly, we express no opinion on them.

This report is intended solely for the information and use of management, Secretary Crisco, Assistant Secretary Holmes, others within the entity, the Governor, the General Assembly, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.



Beth A. Wood, CPA
State Auditor

March 9, 2012

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AUDIT FINDINGS AND RESPONSES

Matters Related to Federal Compliance Objectives

1. FEDERAL ADDITIONAL COMPENSATION OVERPAYMENTS NOT IDENTIFIED

As reported in the prior two years, the Employment Security Commission did not implement programming changes to identify overpayments for Federal Additional Compensation (FAC) payments. As such, no attempts have been made to recover overpayments for FAC as required by the American Recovery and Reinvestment Act. During the year, the Commission paid \$150.2 million in FAC payments. The Commission estimated \$689,475, or 0.5%, in FAC was overpaid, which we consider to be questioned costs.

Federal Award Information: Unemployment Insurance - funding from the Federal Unemployment Trust Fund. This finding affects funds administered under the American Recovery and Reinvestment Act.

Recommendation: The Commission should implement programming to identify federal additional compensation overpayments and begin recovering those overpayments.

Agency Response: The Unemployment Insurance (UI) and Information Systems (IS) sections have completed a thorough analysis to properly identify overpayments of Federal Additional Compensation (FAC). Based on the analysis and guidance from USDOL, the programming required for systematic recovery will be implemented in March 2012. In the past two years, UI staff applied manual methods to recover a portion of FAC overpayments.

2. ERRORS NOTED IN UNEMPLOYMENT INSURANCE BENEFIT PAYMENTS

Tests of unemployment insurance benefits payment data revealed a number of claimants had been overpaid. During the year the Commission paid \$4.4 billion in benefit payments. A summary of the tests performed and the errors found are described below.

- Tests for multiple benefit payments per week revealed 190 instances where individuals received duplicate unemployment compensation payments during the fiscal year. This resulted in \$42,626 in duplicate unemployment benefits plus \$2,375 in duplicated federal additional compensation payments. The unemployment insurance benefit system did not have an edit check to prevent multiple payments for the same benefit week.
- Tests to determine if payments were made after the benefit year-end revealed that five claimants received one additional week of benefits. This issue was caused when manual changes were made to the benefit start date without making the necessary changes to the case payment history. This resulted in overpayments of \$1,491.

AUDIT FINDINGS AND RESPONSES (CONTINUED)

- Tests to determine that the unemployment insurance benefits were calculated correctly revealed that the start date for seven claimants was reset without performing the required redetermination of the weekly benefit amount. This caused the benefits to be paid at a higher, incorrect weekly amount. The total overpayment was \$77.

The deficiencies noted in both the system and manual processing of unemployment benefit payments increase the risk of claimants receiving the wrong amount. The total known overpayments of \$46,569 are being questioned.

Aspects of this finding were reported in the prior two years.

Federal Award Information: Unemployment Insurance - funding from the State and Federal Unemployment Trust Funds. This finding affects funds administered under the American Recovery and Reinvestment Act.

Recommendation: The Commission should implement appropriate edit checks in the benefit payment system to prevent duplicate payments. The Commission should consider using analytic tools to detect errors in benefit payments.

Agency Response: We concur with the finding and as of December 31, 2011, corrective action has been taken. Appropriate edit checks were added to the Benefit Payment System to prevent future duplicate payments. Detective controls have been implemented to identify errors of this nature in the future.

3. LIMITATIONS NOTED IN THE BENEFIT AUDIT REPORTING TRACKING SYSTEM

The Benefit Audit Reporting Tracking System (BARTS) has limitations in its reporting and case management capabilities. These limitations increase the risk that cases that have been identified as possible overpayments will not be monitored effectively and therefore impacts the ability to recover related overpayments.

Federal regulation 20 CFR 602.11(d), requires the Commission to establish and maintain a quality control function within which to operate a Benefit Accuracy Measurement (BAM) program to assess the accuracy of unemployment benefit payments and denied claims. As prescribed in the Employment and Training Handbook, the BAM program must include crossmatches with the National Directory of New Hires (NDNH).

The Commission's Benefit Payment Control section performs this quality control function and uses the BARTS to document matches and cases initiated by the performance of weekly crossmatches with the NDNH. Based on these crossmatches, approximately 600 wage audit notices are automatically sent to claimants and employers to determine if the claimant is eligible for benefits. After the requested information is returned, a case is opened and the information is tracked in BARTS. However, there was no evidence of tracking and monitoring cases for which the wage audit notification information is not returned.

AUDIT FINDINGS AND RESPONSES (CONTINUED)

According to the BARTS internal policy, cases should be worked and completed within 30 days to ensure timely action on potential claim overpayments. The system does not produce summary reports that the Commission management can use to ensure that cases that are established in BARTS are investigated and closed in a timely manner. Although management can review case detail and status on screen for individual investigators and on a case-by-case basis, there was no evidence during our audit period of the monitoring procedures over the investigators' case status and timely completion.

The limited reporting capabilities and lack of evidence in monitoring pending and assigned cases to ensure that they are processed and completed timely increases the risk for failure to identify potential fraud or error and may impact the ability to recover related overpayments.

Federal Award Information: Unemployment Insurance - funding from the State and Federal Unemployment Trust Funds. This finding affects funds administered under the American Recovery and Reinvestment Act.

Recommendation: The Commission should continue working with the BARTS vendor to enhance the reporting capabilities to ensure case information is available in a readily usable manner by management. The Commission should enhance procedures to ensure case tracking and monitoring is evidenced.

Agency Response: We concur with the finding and as of October 31, 2011, corrective action has been taken. Corrective actions to fix the reporting capabilities within the Benefit Audit Reporting Tracking System (BARTS) can only be performed by the vendor. The Division of Employment Security (DES) management has consulted with the vendor on fixing this system issue, and the vendor is diligently working to correct the system error. However, in the interim, DES management has employed a work-around to improve monitoring efforts until the vendor corrects the reporting issues within BARTS. DES management has acquired the data that would normally be reported from BARTS within a spreadsheet, and will utilize this spreadsheet to enhance monitoring and case tracking efforts.

4. INSUFFICIENT DOCUMENTATION NOTED IN WORKFORCE INVESTMENT ACT CASE FILES

The Workforce Investment Act (WIA) case files did not contain sufficient or appropriate documentation to provide evidence of eligibility. This condition increases the risk that services will be provided to ineligible individuals.

Our tests of 60 participants' case files revealed the following:

- One participant was provided training services prior to receiving intensive services. In accordance with 20 CFR 663.310, training services may be made available to adults and dislocated workers who have received at least one intensive service. These services were deemed ineligible in the amount of \$260 and are being questioned.

AUDIT FINDINGS AND RESPONSES (CONCLUDED)

- The case files for three participants did not include a signed “Entitlement Questionnaire,” form NCSES-2723, which is required by policy within the Workforce Plus Entitlement System. By reviewing information outside the case file, we determined that the participants were eligible for WIA services.
- Eight participant case files did not contain the required Financial Analysis Award (FAA) Form. North Carolina Department of Commerce Local Area Issuance No. 2000-02 and the WIA Application Guide require the FAA or alternate form to document available financial resources and eligibility to receive WIA resources for training. Based on other information in the case files the participants were deemed eligible for WIA services and costs were not considered questionable.

The WIA Application Guide requires that documentation be obtained and maintained that supports the eligibility determinations made to receive WIA resources and services. Since it is likely that the questioned costs in the population will exceed \$10,000, the \$260 in ineligible services is considered questioned costs.

Federal Award Information: Workforce Investment Act Cluster pass-through funding from Local Workforce Investment Boards through contracts with local employment security offices. Specifically, Local Board contract numbers: 10-2030-36-9900 with Centralina; 10-2020-55-9900 and 10-2030-55-9900 with Southwestern; 08-4030-43-9900 with Kerr Tar; 08-4030-44-9900 with Lumber River; 10-2020-60-9900 and 10-2030-60-9900 with Triangle South; 09-2030-34-9900 with Capital Area and 10-2030-33-9900 with Cape Fear.

Recommendation: The Commission should strengthen controls and enhance its monitoring to ensure proper documentation is obtained and maintained in participants’ case files to support eligibility and allowance for service costs.

Agency Response: We concur with the finding and as of December 31, 2011, corrective action has been taken. Corrective actions were taken to ensure the following:

- We investigated the one instance where a training participant received training services prior to the documented enrollment process. With approval from the Local Workforce Area, the enrollment process has been corrected and documented to show the participant’s enrollment into training services was prior to the actual beginning of training.
- We included a signed NCSES-2723 form for three participants’ case files.
- We included the missing Financial Analysis Award for eight participants’ case files.

Workforce Solutions will continue to work with the Local Workforce Area Boards to enhance its monitoring efforts of case files. Also, larger sample sizes will be used to provide more supervisory oversight of case file management.

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Audit reports issued by the Office of the State Auditor can be obtained from the web site at www.ncauditor.net. Also, parties may register on the web site to receive automatic email notification whenever reports of interest are issued. Otherwise, copies of audit reports may be obtained by contacting the:

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