

Finding Number	2014-036
CFDA Number	17.225
Program Name	Unemployment Insurance
Federal Agency	Department of Labor
State Agency	Department of Labor and Workforce Development
Grant/Contract No.	ES-23025-12-55-A-47; ES-24646-13-55-A-47; UI-19610-10-55-A-47; UI-21127-11-55-A-47; UI-22341-12-55-A-47; UI-23919-13-55-A-47; UI-25232-14-55-A-47; EUC, Fed EB, UCFE, and UCX; FAC Benefits & UI Admin; and TUC-State Expenditures
Federal Award Year	2010 through 2014
Finding Type	Material Weakness
Compliance Requirement	Other
Questioned Costs	N/A
Repeat Finding	2013-025

To prevent further erosion of the public’s trust in the UI program, management needs to aggressively implement full corrective actions to the numerous control and compliance deficiencies

Background

Management of the Department of Labor and Workforce Development is responsible for establishing and maintaining the processes and internal controls for the department’s programs, including the Unemployment Insurance (UI) program. Management is also responsible for complying with the federal grant requirements in its operation and oversight of the program in Tennessee. Current management assumed this responsibility during the last quarter of fiscal year 2013 and inherited some of the issues reported in this finding for fiscal year 2014.

The UI program is designed to provide benefits to claimants who lose their jobs through no fault of their own. The program is funded by the Tennessee Unemployment Insurance Trust Fund, which was established by the State Unemployment Tax Act. Employers pay premiums into this fund based on the first \$9,000 of wages earned by each covered employee each year. If benefit payments from the trust fund exceed premiums collected from employers, the department is responsible for replenishing the fund and generally accomplishes this by raising premium rates.

Approved claimants may qualify to receive unemployment benefits from the state’s trust fund for up to 26 weeks based on a calculated weekly benefit amount. Once the initial 26 weeks have been exhausted, unemployment benefits may continue through federally funded grants.

Condition

As stated in the 2012 and 2013 *Single Audit Reports*, department management did not adequately address weaknesses in critical functions of the UI program. Our testwork for the period July 1, 2013, through June 30, 2014, showed similar control and compliance deficiencies as the prior period, as well as new deficiencies, all of which are described below.

During testwork, we found that department personnel were unable to properly manage all of the claims submitted through the program. Specifically, the department continued to have backlogs in receiving and responding to incoming telephone calls (staff only answered 2% of calls in fiscal year 2014); resolving pending claims (backlog of 11,899 claims at June 30, 2014); and investigating potentially overpaid claims (backlog was estimated at 16,000 at fiscal year-end.)

In addition, department management had not ensured that UI payments were made only to eligible individuals. Specifically, key internal controls continued to fail to identify ineligible payments to state employees, a deceased individual, state inmates, and individuals whose identities had not been verified. The department's controls also did not allow staff to determine whether partial claim recipients had earned disqualifying wages. Overpaid claims were not always processed consistent with laws, as claims containing indicators of fraud were not forwarded to the proper unit for further review. Also, we identified vulnerabilities with the UI computer system regarding the automated approval process for online claims. These weak controls resulted in the department continuing to pay millions of dollars to ineligible claimants and, despite collection efforts, the uncollected overpayment balance remained at over \$171 million as of June 30, 2014.

This audit also identified the following new deficiencies:

- management did not verify that unemployment insurance beneficiaries were searching for work, as required by law;
- management disregarded information from employers and allowed improper claim determinations to be made;
- management lacked safeguards over sensitive information;
- the Benefit Accuracy Measurement unit's independence from the claims eligibility determination process was impaired; and
- Fiscal Services⁷ incorrectly reported expenditures of federal funds for unemployment compensation for federal employees and ex-service members.

In response to the prior-year audit finding, department management stated that many of the issues were due to technological limitations. Specifically, an aged mainframe system was linked to dozens of separate systems that functioned collectively in the operation of the UI program. Based on inquiry, management is involved in a project to modernize the entire UI system, but the project is not anticipated to be completed until 2016.

Management did take corrective actions to address prior and current audit findings. These actions included the following.

⁷ Per executive order, the Department of Labor and Workforce Development has an agreement with the Department of Finance and Administration that financial accounting and reporting functions of the Department of Labor and Workforce Development will be managed and operated by the Department of Finance and Administration. This agreement includes the completion of federal reporting for the Department of Labor and Workforce Development.

- Management stated they have removed vulnerabilities associated with the automated claim approval process as of May 2014; we could not perform sufficient testwork to determine the impact of management's corrective action for this audit period ending June 30, 2014. Our next audit will evaluate the corrective actions and related impact on the program.
- The backlog of employers' benefit charge protests (involving the employers' premium rate) noted in the prior audit has been eliminated.
- The backlog of pending claims for UI benefits was reduced subsequent to our audit period.
- Subsequent to the audit period, management reported to us that it has implemented a process to reduce the backlog of potentially overpaid claims awaiting investigation; we plan to test this process in the next audit.

Criteria

The state's top officials, the federal grantor, the state's employers, and current and future UI beneficiaries expect management to effectively administer the UI program, which requires strong internal controls and proper oversight of all critical program functions and processes. This expectation is based on best business practices, and the specific criterion for each deficiency noted was included in the respective findings listed below.

Cause

Our audit of this major program determined that the department's management had not ensured critical controls and effective processes were in place and operating as needed. We also noted material weaknesses and significant deficiencies in internal control over compliance with requirements related to this federal program. We detailed several noncompliance and control weaknesses in separate findings in this audit report that indicate management did not properly administer the program during the period July 1, 2013, through June 30, 2014. (See the following Table.)

Table
Summary of Unemployment Insurance Program Findings

<u>Issue –Repeated Findings</u>	<u>Improvement Noted From Department’s Efforts</u>	<u>Finding Number</u>
Uncollected overpayments at over \$171 million place UI program at risk	No	2014-037
Delays in processing claims and establishing overpayments led to backlogs	Yes	2014-044
Benefits were improperly paid	No	2014-039
Overpaid claims were not always processed consistent with laws	No	2014-046
Key controls to detect fraudulent claims were ineffective	Yes	2014-043
Weaknesses existed in the automated approval process	Yes	2014-041
No process for verification of certifications for temporarily laid-off workers	Yes	2014-040

<u>Issue –New Findings</u>	<u>Finding Number</u>
Staff did not verify claimant work searches	2014-038
Management lacked safeguards over sensitive information	2014-047
Fiscal Services incorrectly reported expenditures	2014-045
Management disregarded information from employers and allowed improper eligibility determinations to be made	2014-042
The Benefit Accuracy Measurement unit’s independence was impaired	2014-048

Effect

Management did not adequately address weaknesses in critical functions of the UI program, which continues to threaten the integrity of the UI program. While we recognize that many of the corrective actions may take months, or longer, to implement, until significant progress is made, current management will be unable to properly administer this state and federal program within the federal requirements. Without sufficient controls and oversight in the future, the department

- will continue to make improper benefit payments to ineligible claimants,
- will not hold claimants accountable for returning overpaid benefits to the department,
- will not pay benefits to eligible claimants timely,
- will continue to penalize the state’s employers by unnecessarily increasing premiums,

- will continue to jeopardize federal funding because of noncompliance,
- will continue to submit federal reports with inaccuracies, and
- will be unable to restore the public's trust in the state's ability to administer unemployment compensation to Tennessee's unemployed workers.

We are required by Office of Management and Budget Circular A-133, "Audits of States, Local Governments and Non-Profit Organizations," to report on management's compliance with requirements that could have a direct and material effect on each major program and on internal control over compliance. We noted material weaknesses and significant deficiencies in internal control over compliance for the UI program during the period July 1, 2013, through June 30, 2014. We have also qualified our opinion at the compliance requirement level for eligibility.

Questioned costs may arise from material or immaterial instances of noncompliance with federal grant requirements. These questioned costs are reported in Single Audit findings that involve violations of a provision of law, regulation, contract, grant, or other agreement governing the federal expenditures; expenditures that are not supported by adequate documentation; or expenditures involving an intentionally unnecessary or unreasonable purpose.

The grantor notifies the grantee department how any related costs should be resolved, including repayment to the grantor. It is the responsibility of the grantee department (in this case, the Department of Labor and Workforce Development) to determine and oversee appropriate corrective actions.

Three of the UI findings in this report contain questioned costs for noncompliance with federal grant-related requirements (see findings 2014-039, 2014-042, and 2014-043). The questioned costs in these findings for fiscal years 2014 and 2015 total \$280,870, of which \$238,793 was paid from the state trust fund and \$42,077 was paid from the federal grant program.

Recommendation

The Commissioner of the Department of Labor and Workforce Development should ensure that the recommendations in this report are implemented and should develop a timeline for all corrective action to address the findings in this report. The Commissioner and top management should continue to evaluate the department's corrective action plan and timeline in order to ensure progress is made to correct all findings.

Management's Comment

We concur in part.

As stated in the prior audit, many of the issues noted within this finding and audit are actually due to technological limitations. The Unemployment Insurance (UI) program is operating with a 43+ year aged COBOL mainframe system modified over the years with multiple separate systems linked to the mainframe to address incremental program changes needed over the years.

A contract to replace the entire UI Benefits System was signed in May 2014. Implementation of the new system is in progress and on-schedule to go-live in May 2016.

The department has conducted a root cause analysis and made numerous modifications to systems and processes in an effort to improve the unemployment insurance program. These include:

- The Interactive Voice Response (IVR) was modified in March 2013 by moving self-help options to the beginning of the call, which allowed more claimants to help themselves.
- A new Telephone Information Processing System (TIPS) line was deployed in February 2014 that allows claimants to reset their personal identification number (PIN) and to correct incorrect response to the weekly certification questions.
- A new ticketing application, ZenDesk, was implemented in March 2014. This application works to reduce phone calls and allows staff to track issues without duplication of work, and measure staff's effectiveness and efficiency in answering those issues. Also, this application provides for a self-help knowledge base. To date over 100,000 tickets have been created by over 56,000 claimants. Customer satisfaction remains over 80% through the application's helpdesk.
- A claims status tracker was implemented and utilized by claimants 182,211 times between July and December 2014.
- The new imaging center improved the efficiency and timeliness of claim processing by maintaining all documentation in one place.
- LEAN events were held for Benefit Payment Control (BPC), claims, and collections – several recommendations from these sessions have already been implemented.

Update on Backlogs:

- As noted in the audit, the benefit charge backlog has been eliminated. The backlog peaked at 22,000 in June 2013 and was cleared by June 5, 2014.
- The backlog of 12,375 claims over 21 days awaiting decision was cleared by October 1, 2014.
- The backlog of benefit payment control cases has been reduced from 40,869 in February 2014, to 363 cases as of February 14, 2015. The backlog will be cleared by March 30, 2015.
- Over \$31 million in overpayments have been set up during the clearing of the benefit payment control backlog. Over \$27 million of this amount was designated as fraudulent overpayments.
- The department continues to participate in the Treasury Offset Program. Since July 2012, \$28 million has been intercepted from individual tax returns.

The department acknowledges that improvements to the overall program take time. Much of the time during the audit period was spent analyzing issues and setting in place new processes and

procedures. Often these required some system modifications as well. Progress has been slow, but it has also been steady.

In January 2015, the State of Tennessee received the federal Final Determination regarding the findings contained in the *2013 Single Audit Report*. The federal Final Determination indicated the noted issues were corrected.

Auditor's Comment

With regard to management's comments concerning the aged UI benefit information system, many issues noted in the finding were not caused directly by the current information systems. Management should ensure that proper procedures for determining eligibility are established and followed in order to prevent overpayments, no matter the age of the information system. Management also has the responsibility to establish procedures to compensate for any shortcomings in the information system.

Additionally, the U.S. Department of Labor issued its Final Determination of Tennessee Department of Labor and Workforce Development's *2013 Single Audit* findings based on the department's submission of documentation and correspondence relevant to correct any unresolved or pending issues from that audit. The U.S. Department of Labor has notified the department that its submission of corrective actions was accepted and will be monitored to ensure effective implementation. Based on our *2014 Single Audit* of the Tennessee Department of Labor and Workforce Development, management has not fully implemented corrective action as noted in the finding above.

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Federal Award Year	2010 through 2014
Finding Type	Material Weakness
Compliance Requirement	Eligibility
Questioned Costs	N/A
Repeat Finding	2013-026

Overpayment levels remain high and place the Unemployment Insurance program at risk

Background

The Department of Labor and Workforce Development provides Unemployment Insurance (UI) benefits to individuals who meet certain eligibility criteria. An overpayment occurs when a person receives unemployment compensation to which he or she is not entitled, whether due to error or fraud. Overpayments are a normal part of the UI program, due to the nature of the eligibility determination process, including the fact that the department must rely on employers and claimants to supply accurate and timely information. State law requires individuals to return overpayments to the department, as well as additional penalties and interest if the claimants obtained overpayments fraudulently. Once an overpayment is identified, the department establishes an accounts receivable in its accounting records. Outstanding overpayments remain on the department's accounts receivable for six years, after which time they are written off as uncollectible, in accordance with state law.

The department's Benefit Payment Control (BPC) unit is responsible for preventing, detecting, establishing, and collecting overpayments. BPC staff attempt to collect identified overpayments from those claimants via garnishing wages or reducing current UI benefits. In addition, the department participates in the Treasury Offset Program, a federal program that intercepts individual tax refunds to offset delinquent debts owed to federal and state programs.

Condition

As stated in the 2012 and 2013 *Single Audit Reports*, the department failed to ensure the operating effectiveness of its internal controls over the claimant eligibility determination process, resulting in an excessive amount of overpayments that continued to threaten the integrity of the UI program. In response to the prior audit finding, department management stated that initiatives were in progress to enhance the BPC unit's performance. As of the end of the current audit period, management had completed some but not all of these initiatives.

As part of this audit, we performed an analysis of UI overpayments to determine any changes to current-year and overall levels of overpayments, which should have decreased if management's controls were preventing and identifying overpayments in a timely manner. Additionally, we expected a decrease in overpayments given the large decrease in overall benefit payments from \$779 million in fiscal year 2013 to \$473 million in fiscal year 2014 (a 40% reduction). Based on our analysis, however, the current balances and trends in established overpayments fell short of expected outcomes. The overall overpayment balance and established overpayments in the current year were expected to be lower because these amounts are correlated with the amount of benefit payments for the current year.

- As of June 30, 2014, the department had a balance of more than \$171 million of uncollected UI overpayments. This balance was a cumulative amount of \$98 million uncollected overpayments over the past 6 years (including established overpayments for fiscal year 2014) and an estimated \$73 million of potential overpayments. For accounting purposes, in conjunction with Department of Finance and Administration fiscal staff, management estimated the value of potential overpayments based on the amount of benefit expenditures incurred throughout the previous two years multiplied by the department's internally developed overpayment rate.⁸ Although this overall balance decreased \$10 million from the department's \$181 million balance in fiscal year 2013 (an approximate 6% decrease), the reduction in the balance was less than expected considering the reduction in payments to beneficiaries during fiscal year 2014. We concluded that management continues to overpay UI benefits because controls to prevent overpayments still need improvement.
- During the period July 1, 2013, through June 30, 2014, the department identified \$20.8 million of UI benefits paid to ineligible claimants. This was a decrease of \$3.6 million (15%) from the \$24.4 million in benefit overpayments identified in fiscal year 2013, but the reduction of current-year overpayments was less than expected, considering the approximately 40% decrease in benefit payments.
- Management's efforts to collect overpayments were still not sufficient to recover the total overpayments during the audit period. The department's five-year historical overpayment collections data shows that the average collection rate for UI overpayments is approximately 24%. Collections, write-offs, and other deductions to the cumulative uncollected overpayment balance totaled \$18.1 million in fiscal year 2014. This collection effort was not enough to offset the \$20.8 million of current-year overpayments and the \$1.9 million of related penalties established, both of which added to the already high cumulative accounts receivable balance. Therefore, we concluded that the combination of a lack of controls and insufficient collection efforts continue to negatively effect the outstanding overpayment balance.

⁸ Federal regulations require the department's Benefit Accuracy Measurement (BAM) unit to conduct statistically valid samples of testwork on UI eligibility determinations that department staff has already performed. The BAM testwork is used, among other things, to determine the department's BAM Operational Rate. This rate is the percentage of benefit payments that the state should reasonably be expected to detect and establish as overpayments for recovery. The department and the Department of Finance and Administration also use the rate to calculate potential overpayments: current year ([total benefits paid x BAM operational rate]-overpayments already established) + prior year ([total benefits paid x BAM operational rate]-overpayments already established).

Criteria

According to Office of Management and Budget Circular No. A-133, “Audits of States, Local Governments, and Non-Profit Organizations,” Part 6, *Compliance Supplement*, the department must have sufficient controls “to provide reasonable assurance that only eligible individuals . . . receive assistance under Federal award programs.”

Department of Finance and Administration Policy 23, *Accounts Receivable – Recording, Collection, and Write-Offs*, requires state agencies to “make a reasonable effort to collect all receivables on a systematic and periodic basis.”

Cause

The department lacked proper controls over eligibility determinations, which resulted in an excessive amount of UI benefits issued to ineligible claimants. The department also lacked proper controls within its BPC unit to timely investigate and, where appropriate, establish overpayments for suspicious eligibility cases.

Effect

The department’s failure to ensure the operating effectiveness of its internal controls over the claimant eligibility determination process continues to threaten the integrity of the UI program. Given the significant amount of overpayments already paid out to ineligible claimants, as described above, management cannot afford to delay corrective action without further eroding the public’s trust in the UI program. Furthermore, the state, the employers, and the federal grantor are all impacted when the department continues to overpay UI benefits while collecting on average only 24% of the overpayments. The remaining 76% of overpaid benefits are uncollectible, and this loss further threatens the viability of the UI program.

Recommendation

The department should take immediate action to implement a strong system of internal controls over the claimant eligibility process for the UI program. This control system should both prevent and detect errors and fraud and mitigate the risk that UI benefits will be paid to ineligible claimants. The Commissioner should ensure that BPC unit staff investigates potential overpayments to ineligible UI claimants in a timely manner.

Management’s Comment

We concur in part.

As stated in the previous year’s audit, the department does not agree with the estimated overpayment amounts.

Many of the issues noted within this finding and audit are actually due to technological limitations. The Unemployment Insurance (UI) program is operating with a 43+ year aged

COBOL mainframe system with multiple separate systems linked to the mainframe to address program changes needed over the years. A contract to replace the entire UI Benefits System was signed in May 2014. Implementation of the new system is in progress and on-schedule for completion in May of 2016.

The department does not agree with adding an estimated overpayment amount. The original reason for doing so was due to a backlog within the Benefit Payment Control (BPC) Unit.

A Lean Event conducted in February 2014 resulted in a plan to eliminate the backlog. At that time, the backlog consisted of 40,869 cases pending review. Vacant auditor positions were filled and overtime was authorized to address these cases. All overpayments were centralized within the BPC unit by August 1, 2014. As of February 7, 2015, there are 573 cases remaining to be reviewed and \$28,257,256 set up as overpayments. This is far lower than the \$94.5 million estimated in last year's audit or the \$73 million being estimated in this year's audit.

It should also be noted that the Benefit Payment Control Unit is up-to-date on all cross-match reports. Without a backlog, estimating potential overpayments is not an accurate portrayal of the program.

As of January 2, 2015, the department established a new unit devoted entirely to collection efforts. The UI Recovery Unit was formed to efficiently pursue collection of money owed to the department. The department is continuing to participate in the Treasury Offset Program (TOP), in addition to other collection efforts. The department has also purchased SAS (a predictive statistical package) to assist with identifying fraud. The procurement of this software began in November of 2012 and was approved by CPO in November of 2014. We expect implementation to occur by May of 2015.

This finding indicated a receivable balance of \$171 million, while \$73 million is estimated. (It is important to note that over the last six (6) calendar years the cumulative amount of overpayments established was \$165 million, of which \$71.5 was collected. During that same period approximately \$6.5 billion in benefits was paid out. This results in an overpayment rate of 2.5%. Deduct our collections and the overpayment amount is 1.3% of the total benefits paid in the last six (6) years.

Auditor's Comment

Management estimated the amount of potential overpayments in conjunction with the Department of Finance and Administration.

With regard to management's comments concerning the reduction in the backlog of potential overpayment cases, the majority of this reduction occurred subsequent to our audit period. Therefore, we did not verify the amount of reduction but will do so during the next audit.

With regard to management's comments concerning the aged UI benefit information system, many issues noted in the finding were not caused directly by the current information systems. Management should ensure that proper procedures for determining eligibility are established and

followed in order to prevent overpayments, no matter the age of the information system. Management also has the responsibility to establish procedures to compensate for any shortcomings in the information system.

Finally, with regard to management's comments concerning the formation of the UI Recovery Unit and the implementation of predictive statistical software, this did not occur during our audit period. Therefore, we will examine the effect this may have on overpayments during the next audit.

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State Agency	Department of Labor and Workforce Development
Grant/Contract No.	ES-23025-12-55-A-47; ES-24646-13-55-A-47; UI-19610-10-55-A-47; UI-21127-11-55-A-47; UI-22341-12-55-A-47; UI-23919-13-55-A-47; UI-25232-14-55-A-47; EUC, Fed EB, UCFE, and UCX; FAC Benefits & UI Admin; and TUC-State Expenditures
Federal Award Year	2010 through 2014
Finding Type	Significant Deficiency
Compliance Requirement	Eligibility
Questioned Costs	N/A
Repeat Finding	N/A

Random audits of work search verifications were not conducted

Background

In 2012, the Tennessee state legislature passed the Unemployment Insurance Accountability Act (the Act) in response to complaints from the employer community that an excessive number of Unemployment Insurance (UI) claimants receive benefits to which they are not entitled, particularly because they may not be attempting to find new employment. The Act strengthened eligibility requirements for claimants seeking unemployment benefits, including the requirement that UI claimants demonstrate a reasonable effort to secure work by contacting at least three employers per week or accessing services at a career center. The Act requires the Department of Labor and Workforce Development to conduct random weekly audits to verify the integrity of claimants' work search activity. Current statute requires the department to randomly audit the work search activity of 1,500 claimants per week, which is 78,000 per year.

When the Act was passed into law in 2012, prior department management told the legislature that an anticipated information systems upgrade would allow the department to automatically audit work search activity at minimal cost by requiring all UI claimants to record their weekly work search activity in a central database. Since 2012, the information systems upgrade has transformed into a larger project to modernize the entire UI system, and the upgrade is not anticipated to be completed until 2016. Based on inquiry with management, without the new system in place, the department has had to rely on its existing limited resources to meet audit requirements.

The responsibility for auditing work search verifications was initially appropriately assigned to the Job Services unit, which was organized under the department's Employment Security Division at the time. In late 2012, Job Services was restructured under the newly created Workforce Services Division. As a result of the reorganization, responsibility for work search audits moved with Job Services to the Workforce Services Division, where it has remained since.

We have interpreted the Act's audit requirement to encompass random selection of weekly samples from the entire population of UI claimants that are required to search for work.

Condition and Cause

The department has not established a process to perform weekly audits of UI claimants and has not performed weekly audits of 1,500 claimants per week as required by the Act.

Based on our interviews with Workforce Services Division management, we found that management has not selected random samples each week of 1,500 UI claimants to determine if each claimant had met the work search requirements.

Instead, we found that management performs the following activities:

- Workforce Services Division staff periodically estimates the number of UI claimants who received services at the department's career centers and the number of claimants who were required to participate in the Reemployment and Eligibility Assessment⁹ (REA) initiative. Management told us that they meet the Act's audit requirements because these totals represent UI claimants that have accessed services at the department's career centers and participated in REA.
- Workforce Services Division staff conducts audits of work search activity of those claimants registered to use the department's jobs4tn.gov website.

While these activities are designed to provide management with the number of individuals that utilize the career centers and participate in REA, they are not designed to detect claimants who have not met the work search requirement, which is the purpose of the individualized audits.

We also evaluated the division's audits of work search activity for those who were registered to use the department's jobs4tn.gov website. We found that UI claimants are not required to register to use the website; therefore, division staff cannot select random weekly audit samples from the entire population of UI claimants. Division staff stated that they performed 26,540 audits of registered claimants during fiscal year ended June 30, 2014.

In addition, we also found that top management assigned the responsibility of compliance with the Act's requirements to management of the Workforce Services Division, even though the Act places this responsibility with the department's Employment Security Division Administrator.

Criteria

According to Section 50-7-302(a), *Tennessee Code Annotated*, a UI claimant

shall provide detailed information regarding contact with at least three (3) employers per week or shall access services at a career center created by the

⁹ The Reemployment and Eligibility Assessment is a federal program designed to help certain at-risk unemployed individuals re-enter the workforce. In Tennessee, the program is known as the Reemployment Services Assessment.

department. The administrator shall conduct random verification audits of one thousand five hundred (1,500) claimants weekly to determine if claimants are complying with the requirement of contacting at least three (three) employers per week or accessing services at a career center.

Section 50-7-203(a), *Tennessee Code Annotated*, defines “the administrator” as “the chief administrative officer of the division of employment security of the department of labor and workforce development.”

Effect

By failing to perform work search verification audits in the quantity and manner prescribed by the Act, the department has not fulfilled its obligation to employers and employees to ensure that UI benefits are appropriately distributed to claimants who comply with work search mandates. The department has potentially missed opportunities to identify, suspend, and recoup payments issued to claimants who did not make a reasonable effort to secure work while collecting UI benefits. The department has also not complied with the Act’s requirement to assign oversight for this responsibility to the Employment Security Division Administrator.

Recommendation

The department should transfer responsibility for UI work search verification audits from the Workforce Services Division to the Employment Security Division Administrator. Pending completion of the UI systems modernization project, the Employment Security Division Administrator should develop a process to obtain a weekly population of all UI claimants who are required to search for work. Staff should randomly select and audit a minimum of 1,500 claimants from this pool each week.

Management’s Comment

We do not concur.

The state statute allows the UI claimant to have two options, which include contact with three (3) employers or services at a career center. The department has evidence showing UI claimants were receiving services through the career centers. During the audit period, 176,575 UI claimants received services through the career centers. Of those 176,575 claimants, 158,581 received workforce information services; 168,477 received staff assisted services; 69,828 received career guidance; 54,959 participated in job search activities; and 32,126 were referred to employment. Therefore, we have complied with the state statute.

Additionally, the new UI Benefit System will enhance the capturing of job search activities during the claimant’s weekly certification.

Lastly, no funding was provided to enforce this state statute.

Auditor's Comment

Section 50-7-302(a), *Tennessee Code Annotated*, specifically states that

...The administrator shall conduct random verification audits of one thousand five hundred (1,500) claimants weekly to determine if claimants are complying with the requirement of contacting at least three (three) employers per week or accessing services at a career center.

The department did not conduct random verification audits of 1,500 claimants weekly as required. Management's mere calculation of the total claimants who access services at career centers does not meet the requirements of state law, which are to identify those claimants who have not attempted to contact at least three employers per week or who have not accessed services at a career center.

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Federal Award Year	2010 through 2014
Finding Type	Material Weakness and Noncompliance
Compliance Requirement	Eligibility
Questioned Costs	\$17,602
Repeat Finding	2013-027

The Unemployment Insurance program made improper benefit payments

Background

The Unemployment Insurance (UI) program provides benefits to unemployed workers for periods of involuntary unemployment (workers who have lost their jobs through no fault of their own). The program is funded by the Tennessee Unemployment Insurance Trust Fund (UTF) and federal grants. The UTF, established by the State Unemployment Tax Act, is funded by employer premiums. Claimants who are approved for the UI program are eligible to receive up to 26 weeks of benefits, which are funded by the UTF. Once the 26 weeks of benefits have been exhausted, the unemployment benefits can be extended through federally funded grants. As of January 1, 2014, claimants are only eligible to receive the 26 weeks of benefits funded by the UTF.

According to state regulations, individuals filing UI claims with the department must meet certain earnings (monetary) requirements from past employment and must be currently unemployed or earning less than their weekly benefit amount up to the \$275 maximum weekly benefit amount. Once the monetary requirements are met, other non-monetary eligibility requirements must be met before a claim is approved. For example, claimants must have separated from their most recent employer through no fault of their own, and claimants must be able and available for work. These separation and personal eligibility issues must be evaluated by the Department of Labor and Workforce Development's Employment Security Division staff before a decision to approve benefits can be made. In the past, UI claimants who were determined to be eligible received up to an additional \$15 for each minor dependent, not to exceed a total of \$50 a week. The corresponding statute was amended on July 1, 2013, and the requirement to compensate UI claimants with a minor child was deleted. Division staff paid the last eligible dependent benefits on December 28, 2013.

For both the 2012 and 2013 *Single Audit Report*, we noted control weaknesses in the division's eligibility determination process, including but not limited to failing to maintain documentation to support eligibility determinations and dependent allowance benefits. Department management

concurrent with the weaknesses noted in the 2012 report and concurred in part with weaknesses noted in the 2013 report. Department management did not concur with the weakness noted in the 2013 report for the condition regarding the lack of documentation for dependent payments and stated that their policies and procedures do not specifically require this documentation.

Condition and Criteria

As noted in the two prior audits, the department did not ensure the operating effectiveness of controls over claimants' eligibility determinations. We selected a random nonstatistical sample of 100 benefit payments from a population of 2,067,415 weekly payments for the period July 1, 2013, through June 30, 2014. The sample represented \$21,373 of \$452,296,646 total UI benefit payments. Based on our eligibility testwork, we noted the following:

a. Documentation for Eligibility Determinations

According to Part 6, Compliance Supplement, of the Office of Management and Budget Circular A-133, the department must have sufficient controls "to provide reasonable assurance that only eligible individuals . . . receive assistance under Federal award programs."

- For 22 of the 100 claims tested (22%), division staff paid ineligible claimants or paid claims without proper supporting documentation. Specifically, we found that division staff did not
 - perform additional follow-up to determine claimants' eligibility when employers reported to the department that claimants had earned wages that conflicted with the claimants' previous assertions of the amount of income earned (eight claims);
 - have the required documentation to award UI benefits to the claimant (one claim);
 - send required second requests to the employers for separation information (seven claims);
 - send initial requests for separation information to the claimants' previous employers (two claims); or
 - consider conflicting separation information received from the claimants' previous employers (two claims).

For 20 of the 100 claims, we noted that claimants received payments for dependents. We found that division staff did not maintain documentation to support the dependent allowance benefit payments for one claimant. Furthermore, division staff did not make a required dependent allowance payment to one of the claimants (see Table 1 for results.)

Table 1
Eligibility Sample Errors

Category	Eligibility	Dependent Allowance
Sample Size	100	20
Number of Errors	20	2
Error Rate	20%	10%

b. Standard for Benefit Payment Promptness

Title 20, *Code of Federal Regulations*, Section 640, states that the department should issue the first benefit payment based on the claim’s eligibility decision within 14 days of the first compensable week.¹⁰

- For 50 of the 100 claims tested (50%), division staff did not issue a decision on the claimants’ eligibility for UI benefits within 14 days of the first compensable week, as required by U.S. Department of Labor.

c. Second Request for Separation Information

According to the department’s *Unemployment Insurance Program Manual*, Section 5117, “Procedures When Employer Fails to Respond Timely,”

The employer’s failure to respond to the Time Sensitive Request for Separation Information does not relieve the agency of the responsibility to attempt to obtain employer information. At least one attempt must be made to contact the employer by telephone if no response is received.

Request for Separation Information

According to Section 50-7-304(b)(2)(C), *Tennessee Code Annotated*,

Employer Response to Request for Separation Information. If a separation issue exists, the separating employer will be asked to supply information describing circumstances leading to the separation. The information must be received by the agency within seven (7) days from the date the agency request for information is mailed to the separating employer. In the absence of the response, the decision of entitlement will be based on the claimant’s statement and other information available to the agency.

- For 9 of 88 applicable claims tested¹¹ (10%), division staff did not sufficiently contact the claimants’ separating employers for input regarding the claimants’ eligibility.

¹⁰ Section 50-7-302(a)(5)(A), *Tennessee Code Annotated*, requires a mandatory “waiting week” for which claimants do not receive unemployment benefits. Therefore, in Tennessee the standard is 21 days following the beginning of a claimant’s eligibility (7-day waiting week + 14 days following the first compensable week).

(These errors were also included in the *Documentation for Eligibility Determinations* section above.) Specifically, we found that division staff did not

- send initial requests for separation information to the claimants' previous employers (two claims); or
- send second requests for separation information to the employers (seven claims).

d. *Agency Decision*

Section 50-7-304(b)(1)(B), *Tennessee Code Annotated*, states that

The agency representative shall promptly give written notice to the claimant and all other interested parties of the nonmonetary determination and the reasons for the determination. The nonmonetary determination of the agency representative shall become final, unless an interested party files an appeal from the nonmonetary determination within fifteen (15) calendar days after the date of mailing of the written notification of the nonmonetary determination to the last known address of the party, or within fifteen (15) calendar days after the date the written notification is given to the party, whichever first occurs.

- For 40 of 94 applicable claims tested¹² (43%), division staff did not follow proper review and approval procedures. Specifically, we found that division staff did not
- maintain documentation of issuing agency decision letters to the claimants or the claimants' separating employers (33 claims);
 - review claims to ensure the requests for separation information were sent to the correct employer addresses prior to issuing agency decisions (three claims, two of which were reported above for when staff did not maintain documentation of issuing the required agency decision letters);
 - issue agency decisions by a qualified staff member (five claims); or
 - allow the employer sufficient time to respond to the request for separation information (one claim).

¹¹From our testwork of 100 claimants, division staff was not required to contact the previous employers for 12 claimants, because the separating employer had already provided the department with documentation verifying the claimants' reason for separation from employment.

¹²From our testwork of 100 claimants, division staff was not required to review six claimants, because they were partial claims filed by the claimants' previous employers. Partial claims are claims filed by employers on behalf of employees who are temporarily laid off from work. The department's computer system automatically processes these claims if there are no other issues with the claims.

Cause

Management did not fully implement corrective actions to improve the operating effectiveness of controls over its claimants' eligibility determination process or to comply with the UI program procedures in determining claimants' eligibility. Specifically, division staff did not

- maintain required documentation to support the claimants' eligibility for either regular unemployment benefits or dependent allowance benefits;
- adhere to federal guidelines for benefit payment promptness;
- sufficiently contact the claimants' previous employers;
- properly issue agency decision letters to notify the parties involved when an eligibility determination has been reached; and
- document a review of claims to ensure the correct employers were contacted.

Effect

When division staff does not promptly seek employers' responses to claimants' requests for benefits upon separation from the employers, the associated risk that the department will pay UI benefits to ineligible claimants increases. Similarly, when division staff does not send agency decision letters to notify all parties of the department's decision to issue benefits, it deprives the separating employers of their right to file an appeal of the eligibility decision, thus increasing the risk that the department will pay UI benefits to ineligible claimants.

When management does not ensure the operating effectiveness of controls over the claimant eligibility process for the UI program, the department will continue making improper payments to ineligible individuals from UI funds (see Table 2 for a summary of known questioned costs.)

Known Questioned Costs

Table 2
Benefits Paid to Ineligible Claimants
(based on testwork sample)

Category	Federal Funds	State UI Trust Funds	Total
Eligibility Questioned Costs	\$944	\$3,417	\$4,361
Dependent Allowance Questioned Costs*	\$13	\$0	\$13
Total Questioned Costs	\$957	\$3,417	\$4,374
Total Sample Dollars Tested by Funding Source for One Benefit Week	\$3,175	\$18,198	\$21,373
Total UI Claims Paid for the Fiscal Year Ended June 30, 2014 (Population)			\$452,296,646
Error Rate (%)			20%

* We only noted questioned costs for one of the two dependent allowance errors noted. In addition, the dependent allowance payment is \$13 rather than \$15, as a result of the federally extended benefit amounts being reduced during our audit period.

Due to errors noted in our sample testwork, we extended our testwork on claimants we identified as ineligible to determine the total amount of UI and dependent allowance benefits improperly paid to these claimants through August 2, 2014. The questioned costs represent benefit payments occurring as early as fiscal year 2013. These results are shown in Table 3 below.

**Table 3
Benefits Paid to Ineligible Claimants**

Fiscal Year 2013			
	Federal Funds	State UI Trust Funds	Total
Eligibility Questioned Costs	\$903	\$21,399	\$22,302
Dependent Allowance Questioned Costs	-	\$240	\$240
Total Questioned Costs	\$903	\$21,639	\$22,542

Fiscal Year 2014			
	Federal Funds	State UI Trust Funds	Total
Eligibility Questioned Costs	\$17,446	\$60,227	\$77,673
Dependent Allowance Questioned Costs	\$156	-	\$156
Total Questioned Costs	\$17,602	\$60,227	\$77,829

Fiscal Year 2015 (established through August 2, 2014)			
	Federal Funds	State UI Trust Funds	Total
Eligibility Questioned Costs	-	\$1,094	\$1,094
Dependent Allowance Questioned Costs	-	-	-
Total Questioned Costs	-	\$1,094	\$1,094

The total amount of all federal questioned costs noted during fiscal year 2013 is \$903. The total amount of all federal questioned costs noted during our audit period, July 1, 2013, through June 30, 2014, is \$17,602. The total amount of all state UI Trust Fund questioned costs noted in this finding is \$82,960 (\$21,639 for fiscal year 2013, \$60,227 for fiscal year 2014, and \$1,094 for a portion of fiscal year 2015).

Recommendation

As recommended in the prior two audits, the Commissioner of the Department of Labor and Workforce Development should take immediate corrective action to implement a strong system of internal controls over the claimant eligibility determination process for the UI program. This control system should be designed to prevent and/or detect errors and fraud and to ensure that UI benefits are only paid to eligible claimants. Division management should ensure that payments for the UI program are made based on adequate supporting documentation, that management has properly requested separation information from employers, and that all parties are notified of the department's eligibility decisions. Division management should also review the claims

identified in our testwork and determine what corrective actions, including the collection of any applicable overpayments, penalties, and interest, should be taken.

Management's Comment

We concur in part.

As noted in the prior *Single Audit Report*, the department struggled with an inadequate case management system. When the system completely failed, a manual and paper centric operation process was the only available alternative.

In December 2013 an in-house imaging center was established, utilizing existing scanning capabilities to digitize and maintain scanned claims material in a repository readily accessible to adjudicators on their desktop computers. Adjudicators were able to begin using this repository for their decisions beginning in March 2014.

The department acknowledges that for much of this audit period the claims unit was relying on a manual process, which could result in misplaced documentation. The department does not agree with all the issues noted by the auditors regarding requests for separation information.

Documentation for Eligibility Determinations:

- Proof of dependent information was required for any claim filed on or after August 1, 2013. One claim was noted for missing dependent information; however, the dependent documentation was actually obtained, when the claimant filed a new claim on November 12, 2013.

Standard for Benefit Payment Promptness:

- As previously noted, the department had a claims backlog for the entire audit period and timeliness requirements were not met.
- By October 1, 2014, the backlog was cleared.
- The department also exceeded the US Department of Labor's first pay timeliness requirement of 87% for October 2014 and has met the standard for every succeeding month since October.
- From October 2014 through January 2015, the department processed from 90.3% to 95.5% of all initial claims within the 21-day timeliness requirement.

Request for Separation Information:

- Several scenarios occur where an employer letter is not generated, but a claim may be approved:
 - the claims were either submitted directly by the employer,

- a mass layoff list had been supplied by the employer,
 - the lack of work claim was approved over the phone by the claims agent while taking the claim, or
 - were initial claims where the separation reason had already been correctly addressed on the previous claim.
- Of the nine (9) claims noted with separation issues:
 - One claim was filed in a local office on December 6, 2012, which was outside the audit period, and no documentation was provided. Claims are no longer accepted in a local office.
 - One claim was approved, based on a misdated separation notice, but the employer did not appeal.
 - Three claims were decided without a documented second notice attempt.
 - The employer response for one claim was based on a different assignment, but the employer did not appeal.
 - Three claims were not missing any information, but the auditor determined the adjudicator needed more information. The department does not agree.

Agency Decisions:

- Decision letters are not always required. These are the same instances as when requests for separation information are not needed:
 - the claims were either submitted directly by the employer,
 - a mass layoff list had been supplied by the employer,
 - the lack of work was approved over the phone by the claims agent while taking the claim, or
 - were initial claims where the separation reason had already been correctly addressed on the previous claim.
- During the time staff worked to clear the backlog, experienced claims agents and interviewing supervisors temporarily assisted with decisions.

The department does not agree with the eligibility sample chosen for review. As in the previous audit, the sample was chosen based on payments made during the audit period. Eligibility determinations during the audit period only should have been reviewed. By continuing to review eligibility outside the audit period, the department continues to be penalized for processes and procedures that may have already been corrected.

In January 2015, the State of Tennessee received the federal Final Determination regarding the findings contained in the *2013 Single Audit Report*. The federal Final Determination indicated the noted issues were corrected.

Auditor's Comment

Request for Separation Information:

For situations in which the claim is not filed by an employer or included on a mass layoff list, management is required to verify separation circumstances with the employer (Request for Separation Information), as required by Section 50-7-304(b)(2)(C), *Tennessee Code Annotated*.

Agency Decisions:

Section 50-7-304(b)(1)(B), *Tennessee Code Annotated*, requires the department to give written notice to all interested parties of the nonmonetary determination and the reasons for the determination.

Sample Selection:

Regarding our eligibility sample selection method, we are required to determine that benefit payments made during the audit period are to eligible claimants. Management continues to pay ineligible claimants as noted above.

Corrective Action:

Finally, the U.S. Department of Labor issued its Final Determination of Tennessee Department of Labor and Workforce Development's 2013 *Single Audit* findings based on the department's submission of documentation and correspondence relevant to correct any unresolved or pending issues from that audit. The U.S. Department of Labor has notified the department that its submission of corrective actions was accepted and will be monitored to ensure effective implementation. Based on our 2014 *Single Audit* of the Tennessee Department of Labor and Workforce Development, management has not fully implemented corrective action as noted in the finding above.

Finding Number	2014-040
CFDA Number	17.225
Program Name	Unemployment Insurance
Federal Agency	Department of Labor
State Agency	Department of Labor and Workforce Development
Grant/Contract No.	ES-23025-12-55-A-47; ES-24646-13-55-A-47; UI-19610-10-55-A-47; UI-21127-11-55-A-47; UI-22341-12-55-A-47; UI-23919-13-55-A-47; UI-25232-14-55-A-47; EUC, Fed EB, UCFE, and UCX; FAC Benefits & UI Admin; and TUC-State Expenditures
Federal Award Year	2010 through 2014
Finding Type	Significant Deficiency
Compliance Requirement	Eligibility
Questioned Costs	N/A
Repeat Finding	2013-032

The department has no process to verify partial claims certifications

Background

The Department of Labor and Workforce Development’s Employment Security Division defines partial claims as claims for Unemployment Insurance (UI) benefits filed by employers on behalf of their employees (claimants) when employers must either temporarily lay off or reduce employees’ work hours. Since these claimants are still “job attached”—meaning the employers plan to rehire them in the future or the employers have only reduced their hours—they are not required to search for new employment. Regular claimants, who have filed for benefits themselves and are not anticipated to be re-hired by their former employers, must certify weekly with the division that they are actively searching for work and must list any wages earned. If the claimants’ wages earned are above a certain amount, their benefits for that week will be reduced by the amount of wages earned. Similarly, while they are temporarily laid off or are working at reduced hours, partial claimants must report any wages earned from other employment so that division staff can adjust their UI benefit for earned wages. Partial claimants are not required to actively search for work since they are still classified as job attached. Based on inquiry with division management, partial claims account for approximately 37% of all paid claims the division processes.

The division provides two options for employers to obtain employees’ attestation of earned wages. One option is for employees to complete a “worker’s statement” section within the claim, which requires employees to sign attesting to their eligibility status based on wages earned, and the employers to then submit the statements to the department. The other option requires employers to obtain and maintain the statements of wages earned on-site. In response to the prior findings, the department posted on its website a disclaimer stating that employers must obtain and maintain their employees’ workers’ statements.

Condition

As stated in both the 2012 and 2013 *Single Audit Reports*, the division still did not have a process to ensure that claimants seeking partial benefits did not earn any disqualifying wages, and therefore remained eligible for benefits. Specifically, the division did not require all partial claimants to provide weekly certifications via telephone or online attesting to any wages earned, as they do for regular claims.

As described above, some employers who submit partial claims on behalf of their employees choose to obtain and maintain workers' statements on-site; however, the division still had no process to verify that employers had obtained these statements. In their six-month follow-up report to the Office of the Comptroller of the Treasury and in the state's *Summary Schedule of Prior Audit Findings for Years 2013 and Prior*, department management stated that a quarterly review of partial claims for employee certifications would be implemented by October 31, 2014. Based on our inquiry, this review was still not implemented as of November 2014.

Management's identified control did not include the requirement that division staff verify that employers obtained and maintained employees' certifications of wages earned.

The wording of this finding does not identify specific vulnerabilities that could allow someone to exploit the department's system. Disclosing those vulnerabilities could present a potential security risk by providing readers with information that might be confidential, pursuant to Section 10-7-504(i), *Tennessee Code Annotated*. We provided department management with detailed information regarding the specific vulnerabilities we identified, as well as our recommendations for improvement.

Criteria

According to Part 6, Compliance Supplement, of the Office of Management and Budget Circular A-133, the department must have sufficient controls "to provide reasonable assurance that only eligible individuals . . . receive assistance under Federal award programs."

The *Rules of the Tennessee Department of Labor and Workforce Development* state that

The employer shall, immediately after the termination of each week (as described in 0800-09-01-.10) which begins within such benefit year and for which such worker's earnings fall below such worker's weekly benefit amount because of lack of work in such week, furnish each such worker with a copy of the Joint Low Earnings Report and Claim for Benefits for Partial Unemployment, or submit to the Department a computer diskette or other electronic report approved by the Administrator setting forth the information required. Such information includes:

- (a) the worker's name and social security account number,
- (b) the ending date of such week,
- (c) the wages earned in such week, and

(d) a proper certification as to such worker having worked less than such worker's normal customary full-time hours because of lack of work in such week.

Cause

Although the division could have required all partial claimants to provide weekly certifications via telephone or online, as they do for regular claims, it has historically chosen to treat partial claimants differently. Even though the division has a disclaimer on the department's website stating that employers must obtain and maintain their employees' workers' statements, management still did not have a process in place to verify that employers had obtained and maintained these certifications to ensure the claimants' continued eligibility for benefits.

Effect

Without a process to ensure employers maintain required workers' statements to certify claimants' wages earned and to support claimant eligibility, the department may pay benefits to those who are not entitled to them. Both employers and the department benefit from the partial claims process, but only when proper certifications are obtained and maintained.

Recommendation

Management of the Employment Security Division should ensure that all claimants, including those associated with partial claims, provide weekly certifications either to employers or to the division. Management should develop a process for division staff to periodically test a sample of these employees' certifications maintained at the employers' worksites to verify that claimants are eligible for benefits and that employers are obtaining and maintaining certifications as required.

Management's Comment

We do not concur.

The department has utilized an online automated partial claims filing system (APS) for several years. The system was designed as an easy way for employers to file claims for their job-attached workers. Approximately a third of all claims filed in Tennessee are filed via the APS. Without this system the current staffing level in the claims operations unit would be unable to handle the additional workload.

The U.S. Department of Labor does not have issues with states utilizing employer filed claims systems. Several other states use them. In fact in our region, Georgia, Alabama, and South Carolina also currently use similar systems.

Automated Partial System:

- Employers file the claim for their employees
- By virtue of the employer filing, employer approval is granted

- Claims are processed quickly (usually within 7-10 days)

As noted in the audit, the APS was modified in July 2013 to provide employers with a certification form for employees, limit of 10 consecutive weeks of filing, and require employers provide a return to work date. Employers had to consent to these requirements to use the system.

The audit recommendation for the department to “develop a process for division staff to periodically test a sample of these employees’ certifications maintained at the employers’ worksites” is essentially an unfunded and unreasonable recommendation. Requiring the job-attached workers to do their own weekly certifications is also unnecessary, since USDOL considers the employer filed certifications as acceptable.

The department previously stated a sample review of partial claims would be established by October 2014. The review will require quarterly wage data. The sample review beginning with claims filed in 4th quarter 2014 will be conducted when 4th quarter wage records are available (i.e., March or April 2015).

In January 2015, the State of Tennessee received the federal Final Determination regarding the findings contained in the *2013 Single Audit Report*. The federal Final Determination indicated the noted issues were corrected.

Auditor’s Comment

Until management verifies that partial claimants have not earned wages which would disqualify them from receiving unemployment benefits, they cannot ensure the claimants remain eligible for those benefits.

In addition, the U.S. Department of Labor issued its Final Determination of Tennessee Department of Labor and Workforce Development’s *2013 Single Audit* findings based on the department’s submission of documentation and correspondence relevant to correct any unresolved or pending issues from that audit. The U.S. Department of Labor has notified the department that its submission of corrective actions was accepted and will be monitored to ensure effective implementation. Based on our *2014 Single Audit* of the Tennessee Department of Labor and Workforce Development, management has not fully implemented corrective action as noted in the finding above.

Finding Number	2014-041
CFDA Number	17.225
Program Name	Unemployment Insurance
Federal Agency	Department of Labor
State Agency	Department of Labor and Workforce Development
Grant/Contract No.	ES-23025-12-55-A-47; ES-24646-13-55-A-47; UI-19610-10-55-A-47; UI-21127-11-55-A-47; UI-22341-12-55-A-47; UI-23919-13-55-A-47; UI-25232-14-55-A-47; EUC, Fed EB, UCFE, and UCX; FAC Benefits & UI Admin; and TUC-State Expenditures
Federal Award Year	2010 through 2014
Finding Type	Material Weakness
Compliance Requirement	Eligibility
Questioned Costs	N/A
Repeat Finding	2013-031

As noted in prior audits, the department still has weaknesses in the automated claims approval process

Background

Approval Process for Unemployment Claims

According to state regulations, individuals filing Unemployment Insurance (UI) claims with the Department of Labor and Workforce Development must meet certain earnings (monetary) requirements from past employment and must be currently unemployed or earning less than their weekly benefit amount up to the \$275 maximum weekly benefit amount. Once the monetary requirements are met, other eligibility (non-monetary) requirements must be met before a claim is approved. For example, a claimant must have separated from their most recent employer through no fault of their own. Claimants' circumstances generally fall into one of three non-monetary categories:

1. lack of work—the employer laid off the employee;
2. quit—the employee voluntarily quit with just cause; or
3. discharge—the employee's employment was terminated because of performance issues other than misconduct.

Separation issues and personal eligibility issues (those issues that involve claimants' ability and availability for work) often require evaluation by Employment Security Division staff before a decision to approve benefits can be made. For division staff, the lack of work issue is generally the easiest to resolve, as it only involves employer verification that the claimant's separation was due to lack of available work.

Online Automated Approvals

The division provides an automated claims process for claimants who can file based on the lack of work circumstances when there are no other issues for division staff to evaluate. Through its

Employment Security Combined Online Technology (ESCOT) information system, the division assigns lack of work claims with certain codes, depending on whether the claim was filed online (code 45/00) or by telephone (code 44/00). Once code 44/00 or 45/00 claims are filed, the system generates a verification letter, known as a Request for Separation Information, that is sent to the most recent employer stating that the claimant filed for UI benefits and asserts that separation from employment is due to lack of work. The letter requests that the employer respond to the division only if the employer disagrees with the claimant's assertion that his or her separation from employment was due to a lack of work. If the division does not receive a response from the employer within a certain number of days following the date that the claim was filed, ESCOT automatically approves the claim and benefits begin. Section 50-7-304(b)(2)(C), *Tennessee Code Annotated*, provides at least 7 days for the employer to respond, but department policy allowed 10 days during the audit period.

Condition

As noted in both the 2012 and 2013 *Single Audit Report*, the division did not have adequate controls over its automated approval process, and management could not be sure that employers had sufficient opportunity to dispute claims for lack of work, if necessary. During our audit period, we again noted several weaknesses in the automated approval process related to lack of work claims, as follows:

- Our review identified that the online process had programming issues for the majority of the audit period, which impacted the division's ability to ensure the lack of work verification letters reached the employers. The wording of this finding does not identify specific vulnerabilities that could allow someone to exploit the department's system. Disclosing those vulnerabilities could present a potential security risk by providing readers with information that might be confidential, pursuant to Section 10-7-504(i), *Tennessee Code Annotated*. We provided department management with detailed information regarding the specific vulnerabilities we identified, as well as our recommendations for improvement. Based on inquiry and inspection of documentation, this programming weakness was corrected in May 2014, near the end of the audit period. We will test the impact of this corrective action during the next audit.
- In order to compensate for the programming weakness in the online application process noted above, internal department policy requires division staff to conduct manual reviews of code 45/00 (online) claims. Former department management added this manual review to ensure that staff examined each online claim before the computer system automatically approved claimants' applications for benefits. We found, however, that the current system design prohibits the department from maintaining records of the initial coding for online claims and, therefore, management could not provide us with a complete population of online claims from which to test the effectiveness of the manual review process. Even though management could not provide the population of online claims, we were able to identify 23 claims originally coded as 45/00 and approved during our audit period. We found that for 2 of 23 claims (9%), division management could not provide documentation that staff

reviewed the claim to ensure that the system generated the Request for Separation Information to the most recent employer and that the employer's address was correct.

- During at least a portion of the audit period (primarily August and October 2013), the division did not have an adequate process for responding to separating employers who returned the Request for Separation Information notices to dispute claimants' lack of work assertions. We found that several claims were automatically approved for benefits even though the division had received timely responses from employers disputing the claimants' eligibility prior to the approval of the benefits (see finding 2014-042). To avoid overpayment of benefits, the division cannot allow lack of work claims to be automatically approved when employers' responses indicate they dispute the claimants' eligibility. As required by the division's stated policy, the adjudication staff must review the disputed claims and obtain statements and/or documentation from both the claimant and separating employer prior to division staff issuing decisions on the claimants' eligibility.

Criteria

Request for Separation Information

According to Section 50-7-304(b)(2)(C), *Tennessee Code Annotated*,

Employer Response to Request for Separation Information. If a separation issue exists, the separating employer will be asked to supply information describing circumstances leading to the separation. The information must be received by the agency within seven (7) days from the date the agency request for information is mailed to the separating employer. In the absence of the response, the decision of entitlement will be based on the claimant's statement and other information available to the agency. The separating employer may supply information to the agency prior to a request for information being mailed from the agency if the employer expects a separation issue to arise with regard to an employee.

According to Part 6, Compliance Supplement, of the Office of Management and Budget Circular A-133, the department must have sufficient controls "to provide reasonable assurance that only eligible individuals . . . receive assistance under Federal award programs."

Cause

- Department management did not correct the programming weakness until May 2014.
- Staff failed to document manual reviews of claims.
- The division did not have an adequate process in place to ensure that any timely response received from an employer triggered division staff to remove the claim from the automated approval process. See finding 2014-042.

Effect

When known programming issues with the online claims process and review process exist, management cannot be assured that employers appropriately receive lack of work Request for Separation Information letters. If employers do not receive these letters, they do not receive an opportunity to dispute the claimant's assertion that the separation was due to lack of work, or that the claimant was even employed by the employer. The division's approval of lack of work claims, despite receiving timely responses from employers disputing the claimants' eligibility, results in the approval of claims that should be adjudicated according to policy. The combination of these weaknesses created a risk that claimants applying for benefits (due to lack of work) could be automatically approved for UI benefits even though they were not eligible. See also finding 2014-042.

Recommendation

Management should ensure controls over its automated approval processes are sufficient to provide for proper verification of claimants' requests for UI benefits when separation occurs as a result of lack of work. Management should strengthen procedures to ensure that any employers' responses to a Request for Separation Information letter that are received timely are appropriately incorporated into the claimants' approval process and that the corresponding claims are not allowed to be automatically approved. Management should also ensure that when employers' responses are received after benefits have started, staff appropriately reviews the new information and its impact on the claimants' original eligibility determinations.

Management's Comment

We concur in part.

Many of the issues noted within this finding and audit are actually due to technological limitations. The Unemployment Insurance (UI) program is operating with a 43+ year aged COBOL mainframe system modified over the years with multiple separate systems linked to the mainframe to address incremental program changes needed over the years. A contract to replace the entire UI Benefits System was signed in May 2014. Implementation of the new system is in progress and on-schedule to go-live in May 2016.

During most of the audit period, the claims operations unit was operating entirely on a manual process of matching documents. Claims management instituted a manual review of online filed claims, including those noted as issues due to "programming weakness."

The review and documentation process include:

- 1) 45 Lack of Work (LOW) claims are reviewed when filed and the claimant is contacted, if any discrepancy is noted. The claim is reviewed again after the employer's seven day response period has ended.

- 2) 40/00s are worked and either approved when worked or sent to a suspense file for finishing. These claims are approved, if the information is verified, and adjudicated, if an issue arises.
- 3) Issue claims that the system indicates something needs to be reviewed (about 65-70% of the issue claims) are worked by a Claims Agent.
- 4) Issue claims that do not have any system indication needing review (about 30-35%) are sent straight to Adjudication.

When the department receives a mass layoff list from the employer, LOW claims that are filed, that have no re-earning requirements and no other issues, will be automatically approved.

In January 2015, the State of Tennessee received the federal Final Determination regarding the findings contained in the *2013 Single Audit Report*. The federal Final Determination indicated the noted issues were corrected.

Auditor's Comment

With regard to management's comments concerning the aged UI benefit information system, many issues noted in the finding were not caused directly by the current information systems. Management should ensure that proper procedures for determining eligibility are established and followed in order to prevent overpayments, no matter the age of the information system. Management also has the responsibility to establish procedures to compensate for any shortcomings in the information system.

Finally, the U.S. Department of Labor issued its Final Determination of Tennessee Department of Labor and Workforce Development's *2013 Single Audit* findings based on the department's submission of documentation and correspondence relevant to correct any unresolved or pending issues from that audit. The U.S. Department of Labor has notified the department that its submission of corrective actions was accepted and will be monitored to ensure effective implementation. Based on our *2014 Single Audit* of the Tennessee Department of Labor and Workforce Development, management has not fully implemented corrective action as noted in the finding above.

Finding Number	2014-042
CFDA Number	17.225
Program Name	Unemployment Insurance
Federal Agency	Department of Labor
State Agency	Department of Labor and Workforce Development
Grant/Contract No.	ES-23025-12-55-A-47; ES-24646-13-55-A-47; UI-19610-10-55-A-47; UI-21127-11-55-A-47; UI-22341-12-55-A-47; UI-23919-13-55-A-47; UI-25232-14-55-A-47; EUC, Fed EB, UCFE, and UCX; FAC Benefits & UI Admin; and TUC-State Expenditures
Federal Award Year	2010 through 2014
Finding Type	Material Weakness and Noncompliance
Compliance Requirement	Eligibility
Questioned Costs	\$3,887
Repeat Finding	N/A

Because management disregarded employers' responses disputing statements of laid-off workers, the department made improper eligibility determinations and overpaid UI benefits

Background

The Department of Labor and Workforce Development's Employment Security Division operates the Unemployment Insurance (UI) program to provide benefits for employees who become separated from their employment through no fault of their own. The division processes claims for unemployment benefits at its claims center in Nashville and in regional offices throughout the state. A claimant's circumstances generally fall into one of three categories:

1. Lack of work – the employer laid off the employee,
2. Quit – the employee voluntarily quit with just cause, or
3. Discharge – the employee's employment was terminated because of performance issues other than misconduct.

Process Described by Division

When a claimant files an unemployment claim stating he or she separated from employment due to a lack of available work, the computer system generates a Request for Separation Information that is sent to the most recent employer to inform the employer that the claimant has filed for UI benefits due to a lack of work. This notification requests that the employer respond to the division if the employer disagrees with the claimant's assertion of lack of work. State statute requires that the responses must be received by the department within seven days from the date the request for information is mailed to the employer. If the division does not receive a response from the employer within this time frame, the claim is generally approved automatically or manually without further evaluation.

The department and the state's employers each have unique responsibilities to ensure only eligible claimants are awarded UI benefits. The department must properly determine claimants'

eligibility through proper consideration of all relevant information. Likewise employers must respond promptly to the department's Request for Separation Information. When each fulfills their responsibilities, the department can prevent unwarranted benefit payments to claimants and employers can avoid future increases in their unemployment tax premiums. UI benefits are funded by a premium tax imposed on the state's employers and by the federal government. The state collects these taxes from employers to ensure the state's Unemployment Insurance Trust Fund is sufficiently maintained and available for benefits. Since employers' tax rates are partially determined by the amount of benefits paid to separated employees, those employers who experience more employee separations generally pay a higher tax rate than employers in the same industry with fewer or no separated employees.

While the division is able to approve some claims quickly, other claims that involve employee separation and personal eligibility issues require the division staff to obtain more detailed information from the claimant and often the affected employer. When the division receives employers' responses disputing the claims for lack of work, division staff further evaluate the claims. Within the department's information system, division staff re-code these claims to a pending status and transfer the claims and additional information to staff known as "adjudicators," who review and perform additional procedures as needed to determine claimant eligibility. Claims that are placed in pending status are not paid until the adjudicators obtain and evaluate this information. These additional procedures take time and have resulted in a backlog of pending claims as discussed in finding 2014-044.

The department receives the large majority of employers' responses by mail, fax, or email at the Nashville Claims Center. The claims center staff use the employers' responses to verify with the claimants' former employment the reasons for employees' separations and if the reasons were other than for lack of work. We were told that when employers' responses are received by the claims center, staff are tasked with manually matching employers' responses to the respective claims because the division abandoned its document storage system in fiscal year ending June 30, 2013.

Allegation of Improper Eligibility Determinations

In November 2013, we received an allegation stating that in order to alleviate the backlog of pending claims, the claims center staff processed and approved UI benefit claims without consideration of employers' responses that disputed claimants' assertions of lack of work. To follow up on this allegation, we gained an understanding of the division's eligibility determination process for claimants who requested benefits due to a lack of work.

During a December 2, 2013, visit to the Nashville Claims Center, we requested all employers' responses that staff were processing as of that day. The Adjudication Manager in the claims center¹³ directed us to stacks of claims that had been matched with employers' responses and were waiting assignment to adjudicators for further evaluation.

¹³ This individual was promoted to manager over the Adjudication Unit in July 2013. He was later renamed Director of the UI Integrity unit in December 2013.

Upon further review of documents in the claims center, we found that the division did in fact approve and pay benefits without proper consideration of employers' responses as discussed in the Condition section below.

Condition

From our analysis of the employers' responses and our discussions with division management and claims center personnel, we determined the following:

- A. Top management, including the Employment Security Division Administrator, did not provide proper oversight of the eligibility determination process. The Administrator allowed the claims center Director¹⁴ and Adjudication Manager to operate the claims center without her input or approval regarding the processing of claims. The Administrator and the claims center Director were unaware of the details of the changes that the Adjudication Manager made to the established process involving employers' responses that disputed claimants' assertions of lack of work. The claims center's director did not ensure that staff were properly instructed when key eligibility process functions changed. In addition, management did not ensure sufficient and accurate information was provided to us during the audit.

Specifically, we found the following changes to the established process and internal controls:

- Claims center management and staff failed to properly match employers' responses to the related claims; therefore, the complete documentation was not sent to those tasked with making eligibility determinations. The employers' responses should have been paired with the respective claims and subsequently sent to adjudicators for evaluation.
- Claims center management and staff failed to ensure that all lack-of-work claims were properly re-coded in the department's information system after receiving contradictory statements from employers.
- Claims center management failed to sufficiently communicate eligibility process changes to appropriate staff—changes that were needed so that staff could make proper eligibility determinations. We also found that the claims center management sent different instructions to the regional offices. As a result, staff in both the Nashville Claims Center and in the regional offices approved claimants for benefits without the employers' responses that disputed claimants' assertions regarding lack of work. Based on our discussions, the Adjudication Manager stated that for one regional office, the staff were told to contact the claims center regarding any available employers' responses. We determined, however, that the claims center management's written instructions to the regional office staff did not include instructions to contact the claims center for employers' responses. In fact, regional office staff explained to us that they were not told to contact the claims center in order to obtain responses. During our discussion with a claims

¹⁴ This individual left the department in 2014 and a new Director was named.

center supervisor, we were told that another regional office received the employers' responses when they received the claims for adjudication. Based on our testwork and our discussions with that region's staff, the office did not routinely receive the employers' responses.

- Claims center management did not provide adequate supervision over the Adjudication Manager and either knew or should have known about the changes in the established eligibility determination process, specifically related to how employers' responses were handled, but took no actions to determine the effect or appropriateness of the process changes.

B. In gaining our understanding of the eligibility process, claims center management and supervisors over staff were either unable or unwilling to provide complete information about how employers' responses were handled or to provide a sufficient description of the entire eligibility process. As a result, we had to conduct multiple interviews and had to re-perform audit testwork each time management provided new information or changed the description of the process. For example, as noted in the background above, we asked the Adjudication Manager for all employers' responses that were in process as of December 2, 2013, the date we visited the claims center. After searching in office drawers and filing cabinets, we found employers' responses that had been received in August and October 2013 that had not yet been worked or even assigned to adjudicators for evaluation. When we asked the Adjudication Manager why he did not inform us of these employers' responses, he stated the following:

- August 2013 employers' responses: all related claims had been processed, and the employers' responses were most likely waiting to be filed; and
- October 2013 employers' responses: responses were related to pending claims waiting to be assigned to adjudicators and were therefore not yet needed by staff.

We later determined, based on our testwork, that the Adjudication Manager's previous explanations to us regarding the status of the August and October employers' responses were inaccurate, as described below:

- for the August 2013 employers' responses, multiple claims were still in a pending status on December 2, 2013, which means the employers' responses had not been evaluated; and
- for the October 2013 employers' responses, multiple claims were not in a pending status on December 2, 2013, but had already been processed and paid to the claimants without considering employers' responses.

C. We haphazardly selected a nonstatistical sample of employers' responses from the claims center but were unable to determine the population of employers' responses. We determined that division staff had approved and processed the claims without properly considering (possibly because they were unaware the responses existed) employers' responses that were on hand in the claims center. The details are described as follows:

- from our review of the employers' responses dated August 2013, we found that 4 of 21 claims (19%) were approved without proper evaluation of the employers' responses (see example below); and
- from our review of the employer responses dated October 2013, we found that 27 of 58 claims (47%) were approved without proper evaluation of the respective employers' responses.

One example of an employer's response disputing the claimant's assertion of lack of work is exhibited below. Claims center staff approved and paid the respective claim without consideration of the employer's timely response.

TENNESSEE DEPARTMENT OF LABOR AND WORKFORCE DEVELOPMENT
DIVISION OF EMPLOYMENT SECURITY
1/1 CLAIMS CENTER
P.O. BOX 280870
NASHVILLE, TN 37228

TIME SENSITIVE REQUEST FOR SEPARATION INFORMATION

SSN: [REDACTED]
BYE: 08/16/2014

CLAIM EFFECTIVE DATE: 08/19/2013
DATE MAILED: 08/20/2013
RESPONSE DUE DATE: 08/27/2013

THE CLAIMANT STATES:
HE/SHE WAS LAID OFF DUE TO A LACK OF WORK.

If the reason for separation is different, please explain on the back of this form.

DATES OF EMPLOYMENT (BEGIN DATE) 8/1/07 (END DATE) 07/10/2013 *Current*

What are the total wages earned by the claimant between the dates begin work date and end work date?
\$ 154,384.53

1. Explain why the claimant is no longer employed, or indicate if and what additional information on the claim will be faxed or emailed to the state, or enter additional information relevant to the claim.
Still employed

[REDACTED] 8/23/13 [REDACTED]
Signature & Title Date Phone Number

ELW40 PAGE 2 001086

After examining the sample above, we expanded our testwork and found 21 other employers' responses from August 2013 and September 2013 in which the employers disagreed with the claimants' assertions of lack of work, yet the associated claims were approved without further evaluation of the employers' statements.

Claims center management could not adequately explain why the employers' responses were not properly evaluated.

According to division management, they implemented a document management system in February 2014 and all employer responses are now imaged and stored in the system to assist staff in the evaluation of claims.

Criteria

Section 5116 of the *Unemployment Insurance, UI Manual, Procedures When Employer Responds Timely to Time Sensitive Request for Separation Information*, states:

A. Employer Submits a Written Statement

Give the employer's written statement full consideration in making the determination. Make a decision based on the employer's written statement and the fact-finding interview with the claimant and supporting documentation.

According to Section 50-7-304(b)(2)(C), *Tennessee Code Annotated*,

Employer Response to Request for Separation Information. If a separation issue exists, the separating employer will be asked to supply information describing circumstances leading to the separation. The information must be received by the agency within seven (7) days from the date the agency request for information is mailed to the separating employer. In the absence of the response, the decision of entitlement will be based on the claimant's statement and other information available to the agency. The separating employer may supply information to the agency prior to a request for information being mailed from the agency if the employer expects a separation issue to arise with regard to an employee.

Documentation for Eligibility Determinations

According to Part 6, Compliance Supplement, of the Office of Management and Budget Circular A-133, the department must have sufficient controls "to provide reasonable assurance that only eligible individuals . . . receive assistance under Federal award programs."

Cause

The division improperly approved and paid UI benefit claims when it failed to consider critical eligibility information provided through the employers' responses. After abandoning their document storage system in fiscal year 2013, claims center management relied on a manual system for matching lack-of-work statements from claimants to responses from employers. Based on division management's statements, they did not become involved in the new manual process and did not know the details of the process. The manager and other staff began to assign lists of claims to be worked to regional offices without sending the corresponding employer responses along with the assignments. Furthermore, claims center management did not ensure that all claims were properly re-coded in the department's information system after contradictory statements were received from employers. Had these claims been properly re-coded, staff—both

at regional offices and the Nashville Claims Center—would have been able to determine whether employers’ responses had been received so that determinations would not be made based solely on the claimants’ lack-of-work statements. The division’s failure to properly determine eligibility and properly process these claims may have been affected by pressure to alleviate the backlog of pending claims.

Effect

When employers’ responses are disregarded by claims center management, the department may pay benefits to ineligible claimants. Furthermore, employers may be negatively affected by unnecessary increases in their unemployment tax premiums.

Known Questioned Costs

Because management could not provide proper documentation of eligibility of the claimants identified in our testwork for claims dated August 2013 through October 2013, we have questioned costs for the net amount of benefit payments, less any overpayments that were established. See table for results.

IMPROPER CLAIM DETERMINATIONS

	Federal Funds	State UI Trust Funds	Total
Total UI Benefits Issued	\$6,334	\$121,835	\$128,169
Total Overpayments Established	\$2,447	\$8,765	\$11,212
Net Questioned Costs*	\$3,887	\$113,070	\$116,957

*The “Net Questioned Costs” was calculated by “Total UI Benefits Issued” less “Total Overpayments Established.”

Recommendation

Top management should evaluate the conditions noted above, including actions of claims center management and staff, and statements made to auditors. Claims center management should ensure that clear policies and procedures are developed and implemented for processing lack-of-work claims. These policies should ensure that employers’ responses are matched to claims and forwarded to the appropriate staff. Claims center management should also ensure that claims for which employers’ responses have been received are appropriately re-coded in the department’s information system. Finally, department management should ensure that changes in critical processes are tested and approved before implementation.

Management's Comment

We concur in part.

As previously stated and noted in the prior *Single Audit Report*, the department struggled with an inadequate case management system. When the system completely failed, a manual and paper centric operation process was the only available alternative.

The claims pulled by the auditors were from August and October 2013, at the time that the claims center was operating with a manual system of matching documentation with other claims material to send to adjudication. It should be noted that employer responses were being received in several different ways including:

- the State Information Data Exchange System (SIDES),
- fax (to individual employees or to a general proxy),
- email (to individual employees or to a general proxy), and
- mail.

All these employer responses had to be in printed format to be matched with other claims documents. The entire process was subject to human error at many levels and was compounded by the volume of claims being processed.

There were four of 21 claims dated August 2013 noted by the auditors as being approved without proper evaluation of the employers' responses.

- The department agrees on three of the four claims; while one of the three employers filed an appeal and the decision was reversed.
- The fourth claim was verified via phone with the employer by a claims agent.

There were 27 of 58 claims dated October 2013 noted by the auditors as being approved without proper evaluation of the employers' responses.

- The department agrees on 21 of the 27 claims noted but also notes:
 - Four of the 21 were corrected by adjudication, when additional information was provided.
 - Eight of the 21 were appealed by the employers (six decisions were reversed and two were upheld).
- The other six claims were reviewed and the employers' information was considered before approving.

It must be noted that an employer's response (including the example provided in the finding) may be reviewed and considered, but is not the only determining factor in approving or denying a claim.

In December 2013, an in-house imaging center was established that utilizes existing scanning capabilities to digitize and maintain scanned claims material in a repository readily accessible to adjudicators on their desktop computers. By March 2014, adjudicators began using the repository of claims materials. Both agents and adjudicators have access to the repository to verify whether all documentation has been received.

The department categorically denies that employers' responses were being disregarded by claims center management. Processes and procedures have been reviewed and improved, since this review.

Auditor's Comment

Section 50-7-304(b)(2)(C), *Tennessee Code Annotated*, requires the department to seek and take into account information from separating employers describing the circumstances leading to the separation to ensure all claimants are eligible before receiving benefits.

Finding Number	2014-043
CFDA Number	17.225
Program Name	Unemployment Insurance
Federal Agency	Department of Labor
State Agency	Department of Labor and Workforce Development
Grant/Contract No.	ES-23025-12-55-A-47; ES-24646-13-55-A-47; UI-19610-10-55-A-47; UI-21127-11-55-A-47; UI-22341-12-55-A-47; UI-23919-13-55-A-47; UI-25232-14-55-A-47; EUC, Fed EB, UCFE, and UCX; FAC Benefits & UI Admin; and TUC-State Expenditures
Federal Award Year	2010 through 2014
Finding Type	Significant Deficiency and Noncompliance
Compliance Requirement	Eligibility
Questioned Costs	\$20,588
Repeat Finding	2013-029

The Employment Security Division’s key control for detecting fraudulent claims was ineffective, and staff did not identify ineligible payments to state employees, deceased individuals, state inmates, and unverified individuals

Background

The Employment Security Division (the division) in the Department of Labor and Workforce Development is charged with the administration of the Unemployment Insurance (UI) program and is responsible for determining eligibility and disqualification provisions, as required by Tennessee Employment Security laws and regulations. The division staff, in coordination with the department’s Information Technology Division, perform data cross-matches by comparing data in the UI benefits information system to data obtained from third parties. Cross-matches of data are intended to provide independent verification of the information provided by claimants. For example, Employment Security Division staff compare UI benefit recipients to state payroll records to ensure that active state employees are not receiving UI benefits. Division staff also perform other cross-matches, which include comparing UI benefit recipients with the following data: deceased individuals (vital statistics), new hires for Tennessee and national employers, incarcerated individuals, and individuals’ identity information (name, social security number, or date of birth) with the Social Security Administration. Once they identify possible ineligible recipients, staff must then further investigate the cross-match results in order to determine if the benefit recipients are ineligible. For recipients found to be ineligible, staff stop any future benefit payments and establish overpayments.

Division staff use cross-matches as primary controls to detect potential overpayments due to fraud or errors. In order for staff to use the cross-matches as an effective control, the cross-matches must be programmed correctly, properly reviewed, and acted on timely in order to determine if an overpayment has occurred or if no further action is required.

In the *Single Audit Report* for 2012 and 2013, we noted deficiencies with the division’s cross-matches. Our findings reported that the division’s cross-matches had not identified individuals receiving UI benefits who were simultaneously employed by the state, deceased, or incarcerated.

We also noted that the cross-match to validate individuals' identities through the Social Security Administration was not always effective, resulting in payments to unverified individuals. Department management concurred with the deficiencies noted in the 2012 *Single Audit Report* and concurred in part with the weakness noted in the 2013 *Single Audit Report*. Specifically, department management did not concur with the 2013 *Single Audit Report* that all of those individuals identified on their cross-match were necessarily ineligible, since they had not investigated those individuals' claims.

Condition

In order to determine if the Department of Labor and Workforce Development's cross-matches and identity verification process were effective, we performed our own cross-matches and analytical procedures by comparing the population of UI benefit recipients to populations of state employees, deceased individuals, and state inmates. In addition, when we performed a query of the department's information system for individuals who received benefits during the audit period July 1, 2013, through June 30, 2014, we found the Employment Security Division had not verified identities of all benefit recipients before they received UI benefits.

A. State Employees

As stated in the 2012 and 2013 *Single Audit Report*, we found that the division's state employee cross-match was not effective since it did not identify all active state employees who received UI benefits. Our cross-match identified 24 instances where division staff did not properly establish UI benefit overpayments to state employees when those employees failed to fully report their wages while also receiving UI benefits. The potential overpayments totaled \$14,536. Specifically, we found the division's staff did not

- detect 10 state employees who received UI benefits throughout the audit period;
- properly follow up on 11 cross-match results to determine whether state employees identified were eligible for UI benefits and, if necessary, stop further benefit payments and establish overpayments; and
- properly calculate and establish overpayments for 3 state employees determined ineligible.

B. Vital Statistics

As stated in the 2012 and 2013 *Single Audit Report*, we found that the division's vital statistics cross-match failed to identify deceased individuals. Our cross-match identified one instance where UI benefits were paid after the individual's date of death. The potential overpayment totaled \$825.

C. State Inmates

As stated in the 2013 *Single Audit Report*, we found that the division's state inmate cross-match was not sufficiently designed to include all incarcerated individuals. Our cross-match identified

44 instances where the department did not properly establish overpayments for state inmates who received UI benefits while incarcerated. The potential overpayments totaled \$50,778. Specifically, we found that division staff did not

- detect 41 state inmates who received UI benefits throughout the audit period;
- properly follow up cross-match results on 1 state inmate to determine eligibility and, if necessary, stop further benefit payments and establish an overpayment; and
- properly calculate and establish overpayments for 2 ineligible inmates.

D. Identity Verification

As stated in the 2012 and 2013 *Single Audit Report*, we found that the division's identity verification procedures were not always effective. Our cross-match identified 31 individuals who received UI benefits even though division staff had not verified the individuals' identities through the Social Security Administration as required. Based on the analytical procedures performed, we determined that the potential overpayments totaled \$18,851.

In addition, we identified 16 other individuals that were approved for benefits even though the division had failed to verify their identities. While these individuals were improperly approved for benefits, they did not receive any improper benefits, since the division subsequently verified their identities or canceled any pending benefit payments of these individuals.

Criteria

The Department of Labor and Workforce Development is responsible for determining eligibility and disqualification provisions of individuals according to Tennessee Employment Security laws and regulations.

A. State Employees

Section 50-7-211(a), *Tennessee Code Annotated*, states:

An individual shall be deemed "unemployed" in any week during which the individual performs no services and with respect to which no wages are payable to the individual, or in any week of less than full-time work if the wages payable to the individual with respect to the week are less than the individual's weekly benefit amount.

B. Vital Statistics

Section 50-7-302(a), *Tennessee Code Annotated*, states:

An unemployment claimant shall be eligible to receive benefits with respect to any week only if . . . the claimant is able to work, available for work, and making a reasonable effort to secure work.

C. State Inmates

Section 50-7-302(a)(4)(F), *Tennessee Code Annotated*, states:

A claimant shall be considered ineligible for benefits if the claimant is incarcerated four (4) or more days in any week for which unemployment benefits are being claimed.

D. Identity Verification

Section 4-58-103(a), *Tennessee Code Annotated*, states:

Except where prohibited by federal law, every state governmental entity and local health department shall verify that each applicant eighteen (18) years of age or older, who applies for a federal, state or local public benefit from the entity or local health department, is a United States citizen or lawfully present in the United States in the manner provided in this chapter.

Section 1137(a)(1) of the *Social Security Act* states:

The State shall require, as a condition of an individual's eligibility for benefits . . . that each applicant for or recipient of benefits under that program furnish to the State his social security account number (or numbers, if he has more than one such number), and the State shall utilize such account numbers in the administration of that program so as to enable the association of the records pertaining to the applicant or recipient with his account number.

Cause

The Division of Employment Security's cross-matches were ineffective due to continuing flaws in program logic, staff's failure to follow up on cross-match results, issue timely agency decisions, and correctly calculate overpayments. Based on our discussions with Department of Health staff, the division's vital statistics cross-match failed to identify the deceased individual in question because the data records received from the Department of Health's Office of Vital Statistics do not include deaths with a particular cause-of-death code. The division's state inmate cross-match failed to identify state inmates because the data received from the Tennessee Department of Correction does not include state inmates housed at county-owned facilities. According to management, the state inmate cross-match was corrected in June 2014. Department management stated that its planned corrective action of the identity verification issue is contingent upon implementation of its new UI system scheduled for completion in 2016.

Effect

When the Department of Labor and Workforce Development continues to perform cross-matches that do not include necessary program logic and information, the risk increases that UI benefits

will be paid to ineligible individuals, including state employees, deceased individuals, state inmates, and those who may have committed identity theft or are in the country illegally.

Known Questioned Costs

Based on our testwork noted above, we identified known questioned costs for UI benefits paid to ineligible individuals. See the results in the table below.

BENEFITS PAID TO INELIGIBLE INDIVIDUALS

Category (# of Matches Requiring Follow-up)	State UI Trust Funds	Federal Funds	Total Ineligible Payments
State Employee (24)	\$11,086	\$3,450	\$14,536
Deceased (1)	\$825	-	\$825
Incarcerated (44)	\$33,640	\$17,138	\$50,778
Identity Verification (31)	\$18,851	-	\$18,851
Total (100)	\$64,402	\$20,588	\$84,990

Recommendation

The Commissioner of the Department of Labor and Workforce Development and the Employment Security Administrator should ensure that the cross-matches are properly designed to ensure UI benefits are only issued to eligible individuals. Additionally, management should determine the reliability, completeness, and accuracy of the third-party agencies’ cross-match data and whether the cross-matches provide effective controls to identify when the Employment Security Division issues benefit payments to potentially ineligible individuals.

Division management should ensure policies and procedures are in place to conduct proper reviews of the cross-match results. Furthermore, management should ensure staff perform prompt follow-up investigations, issue agency decisions, and establish accurate overpayments when necessary.

Division management should also implement procedures to ensure that no individuals receive benefits before their identities are verified.

Management’s Comment

We concur in part.

The department does not concur that all cited claims are overpayments. Cross matches are simply indicators of possible overpayments. Each possible overpayment must be fully investigated, and if warranted, an overpayment established.

Updates on the cross-matches noted in the audit are as follows:

- The state employee cross-match had 24 noted cases. After being reviewed by the department, three (3) of these noted cases were determined not to be overpayments. For the remaining 21 noted cases, the department has established \$21,333 in overpayments.
- An overpayment has also been investigated and established on the one Vital Statistics cross-match case. It should also be noted that this single case was not included in any cross-match file received from Vital Statistics. This was verified by both the department and the state auditors.
- The incarcerated cross-match results were based completely on a different file than the one currently received from the Department of Correction. A weekly cross-match was evaluated and began production as of June 10, 2014. The department did review the list of incarcerated claimants provided by the auditors. Eight (8) of the 44 noted cases were not incarcerated during the times listed. For the remaining 36 noted cases, the department has established \$63,892.00 in overpayments.

There were 31 individuals noted in the audit as receiving UI benefits without the required Social Security Administration identity verification.

- Twenty-one (21) of these were on “drop-sheets,” but due to the claims backlog, the drop sheet was not worked immediately. When they were worked, the claims were stopped. Overpayments are being processed for these claims.
- The other ten (10) claims were originally denied, due to failure to provide proof of ID; but subsequently, an add or re-open claim was filed. Notices are being sent to these for proof of ID. If not provided, overpayments will be processed.
- Auditors also noted that another 16 individuals filed claims that were initially approved but did not receive any UI benefits, because the department subsequently denied the claims for failure to produce proof of identity before any benefits were paid.

The department has reassigned the review of cross-match results and centralized several of these within the Nashville office. They are assigned to specific auditors, instead of distributed to all auditors, and are completed timely.

It should also be noted that the Benefit Payment Control Unit is now up-to-date on reviewing all cross-match reports.

As stated in other findings, the department continues to pursue replacement of existing systems. Even though the mainframe will be the primary system impacted, this replacement would also include the FoxPro database that maintains most of the cross-match indications. The FoxPro database will be replaced by SAS (a predictive statistical package). In November 2012, the department initiated the process with the Central Procurement Office to purchase SAS in assisting with identifying fraud. The purchase was approved in November 2014, and implementation of the new package is expected by May 2015.

In January 2015, the State of Tennessee received the federal Final Determination regarding the findings contained in the *2013 Single Audit Report*. The federal Final Determination indicated the noted issues were corrected.

Auditor's Comment

As evidenced by our audit results, management's cross-matches did not detect all potentially ineligible claimants.

We asked management on December 2, 2014, and January 9, 2015, for all documentation to resolve questionable issues with the cases noted in our cross-match results; however, management did not provide documentation at the time of the audit.

We will evaluate the impact of management's new cross-match procedures (effective June 10, 2014, for incarcerated) during the next audit.

Finally, the U.S. Department of Labor issued its Final Determination of Tennessee Department of Labor and Workforce Development's *2013 Single Audit* findings based on the department's submission of documentation and correspondence relevant to correct any unresolved or pending issues from that audit. The U.S. Department of Labor has notified the department that its submission of corrective actions was accepted and will be monitored to ensure effective implementation. Based on our *2014 Single Audit* of the Tennessee Department of Labor and Workforce Development, management has not fully implemented corrective action as noted in the finding above.

Finding Number	2014-044
CFDA Number	17.225
Program Name	Unemployment Insurance
Federal Agency	Department of Labor
State Agency	Department of Labor and Workforce Development
Grant/Contract No.	ES-23025-12-55-A-47; ES-24646-13-55-A-47; UI-19610-10-55-A-47; UI-21127-11-55-A-47; UI-22341-12-55-A-47; UI-23919-13-55-A-47; UI-25232-14-55-A-47; EUC, Fed EB, UCFE, and UCX; FAC Benefits & UI Admin; and TUC-State Expenditures
Federal Award Year	2010 through 2014
Finding Type	Significant Deficiency, Material Weakness, and Noncompliance
Compliance Requirement	Eligibility - Significant Deficiency and Noncompliance Reporting - Significant Deficiency and Noncompliance Special Tests and Provisions - Material Weakness and Noncompliance
Questioned Costs	N/A
Repeat Finding	2013-028

Delays in processing claims and establishing overpayments led to backlogs

Background

The purpose of the Unemployment Insurance (UI) program is to provide economic security to workers during times of unemployment, according to the Tennessee Employment Security Law, *Tennessee Code Annotated*, Title 50, Chapter 7. The Department of Labor and Workforce Development's Employment Security Division operates the UI program to provide benefits for employees who become separated from their employment through no fault of their own.

In general, claimants file initial unemployment claims online or over the telephone. While some claims may be filed online, other claims cannot be processed without claims center representatives working directly with claimants and employers. Much of this interaction occurs through telephone calls to the claims center. The claims center's interviewers are responsible for answering phone calls and obtaining information regarding initial claims. Telephone calls received by the claims center are routed to the next available interviewer. These same interviewers are also responsible for fielding questions from employers regarding benefit issues; following up with questions from claimants for claims already filed; and assisting claimants who have been approved but need assistance with their weekly certifications.

While division staff are able to approve some claims quickly, other claims that involve employee separation and personal eligibility issues require the division interviewers to obtain more detailed information from the claimant and often the affected employer. After interviewers have collected information regarding the claimants' separation and personal eligibility, they transfer the claims and additional information to staff known as "adjudicators," who review and perform additional procedures as needed to determine claimant eligibility. Claims that require evaluation by adjudicators are placed in a collection of pending claims and should not be paid until the information is obtained and evaluated by an adjudicator. Once eligibility determinations are

made, adjudicators record their eligibility decisions (approvals and denials) in the division's Employment Security Combined Online Technology (ESCOT) system. In addition to the adjudicators' review of initial pending claims, the adjudicators also review eligibility of existing beneficiaries when the division receives new information from other state departments, claimants, or employers indicating that eligibility status may have changed. The division's staff place the current beneficiaries' unemployment claims in a pending status until the new information can be considered by an adjudicator.

When division staff determine that benefits may have been paid to ineligible claimants, the Benefit Payment Control (BPC) staff perform additional procedures to review the circumstances before establishing an overpayment in the accounting system. Specifically, BPC unit staff are responsible for detecting potential overpayments, investigating potential overpayments by obtaining additional claimant and employer statements and information, and then deciding whether an overpayment occurred. BPC staff also determine whether the overpayment was a result of error by the department or the claimant—and in some cases, whether the overpayment was the result of fraud on the part of the claimant—and record the overpayment in the ESCOT system. The BPC unit uses multiple data matches to detect possible overpayments by comparing data from ESCOT with third-party information. These data matches are intended to provide an independent verification of the information provided by claimants or in some cases to identify information not disclosed by the claimants (such as wages earned). Once BPC determines that a potential overpayment has occurred, the potential overpayment is logged as a pending case until a final eligibility determination can be made. Generally, the division continues to pay claims with potential overpayments until claimants are determined to be ineligible.

For both the 2012 and 2013 *Single Audit Report*, we noted that delays in processing claims and establishing overpayments led to backlogs in these areas. In March 2014, management's response to the prior-year audit finding included plans for improvements to claims processing. The department made a change to its Interactive Voice Response System by adding new self-service options for claimants. This system now allows claimants to perform simple functions and thereby reduce calls to the claims center staff. The department has also implemented a customer service option on its website that allows claimants to notify the division of issues with their UI benefits. According to management, this service is expected to reduce the number of calls to the claims center. Management responded that it had filled vacant adjudicator positions, approved staff overtime, and implemented a new document storage system to assist with the backlog of pending claims. Management also responded that BPC staff were tasked to eliminate duplicate potential overpayment cases (multiple benefit payments to the same claimant) into single cases, establish new procedures for assigning cases, and seek an evaluation and advice from the U.S. Department of Labor regional office in order to reduce the potential overpayment case backlog.

Condition

Based on our review of the claims process, we found that the Employment Security Division continued to experience backlogs for the intake and processing of claims for benefits, as well as for investigating potential benefit overpayments. For the third consecutive year, the division was unable to handle the intake of telephone calls or to timely process the benefit claims that required

staff interactions. For the second consecutive year, the division experienced delays investigating potential overpayments. Although there were approximately 254,000 claims filed during fiscal year 2014 compared to approximately 311,000 filed in fiscal year 2013, the division still experienced backlogs and delays in these areas as described below:

A. The division did not answer the majority of incoming telephone calls.

- The division's claims center answered only 2%¹⁵ of incoming telephone calls requiring live interaction with staff. In response to the prior audit finding, department management stated it had expanded self-service telephone options. Based on call statistics provided by the division, incoming calls directed to self-service increased by 568%¹⁶ during fiscal year 2014. As a result of callers' access to the expanded self-service option, along with a reduction in claimants pursuing UI benefits, the department experienced approximately 3.6 million fewer incoming calls directed to the division's claims center staff. Even with the reduction in the number of incoming calls, however, we found that staff actually answered approximately 91,000¹⁷ fewer calls during fiscal year 2014 than in fiscal year 2013, resulting in approximately 98% of calls not being connected to a claims center representative.
- The department's response to the Office of the Comptroller of the Treasury's *Six Month Follow-up* from the *2013 Single Audit Report* stated that call volume decreased from over 800,000 calls in January 2014 to less than 200,000 in August 2014. Similarly, management reported in June 2014 to the joint legislative Fiscal Review Committee that the call volume had been reduced from over 800,000 calls in January 2014 to over 200,000 in May 2014. While we found management's statements for these two months were supported by internal claims center statistics, we also found that call volumes fluctuate throughout the year, possibly due to fluctuations in seasonal unemployment. Data provided by the department for fiscal year 2013 and fiscal year 2014 indicates that the highest numbers of calls are received in January and the lowest numbers of calls occur during summer months. See Table for results.
- During our audit fieldwork and subsequent to the audit period, we attempted 20 calls to the claims center at haphazard times, in order to reach a staff member. For 17 of 20 calls attempted (85%), we were neither placed on hold nor connected to a claims center representative. For 16 of these 17 calls, we received the following message: "We are unable to handle your call at this time due to extremely high call volume." For the other call, we received a message stating, "We are sorry you have reached a number that has

¹⁵ According to the claims center statistics provided by the division, the claims center received 5,126,764 incoming calls during fiscal year 2014. Of the 5,126,764 incoming calls, 1,735,720 incoming calls were directed to self-service. The department received 3,391,044 incoming calls requiring live interaction (5,126,764 incoming calls less 1,735,720 incoming calls directed to self-service). The department answered 73,712 of the 3,391,044 incoming calls requiring live interaction (approximately 2%).

¹⁶ According to the claims center statistics provided by the division, 260,000 incoming calls were directed to self-service during fiscal year 2013, and 1,735,720 incoming calls were directed to self-service during fiscal year 2014, an increase of 568%.

¹⁷ According to the claims center statistics provided by the division, the department answered 164,800 incoming calls during fiscal year 2013 and answered 73,712 incoming calls during fiscal year 2014.

been disconnected or no longer in service. If you feel that you have reached this number in error, please hang up and try your call again.”

MONTHLY CLAIMS CENTER STATISTICS (unaudited)

Month ¹⁸	Incoming Calls	Calls Directed to Self Service	Calls Directed to Claims Center	Calls Answered by Claims Center Staff	% of Calls Directed to the Claims Center That Were Answered	Average Wait Time (Minutes)
January 2013	1,600,000	3,500	1,596,500	9,300	0.6%	61
June 2013	187,000	77,000	110,000	16,000	14.5%	55
July 2013	499,088	154,329	344,759	11,194	3.3%	60
August 2013	430,331	151,511	278,820	9,999	3.6%	50
September 2013	372,990	145,425	227,565	9,434	4.2%	47
October 2013	473,612	139,013	334,599	8,776	2.6%	56
November 2013	364,816	120,224	244,592	5,642	2.3%	51
December 2013	648,401	156,859	491,542	4,006	0.8%	73
January 2014	803,786	208,000	595,786	5,013	0.8%	41
February 2014	402,184	177,684	224,500	2,965	1.3%	42
March 2014	299,948	135,739	164,209	3,816	2.3%	30
April 2014	298,955	128,616	170,339	4,991	2.9%	30
May 2014	248,929	107,152	141,777	4,077	2.9%	52
June 2014	283,724	111,168	172,556	3,799	2.2%	58

Source: Employment Security Division management.

B. Division management and staff did not address the significant backlog of pending claims for UI benefits during the audit period. Pending claims are those claims that must go through the department’s adjudication process which requires UI division staff to obtain statements and/or documentation from both the claimant and separating employer prior to making a decision on claimants’ eligibility.

- Based on a review of the division’s pending claim reports, the backlog of pending claims, which totaled 15,489 on June 30, 2013, increased to over 20,000 in the winter of 2014 and then decreased to 11,899 at June 30, 2014. Based on our inquiry and review of pending claims reports, it took approximately 8 weeks for staff to process pending claims throughout the audit period. During our audit fieldwork, we found that division staff continued to reduce the pending claims backlog to approximately 4,000 claims by the end of November 2014. While we recognize the division has made improvements, full corrective action has not been achieved, and we have reported material weaknesses in the division’s processing of claims. (See findings 2014-039 and 2014-042.)

¹⁸ Statistics for January 2013 and June 2013 are shown to illustrate the trend of higher incoming calls during winter months and lower incoming calls during summer months.

C. The Benefit Payment Control (BPC) unit¹⁹ did not address the significant backlog of potential overpayments awaiting investigation.

- As of June 30, 2014, the BPC unit staff estimated the backlog to be approximately 16,000 potential overpayment cases, a reduction from the approximately 37,000 cases at June 30, 2013; however, according to BPC management, this reduction was primarily achieved when staff identified and eliminated “duplicate”²⁰ cases.
- The department reports its overpayments to the U.S. Department of Labor quarterly through the Employment and Training Administration (ETA) 227 Overpayment Detection and Recovery Activities report. ETA uses the information provided in the report to monitor the integrity of the benefit payment processes. The U.S. Department of Labor reporting instructions require only those overpayments established by the department to be reported on the ETA 227 report. We found that the department accurately reported the overpayments established and recorded in ESCOT on the ETA 227 report; however, the backlog of approximately 16,000 potential overpayment cases awaiting investigation by the BPC unit were not included on the ETA 227 report.

Criteria

A and B: Section 303(a)(1) of the Social Security Act states that the department must have “such methods of administration . . . as are found by the Secretary of Labor to be reasonably calculated to insure full payment of unemployment compensation when due.”

According to the *Code of Federal Regulations*, Title 20, Section 640, the department should issue the first benefit payment for eligible claims within 14 days of the first compensable week.²¹

C: According Part 6, Compliance Supplement, of the Office of Management and Budget Circular No. A-133, the department must have sufficient controls “to provide reasonable assurance that only eligible individuals . . . receive assistance under Federal award programs.”

Department of Finance and Administration Policy 23, “Accounts Receivable – Recording, Collection, and Write-Offs,” requires state agencies to “make a reasonable effort to collect all receivables on a systematic and periodic basis.”

UI Reports Handbook No. 401, ETA 227, “Overpayment Detection and Recovery Activities,” Part B. Purpose, states:

¹⁹ The Benefit Payment Control unit is a unit within the Employment Security Division responsible for the prevention, detection, and establishment of benefit overpayments.

²⁰ These duplicate cases were a result of multiple overpayments to the same claimants that occurred since the BPC staff could not investigate the cases quickly enough to prevent issuing multiple overpayments to an ineligible claimant.

²¹ Section 50-7-302(a)(5)(A), *Tennessee Code Annotated*, requires a mandatory “waiting week” for which claimants do not receive unemployment benefits. Therefore, in Tennessee the standard is 21 days following the beginning of a claimant’s eligibility (7 day waiting week + 14 days following first compensable week).

The state agency's accomplishments in principal detection areas of benefit payment control are shown on the ETA 227 report. The Employment and Training Administration (ETA) and state agencies need such information to monitor the integrity of the benefit payment processes in the UI system.

Cause

A: Management reduced the number of staff available to answer calls. According to division management, some claims center staff who were previously answering incoming telephone calls were reassigned to assist with the new functions designed to alleviate the number of telephone calls.

B and C: Because the department did not allocate sufficient resources to ensure timely adjudication of pending claims and timely investigation of potential overpayments, backlogs have accumulated over the past several years.

Effect

The inability to answer incoming telephone calls or to process UI claims timely affects the department's mission to provide unemployment benefits to those in need. In addition, delays in investigating overpayments lessen management's ability to recoup overpaid benefits and threaten the integrity and financial viability of the UI program. The backlog of overpayment cases are not included on the ETA 227 report; therefore, the information that the department reported to the U.S. Department of Labor does not provide a complete picture of the amount overpaid, number of claimants overpaid, and whether the overpaid amount was due to error or fraud. As a result, the U.S. Department of Labor may not fully assess the integrity of the department's benefit payment process.

Recommendation

The Commissioner and Employment Security Division Administrator should assess staffing levels at the claims center and ensure that claimants who file their UI claims by telephone are able to do so promptly. Furthermore, management should determine appropriate staffing levels and training needs to support the adjudication process to ensure that the division is able to properly and timely process unemployment claims. Management should also ensure that the BPC unit has adequate resources to investigate and, where appropriate, establish overpayments so that department staff perform overpayment collection timely and report complete data to the federal grantor.

Management's Comment

We concur in part.

As previously stated, improved technology will significantly improve operations efficiency. Implementation of the new UI benefits system has begun and is on-schedule to be completed by mid-2016. Staffing is continually being evaluated and positions filled as funding permits.

Steps taken to reduce / manage call volume include the following:

- The Interactive Voice Response (IVR) was modified in March 2013 by moving self-help options to the beginning of the call, which allowed more claimants to help themselves.
- A new Telephone Information Processing System (TIPS) line was deployed in February 2014 that allows claimants to reset their personal identification number (PIN) and to correct incorrect response to the weekly certification questions.
- A claims status tracker was implemented and utilized by claimants 182,211 times between July and December 2014.
- A new helpdesk ticketing application, ZenDesk, was implemented in March 2014. This application works to reduce the number of phone calls and allows staff to track issues without duplication of work and measures staff's effectiveness and efficiency in answering those issues. Also, this application provides for a self-help knowledge base. To date over 100,000 tickets have been created by over 56,000 claimants. Customer satisfaction remains over 80% through this helpdesk.

Division management addressed the significant backlog of pending claims for UI benefits during the audit period with the following:

- As noted in the prior *Single Audit Report*, the department struggled with an inadequate case management system. When the system completely failed, a manual and paper centric operation process was the only available alternative. In December 2013 an in-house imaging center was established that utilizes existing scanning capabilities to digitize and maintain scanned claims material in a repository readily accessible to adjudicators on their desktop computers. In 2014, over 3.57 million individual pieces of paper were digitized, which transitioned the paper centric process to paperless.
- By March 2014, adjudicators began using the repository of claims materials. Both agents and adjudicators have access to the repository to verify whether all documentation has been received.
- In January 2014, the backlog of claims over 21 days awaiting decisions peaked at 12,375 claims.
- By October 1, 2014, the backlog was cleared.
- The department also exceeded the US Department of Labor's first pay timeliness requirement of 87% for October 2014 and has met the standard for every succeeding month since October 2014.
- From October 2014 through January 2015, the department processed from 90.3% to 95.5% of all initial claims within the 21-day timeliness requirement.

The BPC unit addressed the significant backlog of potential overpayments with the following:

- A Lean Event conducted in February 2014 resulted in a plan to eliminate the backlog. At that time, the backlog consisted of 40,869 cases pending review.

- Vacant auditor positions were filled and overtime was authorized to address these cases.
- The backlog of benefit payment control cases has been reduced from 40,869 in February 2014, to 363 cases as of February 14, 2015. The backlog will be cleared by March 30, 2015.
- Over \$31 million in overpayments have been set up, during the clearing of the BPC backlog.
- BPC unit is current on all cross-match reports.
- The department is completing the ETA 227 report in accordance with the US DOL guidance.

The department acknowledges that it is unable to answer the volume of call attempts. However, it should be noted that:

- Since February 2014, TIPS line calls are included in the total call attempts. As of October 2014, due to program modifications needed for the online certification system, TIPS became the only certification method. So, calls are currently averaging 30,000 per week or 120,000 per month. In January 2015, we received a total of 276,000 calls of which approximately 120,000 were certification calls that do not require any assistance. For comparison January 2014, we recorded 803,000 calls, and in January 2015 we are now at 156,000.
- The department has determined that it is much more effective and efficient to handle ZenDesk tickets, as opposed to putting more claims agents on the phone. The agents are able to handle multiple requests for assistance at the same time. The customer satisfaction scores stay above 80% and the claim process times which are in excess of 90% timely are proof that this is working.
- The department will be testing the ZenDesk “voice over” feature in the next few weeks. The “voice over” feature will allow the caller to leave a voice message that converts to a ZenDesk ticket.

In January 2015, the State of Tennessee received the federal Final Determination regarding the findings contained in the *2013 Single Audit Report*. The federal Final Determination indicated the noted issues were corrected.

The department remains committed to serving our customers quickly, efficiently, and accurately.

Auditor’s Comment

The U.S. Department of Labor issued its Final Determination of Tennessee Department of Labor and Workforce Development’s *2013 Single Audit* findings based on the department’s submission of documentation and correspondence relevant to correct any unresolved or pending issues from that audit. The U.S. Department of Labor has notified the department that its submission of corrective actions was accepted and will be monitored to ensure effective implementation. Based on our *2014 Single Audit* of the Tennessee Department of Labor and Workforce

Development, management has not fully implemented corrective action as noted in the finding above.

Finding Number	2014-045
CFDA Number	17.225
Program Name	Unemployment Insurance
Federal Agency	Department of Labor
State Agency	Department of Labor and Workforce Development
Grant/Contract No.	ES-23025-12-55-A-47; ES-24646-13-55-A-47; UI-19610-10-55-A-47; UI-21127-11-55-A-47; UI-22341-12-55-A-47; UI-23919-13-55-A-47; UI-25232-14-55-A-47; EUC, Fed EB, UCFE, and UCX; FAC Benefits & UI Admin; and TUC-State Expenditures
Federal Award Year	2010 through 2014
Finding Type	Significant Deficiency and Noncompliance
Compliance Requirement	Reporting
Questioned Costs	N/A
Repeat Finding	N/A

Incorrect amounts entered in financial report

Background

For the Unemployment Insurance (UI) program, Fiscal Services staff from the Department of Finance and Administration (F&A) prepare the ETA²² 191 report. (Per executive order, the Department of Labor and Workforce Development [LWD] has an agreement with F&A that financial accounting and reporting functions of LWD will be managed and operated by F&A. This agreement includes F&A's completion of federal reporting for LWD.) The ETA 191 report, also known as the *Statement of Expenditures and Financial Adjustments of Federal Funds for Unemployment Compensation for Federal employees and Ex-Servicemembers*, reports federal funds used to pay unemployment compensation for federal employees (UCFE) and unemployment compensation for ex-servicemembers (UCX) benefits. Fiscal staff prepare the ETA 191 report on a quarterly basis and submit the report to the U.S. Department of Labor. Each federal and military agency is responsible for reimbursing the federal account for benefits paid to former employees based on what is reported.

ETA 191, Section A: Summary Statement of Expenditures and Adjustments, includes summary information of expenditures, as well as financial adjustments such as benefit payment cancellations and restorations of overpayments. These adjustments are classified as assigned or unassigned, depending on whether they have been credited to a specific federal or military agency.

ETA 191, Section B: Detailed Statement of Expenditures and Adjustments By Federal (Civilian) and Military Agencies, contains the specific benefit charges assigned to individual agencies and is the section of the report used by agencies to identify their specific charges to reimburse the federal account.

²² The Employment and Training Administration (ETA), which is part of the U.S. Department of Labor, administers the Unemployment Insurance program on the federal level.

Condition

The ETA 191 report submitted by fiscal staff for the period ending March 31, 2014, was not accurate and did not contain all pertinent information. Based on our testwork and review of supporting documents, we determined that fiscal staff:

- incorrectly entered data in Section A of the report for 14 of 16 line items tested (88%);
- incorrectly classified the same adjustments as both assigned and unassigned; and
- did not include an explanation for the unassigned adjustments in the report and did not maintain a record of when or if these unassigned charges had been assigned to specific agencies in the subsequent June 30, 2014, report.

The table below lists line items that were not accurately reported for both UCFE and UCX benefits:

<u>Line No. and Description</u>	<u>Description of Amounts Entered on the ETA 191 Report</u>
1. Benefit Expenditures	Only total UCFE and UCX UI benefits paid should have been reported; however, total unassigned adjustments were included in the totals.
2(a). Adjustments Assigned to Agencies - Cancellations	Only total assigned cancellations should have been reported; however, total unassigned cancellations were reported. These same amounts were reported on line 4(b) as unassigned, meaning this total was reported twice.
2(b). Adjustments Assigned to Agencies - Restoration of Overpayments	Only total assigned restorations should have been reported; however, total unassigned restorations were reported. These same amounts were reported on line 4(b) as unassigned, meaning this total was reported twice.
4(b). Expenditures and Adjustments Not Assigned to Agencies - Other - Explain in Comments	Only unassigned adjustments should have been reported; however, for both UCFE and UCX benefit payments, there were discrepancies between the UI expenditure amounts recorded in Edison, the state's accounting system, and the amounts recorded in LWD's Employment Security Combined Online Technology system (ESCOT). The discrepancies between Edison and ESCOT were added to the unassigned adjustment totals, without any comment explaining what these amounts included.
5. Total Expenditures and Adjustments Not Assigned to Agencies	Only unassigned adjustments should have been reported; however, discrepancies between UI expenditure amounts recorded in Edison and ESCOT were included in the totals, as noted for line 4(b) above.

6. Grand Total - All Expenditures and Adjustments	The Grand Totals were incorrect due to the errors noted in the lines above.
7. Comments	Line 7 should be used to identify and explain unassigned charges and adjustments from previous quarters that have been reclassified as assigned charges and adjustments. The comment entered by fiscal staff for line 7 only states, "For both lines 4B; corrections to expenditures to be made in second quarter 2014." We reviewed the subsequent ETA 191 report (June 30, 2014) and determined that there were no explanations on line 7 for whether any unassigned charges from the March 30, 2014, report had been assigned or reclassified.

Criteria

According to UI Reports Handbook No. 401, state agencies are responsible for paying UCFE and UCX benefits to the claimant and for reporting these quarterly benefit payments to the U.S. Department of Labor in a timely manner. Handbook No. 401 instructions for relevant line items are listed below:

<u>Line No. and Description</u>	<u>UI Reports Handbook No. 401 Reporting Instructions</u>
1. Benefit Expenditures	Include in the appropriate columns all UCFE and UCX unemployment compensation benefits paid to eligible (as based on title 5 U.S. Code) Federal civilian claimants and ex-servicepersons during the reported quarter.
2(a). Adjustments Assigned to Agencies - Cancellations	Enter in the appropriate UCFE or UCX columns the total amount of any checks canceled during the quarter which were reported as expenditures in prior quarters. Cancellations of checks drawn in the current quarter are to be reflected in Item 1. Check cancellations are subtracted when computing subtotals and totals.
2(b). Adjustments Assigned to Agencies - Restoration of Overpayments	Enter in the appropriate UCFE or UCX columns the total amount of restorations made during the current quarter of overpayments made in prior quarters. Restorations of overpayments received during the current quarter and based on expenditures in this current quarter should be reflected in item 1.
4(b). Expenditures and Adjustments Not Assigned to Agencies - Other - Explain in Comments	Enter the total for UCFE and the total UCX expenditures in the appropriate columns.
5. Total Expenditures and Adjustments Not Assigned to Agencies	No instructions; item is the total of lines 4A and 4B.

6. Grand Total - All Expenditures and Adjustments	No instructions; item is the total of line 3 and 5.
7. Comments	...The State will close the adjustment by explaining the reclassification in the comments section. The State should enter the following items in comments for the reclassification: 1) the reporting quarter of the “not assigned” charge, 2) the name of the Federal agency, 3) the three-digit code of the agency (as provided by the NO), and (4) the amount of the newly-assigned charge.

Cause

Based on discussion with the Fiscal Director, there were differences between the total amounts of benefit expenditures obtained from LWD’s ESCOT system and Edison. Fiscal staff could not determine the cause of the differences, which may have been the result of simple timing issues. Edison data was used as the source documentation for reporting purposes since Edison is the state’s official accounting system. Information for other line items, such as individual charges assigned to agencies, can only be obtained from ESCOT. As a result, fiscal staff placed both amounts on the report. Because the ESCOT-Edison discrepancies were internal accounting discrepancies, they should not have been included in this report. Should fiscal staff have felt it was necessary to include the differences between Edison and ESCOT on the report, they should have included a comment explaining the differences and circumstances of the data being reported.

Effect

When the ETA 191 reports are not properly prepared, incorrect and ambiguous data is reported to the U.S. Department of Labor, preventing proper monitoring of the UI program.

Recommendation

The Department of Finance and Administration should ensure that Fiscal Services staff have the proper training to prepare the ETA 191 report and that an adequate review of this report, including a review and sign off by LWD management, is completed prior to submission. As business partners, it is the responsibility of both F&A and LWD to ensure a mutual exchange of accounting, financial, and program information that will result in proper federal financial reporting.

Managements’ Comments

Department of Labor and Workforce Development

We concur. Where applicable, we will work with the Department of Finance and Administration to ensure proper financial reporting.

Department of Finance and Administration

We concur. The Department of Finance and Administration (F&A) fiscal staff has implemented controls to ensure errors are detected and reconciliations occur prior to the submittal of the ETA 191 reports. F&A fiscal staff will work to determine the cause(s) of the differences between LWD's ESCOT system and Edison. Once the cause(s) is identified, errors will be corrected and F&A fiscal staff will make necessary adjustments to the ETA 191 reports. F&A will work with LWD to improve the current review process as necessary to ensure proper federal financial reporting.

Finding Number	2014-046
CFDA Number	17.225
Program Name	Unemployment Insurance
Federal Agency	Department of Labor
State Agency	Department of Labor and Workforce Development
Grant/Contract No.	ES-23025-12-55-A-47; ES-24646-13-55-A-47; UI-19610-10-55-A-47; UI-21127-11-55-A-47; UI-22341-12-55-A-47; UI-23919-13-55-A-47; UI-25232-14-55-A-47; EUC, Fed EB, UCFE, and UCX; FAC Benefits & UI Admin; and TUC-State Expenditures
Federal Award Year	2010 through 2014
Finding Type	Material Weakness and Noncompliance
Compliance Requirement	Special Tests and Provisions
Questioned Costs	N/A
Repeat Finding	2013-030

Employment Security Division staff did not identify, establish, and process overpayments consistent with state and federal law and departmental procedures

Background

When the Department of Labor and Workforce Development determines that a claimant received Unemployment Insurance (UI) benefits for a week or weeks for which they were not eligible, the Employment Security Division establishes overpayments and classifies them as caused by either error or fraud. The claimant is responsible for reimbursing the department for the established overpayment, regardless of whether it is due to error or fraud.

The division is responsible for ensuring not only that UI benefit claimants meet eligibility requirements before claims are paid, but also that claimants continue to remain eligible for benefits. Division staff performs cross-matches by comparing data in Employment Security Combined Online Technology (ESCOT), the department's unemployment benefits information system, to data obtained from third parties—including other departments and employers—to determine if the claimants remain eligible for benefits. These cross-matches are intended to provide independent verification of the information provided by claimants. Division staff also flags current claims for review when claimants, employers, or other departments submit new information. Division staff is responsible for investigating this new information to determine if claimants remain eligible for benefits and/or whether benefit overpayments have occurred.

The division's Adjudication unit, which is generally responsible for resolving claimant eligibility issues, is also responsible for processing overpayments that result from errors. If, while fulfilling their responsibilities, the Adjudication unit staff identifies claims with fraud indicators, the unit forwards the claims to the division's Benefit Payment Control (BPC) unit for additional review. BPC staff is responsible for preventing, detecting, establishing, and collecting overpayments. Fraud indicators are documents or statements that are misleading or are intended to conceal earnings and/or other facts regarding a claimant's eligibility for unemployment benefits. Department policy states that only the BPC unit can investigate and establish overpayments

classified as fraudulent, since fraudulent overpayments are subject to additional penalties and interest.

Condition

As stated in both the 2012 and 2013 *Single Audit Report*, division staff did not identify, establish, and process overpayments consistent with state and federal law and departmental procedures. From the Adjudication unit's population²³ of 2,364 established overpayments, we selected a random, nonstatistical sample of 60 overpayments equaling \$1,000 or greater. For 8 of the 60 overpayments tested (13%), we found that the Adjudication unit did not properly identify overpayments containing fraud indicators, did not establish overpayments at the correct amount, and did not offset the overpayment against the claimants' subsequent UI benefits.

Specifically, the Adjudication unit

- classified six overpayments as not fraudulent, despite the existence of fraud indicators, and failed to refer these claims to the BPC unit for further evaluation, as required by departmental policy;
- established one overpayment for \$120 lower than the benefits actually received by the claimant; and
- did not offset one overpayment against the claimant's subsequent UI benefits because the Adjudication unit rendered an overpayment decision that the BPC unit did not enter into the department's ESCOT information system until three months later, missing the opportunity to offset the \$1,693 overpayment against UI benefits that the claimant had received in the interim.

Criteria

The department's *UI Manual* and *Benefit Payment Control Procedures Manual* provide written guidelines for identifying, establishing, and processing UI overpayments to maintain compliance with relevant state and federal laws:

- Section 50-7-303(a)(7), *Tennessee Code Annotated*, states a claimant will be disqualified for benefits

[f]or the week or weeks in which the administrator finds that the claimant has made any false or fraudulent representation or intentionally withheld material information for the purpose of obtaining benefits contrary to this chapter and for not less than four (4) nor more than the fifty-two (52) next following weeks, beginning with the week following the week in which the findings were made, as determined by the administrator in each case according to the seriousness of the facts. In addition, the claimant shall

²³ We obtained a population of 26,579 overpayments established by the department during the period July 1, 2013, through June 30, 2014. We filtered the population to determine that the Adjudication unit was responsible for a total of 2,364 of the established overpayments.

remain disqualified from future benefits so long as any portion of the overpayment or interest on the overpayment is still outstanding. In the event an overpayment of benefits results from the application of this disqualifying provision, the overpayment of benefits shall not be chargeable to any employer's account for experience rating purposes;

- Section 50-7-715, *Tennessee Code Annotated*, states:

(a) Any person who has received unemployment benefits by knowingly misrepresenting, misstating, or failing to disclose any material fact, or by making a false statement or false representation without a good faith belief as to the correctness of the statement or representation, after a determination by the commissioner that such a violation has occurred, shall be required to repay the amount of benefits received. (b) (1) The commissioner shall assess a penalty equal to fifteen percent (15%) of the overpaid benefits as described in subsection (a), to comply with the requirements of 42 U.S.C. § 503(a)(11). Moneys collected by this penalty shall be deposited into the unemployment compensation fund as provided in § 50-7-501. (2) The commissioner shall further assess a penalty equal to seven and one-half percent (7.5%) of the overpaid benefits described in subsection (a). Moneys collected by this penalty shall be used to defray the costs of deterring, detecting, or collecting overpayments. The penalty provided in this subdivision (b)(2) is in addition to the penalty provided in subdivision (b)(1). (c) (1) In addition to the requirements of subsections (a) and (b), the commissioner shall assess interest at a rate of no more than one and one-half percent (1.5%) per month on the total amount due that remains unpaid for a period of thirty (30) or more calendar days after the date on which the commissioner sends notice of the commissioner's determination that a violation has occurred to the last known address of the claimant. For purposes of this subdivision (c)(1), "total amount due" includes the unemployment benefits received pursuant to subsection (a) and the penalties provided for in subsection (b).

- Section 50-7-303(d), *Tennessee Code Annotated*, states that "Any person who is overpaid any amounts as benefits . . . is liable to repay those amounts . . ."
- Section 303(g)(1) of the Social Security Act states,

A State shall deduct from unemployment benefits otherwise payable to an individual an amount equal to any overpayment made to such individual under an unemployment benefit program of the United States or of any other State, and not previously recovered.

Cause

Top management did not ensure a clear delineation of responsibilities for detecting claims with fraud indicators or for establishing overpayments. During the audit period, both the Adjudication unit and the BPC unit were involved in detecting and investigating claims with

fraud indicators. As a result, the division established overpayments inconsistently and inaccurately. Furthermore, communication between the two units was not sufficient to ensure overpayments were properly offset against future UI benefits.

Effect

When staff does not properly identify, establish, and process overpayments, the division increases the risk that claimants will not be held accountable for returning overpaid benefits due to fraud or error. Additionally, this condition increases the risk that claimants who commit fraud will not be properly disqualified from the UI program and/or will not be subject to penalties and interest for fraudulent claims, as prescribed by state law.

Recommendation

Department management should either ensure that all overpayment functions are assigned to the BPC unit or ensure that Adjudication unit staff refers all suspected fraudulent overpayments to the BPC unit for further evaluation. Division staff should identify, establish, and process overpayments in accordance with state and federal law and the department's written procedures.

Management's Comment

We concur in part.

As noted in the finding, overpayments were established by adjudication staff (non-fraud) and benefit payment control (BPC) staff (fraud) during the audit period.

A Lean Event of the BPC functions was conducted in February 2014. One of the recommendations from the group was to centralize all overpayments within the BPC unit. During the audit period, the department was in the process of centralizing these functions within the BPC unit. The original deadline was October 2014, but actually was completed by August 1, 2014.

BPC management also has provided refresher training to audit staff regarding investigating and establishing overpayments, either fraudulent or non-fraudulent overpayments. US Department of Labor's policies and procedures are being followed.

Updates on the eight (8) overpayments identified by the auditors are as follows:

- The six (6) overpayments noted as not fraudulent but had fraud indicators were subsequently reviewed by a BPC auditor. Five (5) of these overpayments should have been designated as fraudulent.
- The overpayment established for \$120 less than benefits paid was corrected. The dependent allowance was not included.
- One of the overpayments was not promptly entered into the mainframe and a claimant received subsequent UI benefits without being offset for the overpayment. The audit

stated the BPC unit failed to enter this until three months later. The UI Control Unit, which was not part of BPC, was in fact several months delinquent in entering these overpayments. In May 2014, the UI Control Unit was absorbed by the BPC unit.

The detection of overpayments is one of the Core Performance Measures required by US Department of Labor (USDOL). The measure is defined as the “% of detectable, recoverable overpayments estimated by the Benefit Accuracy Measurement survey that were established for recovery.” The Acceptable Level of Performance is greater than or equal to 50% and less than or equal to 95%. A query report pulled from the USDOL website on February 10, 2015, for the period of January 1, 2012, to December 31, 2014, ranked Tennessee at 52.49%, which is within the acceptable performance level.

In January 2015, the State of Tennessee received the federal Final Determination regarding the findings contained in the *2013 Single Audit Report*. The federal Final Determination indicated the noted issues were corrected.

The department management believes this finding is resolved.

Auditor’s Comment

The U.S. Department of Labor issued its Final Determination of Tennessee Department of Labor and Workforce Development’s *2013 Single Audit* findings based on the department’s submission of documentation and correspondence relevant to correct any unresolved or pending issues from that audit. The U.S. Department of Labor has notified the department that its submission of corrective actions was accepted and will be monitored to ensure effective implementation. Based on our *2014 Single Audit* of the Tennessee Department of Labor and Workforce Development, management has not fully implemented corrective action as noted in the finding above.

We will evaluate management’s actions subsequent to the audit period during our next audit.

Finding Number	2014-047
CFDA Number	17.225
Program Name	Unemployment Insurance
Federal Agency	Department of Labor
State Agency	Department of Labor and Workforce Development
Grant/Contract No.	ES-23025-12-55-A-47; ES-24646-13-55-A-47; UI-19610-10-55-A-47; UI-21127-11-55-A-47; UI-22341-12-55-A-47; UI-23919-13-55-A-47; UI-25232-14-55-A-47; EUC, Fed EB, UCFE, and UCX; FAC Benefits & UI Admin; and TUC-State Expenditures
Federal Award Year	2010 through 2014
Finding Type	Material Weakness and Noncompliance
Compliance Requirement	Special Tests and Provisions
Questioned Costs	N/A
Repeat Finding	N/A

Internal controls not adequate in one area

The Department of Labor and Workforce Development did not provide adequate internal controls in one specific area. The details of this finding, however, are confidential pursuant to *Tennessee Code Annotated* Section 10-7-504(i). We provided management with detailed information regarding the specific conditions we identified, as well as the related criteria, cause, and our specific recommendations for improvement.

Ineffective implementation of internal controls increases the risk of noncompliance and the potential for the loss and misuse of data.

Recommendation

Management should ensure that these conditions are remedied by the prompt development and consistent implementation of internal controls in this area. Management should implement effective controls to ensure compliance with applicable requirements; assign staff to be responsible for ongoing monitoring of the risks and mitigating controls; and take action if deficiencies occur.

Management's Comment

We concur and are working with the applicable federal government agency in implementing the applicable internal controls.

Finding Number	2014-048
CFDA Number	17.225
Program Name	Unemployment Insurance
Federal Agency	Department of Labor
State Agency	Department of Labor and Workforce Development
Grant/Contract No.	ES-23025-12-55-A-47; ES-24646-13-55-A-47; UI-19610-10-55-A-47; UI-21127-11-55-A-47; UI-22341-12-55-A-47; UI-23919-13-55-A-47; UI-25232-14-55-A-47; EUC, Fed EB, UCFE, and UCX; FAC Benefits & UI Admin; and TUC-State Expenditures
Federal Award Year	2010 through 2014
Finding Type	Material Weakness and Noncompliance
Compliance Requirement	Special Tests and Provisions
Questioned Costs	N/A
Repeat Finding	N/A

The Benefit Accuracy Measurement unit’s independence was impaired

Background

The Department of Labor and Workforce Development’s Employment Security Division administers the Unemployment Insurance (UI) program. The division is responsible for a claims center, which makes eligibility determinations of claimants seeking UI benefits, and for the Integrity unit, whose purpose is to ensure the UI program’s integrity by monitoring its compliance with federal and state requirements and preventing overpayments of benefits.

The Integrity unit includes the Benefit Accuracy Measurement (BAM) unit, which is required by the U.S. Department of Labor. The unit is responsible for determining whether the division is appropriately paying or denying UI benefit claims requested by claimants. The BAM unit fulfills its responsibility by evaluating a sample of paid and denied claimant cases. The BAM unit reports its evaluation results to the U.S. Department of Labor, which uses the results to determine the division’s benefit accuracy rates. The BAM unit also serves as the division’s quality control function by attempting to identify and report to management any patterns of errors in the division’s eligibility determination and benefit payment processes. The Integrity unit also includes the Benefit Timeliness and Quality (BTQ) unit. This unit is required to evaluate a sample of the department’s eligibility determinations and report results of the reviews to the U.S. Department of Labor.

Since these units are required to objectively perform and report results of testwork on functions performed by the division’s claims center, it is essential that both the BAM and BTQ units maintain independence from the claims center to avoid any impairment of independence through conflicts of interest.

Condition

Based on our review, the BAM unit’s independence was impaired. We found that the division’s Administrator instructed claims center staff to send the director of the Integrity unit lists of

pending claims for UI benefits so Integrity unit staff could help reduce backlogs related to pending claims. The Integrity unit director then distributed these pending claims lists to the BAM unit so that BAM unit staff could assist the claims center by making eligibility decisions on claimants requesting UI benefits.

Based on inquiry, this practice began at the beginning of calendar year 2014, shortly after the current Integrity unit director was instated. (This director was formerly a manager within the claims center.) We were also told that this practice lasted several weeks and ended when we questioned the decision to allow BAM unit staff to make eligibility determinations (see finding 2014-042). The BAM unit selected its claims eligibility sample from a population of cases that included eligibility determinations made by staff. As a result, the BAM unit could not provide an independent and objective review of the eligibility determination process as required by federal regulations.

Criteria

Chapter II of the U.S. Department of Labor's Employment and Training Handbook 395 states:

Each BAM unit is required to be organizationally independent of, and not accountable to, any unit performing functions subject to evaluation by the BAM unit. The organizational location of this unit must be positioned to maintain its objectivity, to have access to information necessary to carry out its responsibilities, and to minimize organizational conflict of interest.

Cause

According to the director of the Integrity unit, shortly after assuming his new position, the division Administrator instructed the director to make eligibility decisions on certain types of claims. This was an apparent attempt to alleviate the large backlog of pending claims, which totaled over 15,000 in January 2014. (See findings 2014-042 and 2014-044.)

Effect

If BAM unit staff is directly involved with claimants' eligibility determinations, the BAM unit cannot objectively evaluate and/or make recommendations on eligibility and payment determination processes.

Recommendation

The Commissioner must ensure that top division management does not compromise the BAM unit's independence, or the independence of other units whose independence is required.

The Commissioner may wish to consider organizational changes such as requiring the director of the Integrity unit to report administratively to a member of management who is not directly responsible for the UI program, rather than to the division Administrator. If the Commissioner chooses to continue the current organizational structure, he should require the director of Internal

Audit to continuously monitor the independence and objectivity of the Integrity unit and, specifically, the Benefit Accuracy Measurement and Benefit Timeliness and Quality units.

Management's Comment

We do not concur.

BAM investigators are required to have at least three years of full-time experience in unemployment insurance claims taking or investigating or adjudicating unemployment insurance claims. With this requirement the investigator position is filled from the pool of experienced claims agents and adjudicators.

When a new BAM investigator is hired, it is not uncommon for a claim that they had previously worked in their old position to be included in the BAM sample. To avoid any conflict, the BAM supervisor assigns these cases to other investigators.

The auditors questioned the use of BAM investigators in reviewing claims. Three recently promoted BAM investigators were temporarily used to review some Internet filed claims. The facts are as follows:

- Due to a heavy seasonal increase in lack of work claims, between 11,000 and 13,000 Internet filed claims were awaiting review.
- Claims operations staff were already working overtime but were unable to keep up with the increased demand.
- A suggestion was made that there were some staff who had recently been promoted to other units that might be able to assist the claims unit (there were three of these staff in the BAM unit).
- The UI Integrity director was asked, not instructed, if any of these folks or others in his area would be interested or available to assist, depending upon their current workload.
- This was voluntary and the BAM investigators were removed from the BAM sample and did not come in contact with any claim they worked.
- Only three investigators were used, not the whole BAM unit as mentioned in the finding.
- They did not issue countable non-monetary agency decisions into ESCOT. These claims were lack of work claims that they reviewed for employer responses or availability issues.
- They did approve the claim, only if the employer agreed with the lack of work or did not respond. All of the worked claims were not approved. They also changed the claims to a pending issue, if the employer response said it was not lack of work or the claimant gave a disqualifying answer. These claims were processed by adjudicators.
- They reviewed 300 to 400 claims from January 23, 2014, through January 30, 2014, and stopped reviewing claims, because the three employees were no longer needed to review claims.

A lack of work claim approved by these investigators that later appeared in the BAM sample would have been reassigned to another auditor by the BAM supervisor, thereby eliminating any potential conflict of interest. The department does not consider this temporary use of three newly promoted investigators to be any different than hiring new investigators.

The Commissioner does not agree that there is any necessity for organizational changes.

Auditor's Comment

Chapter II of the U.S. Department of Labor's Employment and Training Handbook 395 states:

Each BAM unit is required to be organizationally independent of, and not accountable to, any unit performing functions subject to evaluation by the BAM unit. The organizational location of this unit must be positioned to maintain its objectivity, to have access to information necessary to carry out its responsibilities, and to minimize organizational conflict of interest.

As confirmed in management's responses the director of the Integrity unit and BAM unit staff participated in the eligibility determination process of claims that were later subject to review by the BAM unit, thereby impairing the unit's independence.

Finding Number	2014-049
CFDA Number	17.258, 17.259 and 17.278
Program Name	Workforce Investment Act Cluster
Federal Agency	Department of Labor
State Agency	Department of Labor and Workforce Development
Grant/Contract No.	AA-20221-10-55-A-47, AA-21423-11-55-A-47, DI-22464-11-75-A-47, AA-22963-12-55-A-47, AA-24120-13-55-A-47
Federal Award Year	2010 through 2013
Finding Type	Material Weakness and Noncompliance
Compliance Requirement	Activities Allowed or Unallowed Allowable Costs/Cost Principles Cash Management Period of Availability Subrecipient Monitoring
Questioned Costs	\$86,139
Repeat Finding	N/A

The department paid Local Workforce Investment Areas for improper drawdown requests and unallowable costs, resulting in federal questioned costs of \$86,139

Background

The Department of Labor and Workforce Development administers the Workforce Investment Act (WIA) cluster of programs through 13 subrecipients, or Local Workforce Investment Areas (LWIAs). The department awards the LWIAs multiple grant contracts throughout each year to provide adults, youth, and dislocated workers with workforce development and career services (e.g., training) based on local needs. The department finances the LWIAs on a limited advance basis²⁴ and requires them to request payment for each of their contracts on drawdown request forms. The department’s Program Accountability Review Office is responsible for monitoring the LWIAs to ensure that they have complied with fiscal and program requirements.

Condition

Based on our audit work, we found that the Program Accountability Review Office did not adequately review the LWIAs’ cash management processes or ensure that expenditures were made within the time frames specified by the LWIAs’ contracts and federal grant awards, nor did it identify unallowable food, event, and other expenditures charged to the WIA programs. In our expenditure testwork for the WIA programs, we tested two randomly selected subrecipient

²⁴ According to the department’s *Supplementary Financial Guide to the One-Stop Comprehensive Financial Management Technical Assistance Guide* (the *Supplementary Financial Guide*), “the financing of the WIA program will be on limited advance or reimbursement basis, in accordance with procedures established by the Tennessee Department of Labor and Workforce Development. The Sub recipient or contractor shall never retain funds which exceed immediate cash needs.”

reimbursement requests from each of nine LWIAs for the period of July 1, 2013, through June 30, 2014.²⁵ Based on our testwork, we identified the following.

- a. Two LWIAs (LWIA 8 and LWIA 10) did not prepare their drawdown requests based on individual contracts or maintain documentation establishing that the amounts they requested were limited to their immediate cash needs for the WIA programs.
- b. Four LWIAs (including the two noted above) received \$71,551 in WIA funds for
 - unallowable meals and events;
 - payments to program participants for course materials that were supplemental and exceeded the necessary amounts;
 - drawdown requests without adequate support; and
 - a phone bill that was not charged to one LWIA's contracts in accordance with its cost allocation plan.

Since we noted multiple food expenditures in our review of the general ledgers and expenditures for two LWIAs, we expanded our testwork to review all food-related expenditures from these two subrecipients charged to the WIA program during our audit period. Based on the results of our expanded testwork, we found that two LWIAs charged \$14,588 of unallowable food, meeting, and event costs.

²⁵ We originally selected the 18 subrecipient reimbursement requests, totaling \$660,780, from a population of 1,370 payments to the LWIAs, totaling \$43,909,231. As noted in the finding, two LWIAs did not maintain adequate documentation in support of their drawdown requests.

LWIA 8 records its expenditures at the contract level, allowing us to perform alternate testwork to determine whether expenditures recorded in its general ledger were allowable activities and costs for the WIA programs. The original sample had two \$50,000 drawdown requests paid to the LWIA. To replace the sample items, we tested a nonstatistical, haphazard sample of 66 items totaling \$64,044 from the LWIA's general ledger.

LWIA 10 did not record its expenditures at the contract level. As a result, we were unable to perform alternate testwork to determine whether general ledger expenditures were allowable activities and costs, resulting in questioned costs of \$70,000.

**TABLE 1:
LOCAL WORKFORCE INVESTMENT AREAS
WITH DEFICIENCIES IN DRAWDOWN REQUEST PROCESSES
AND/OR QUESTIONED COSTS**

LWIA No.	Entity Name	Notes / Description	Questioned Cost Amount
3		Meals; field trips for youth and staff	\$1,195
		Food and events (from expanded testwork)	12,168
8		Items not supported by documentation - (dremel accessory kit, welding cap, and welding jacket)	72
		Coupon discount not applied to payment for a participant's textbooks	22
10	South Central Tennessee Workforce Alliance	Drawdown requests could not be reconciled to expenditures on WIA contracts	70,000
11		Item not supported by documentation - phone bill allocation	262
		Food (from expanded testwork)	2,420
Total:			\$86,139

Criteria

- a. The *Code of Federal Regulations* (CFR), Title 29, Section 97.20(a)(2), states,

Grantees and subgrantees must maintain records which adequately identify the source and application of funds provided for financially-assisted activities. These records must contain information pertaining to grant or subgrant awards and authorizations, obligations, unobligated balances, assets, liabilities, outlays or expenditures, and income.

The department’s *Supplementary Financial Guide* to the U.S. Department of Labor’s *One Stop Comprehensive Financial Management Technical Assistance Guide* (TAG) requires that the LWIAs’ “accounting systems shall be supported by source documentation, which identifies the source and use of contract funds.” Additionally, the department’s instructions for completing the drawdown requests state that “the purpose of the Drawdown is to draw funds *by contract* on an as needed basis.”

- b. According to 2 CFR, Part 225, Appendix B, Section 14, the “costs of entertainment, including amusement, diversion, and social activities and any costs directly associated with

such costs (such as tickets to shows or sports events, meals, lodging, rentals, transportation, and gratuities) are unallowable.” In addition, 2 CFR, Part 225, Appendix B, Section 27, states that the “costs of meetings and conferences, the primary purpose of which is the dissemination of technical information, is allowable” and that “this includes costs of meals.” According to 2 CFR, Part 225, Appendix A (18)(C)(1)(f) and (i), the state’s costs should be “accorded consistent treatment” and “net of all applicable credit.” Finally, 20 CFR 663.805(b) states that “supportive services may only be provided when they are necessary to enable individuals to participate in title I activities.”²⁶

Cause

- a. The fiscal director for LWIA 8 prepares drawdown requests using an aging report, which shows the total amount needed for invoices scheduled for payment in the next two weeks but does not separate the drawdown requests by the agency’s adult, youth, and dislocated worker contracts. We were unable to verify the fiscal director’s description of the process since the LWIA staff did not maintain the aging reports or documentation showing how the amounts from the aging report were allocated to the different contracts.

According to the fiscal director for LWIA 10, she prepares the drawdown requests based on the total amount of checks scheduled for upcoming payment by the agency. If necessary, the fiscal director adds to this amount to adjust for any significant upcoming expenditures that are not scheduled for payment (e.g., payroll costs or payments on behalf of program participants). We were unable to verify the fiscal director’s description of the process since she did not maintain any record of the agency’s estimates of cash needs. The fiscal director stated that none of the agency’s other programs operate on an advance basis and that “all of the expenses are fronted by WIA and reimbursed by other programs,” indicating that the department may have paid the LWIA for expenditures and upcoming cash needs for other, non-WIA programs. Based on our review of general ledger reports and a chart of accounts provided by the fiscal director, as well as our discussions with her, the LWIA’s accounting system records information at the program level and not at the contract level as required by the TAG and the *Supplementary Financial Guide*.

The Program Accountability Review Office, which conducts annual monitoring reviews of the agencies, reviews the cumulative expenditures and drawdowns by contract to determine whether the LWIAs have excess cash on hand. Based on discussion with the office’s director and our review of the office’s working papers, monitors do not match individual drawdown requests to the LWIAs’ expenditures for the WIA programs.

- b. Based on review of supporting documentation at LWIA 8, we identified \$72 of WIA funds expended on participant training costs that were not necessary to enable the individual to participate in title I activities, and not listed on the list of required materials for the course. In addition, LWIA staff paid for a participant’s textbooks without taking a \$22 coupon discount into account, thereby failing to follow grant management procedures by ensuring that the expenditure was “net of all applicable credit.”

²⁶ 20 CFR 660.100 defines title I activities as “workforce investment activities that increase the employment, retention and earnings of participants, and increase occupational skill attainment by participants.”

Due to the grant accounting concerns noted at LWIA 10 (as described above), we were unable to test whether the payments to the agency included in our testwork were for allowable costs for the WIA program. We were also unable to determine the period of availability for the expenditures or test whether they were within the required beginning and end dates due to the LWIA's failure to maintain documentation in support of its drawdown requests or establish the required accounting system recording expenditures at the contract level.

LWIA 11 was unable to provide adequate supporting documentation to demonstrate how a phone bill allocated among the different WIA grants in accordance with its cost allocation plan. Although the LWIA's account clerk provided us with documentation showing how she allocated phone bill charges, we were unable to arrive at the amount that was charged to the program by the LWIA to ensure consistent treatment.

With regard to the food and event costs included in our testwork and expanded testwork, the fiscal manager at LWIA 3 explained that most of the food expenditures for his agency were for the youth program and provided an extra incentive for youth participants to attend youth meetings. (In our review, we noted that the LWIA paid for meals and for youth and staff to attend field trips.) The fiscal manager also stated some of the expenditures were for events such as the youth Senior Banquet and for SNAAP (Science, Nature, Arts, Adventure, and Proficiency), a week-long event for youth participants that included field trips to a local aquarium and garden. While well intentioned, these expenditures do not demonstrate the best use of federal funds. For the cost associated with staff events, neither LWIA 3 nor LWIA 11 provided documentation that adequately demonstrated that the events were for meetings and conferences, the primary purpose of which was the "dissemination of technical information."

Effect

- a. Without ensuring the LWIAs properly track the department's contract expenditures and maintain the required documentation to support their reimbursement requests, the department cannot be certain that the requests are within grant guidelines and allowable. In addition, if the department does not ensure adequate monitoring activities are performed, the department's risk of noncompliance with WIA allowable cost requirements is increased. Also, the LWIAs and the department cannot match grant revenue to expenses in accordance with *Generally Accepted Accounting Principles* when LWIA staff do not take all reasonable and available steps to ensure that their requests for federal funds are based on the expenditures and obligations for specific contracts.
- b. By not adequately monitoring subrecipients to ensure funds are expended on allowable activities and costs, the department increases the risk that federal resources may be used to fund unallowable activities and costs instead of providing services to more individuals through the WIA program.

Recommendation

- a. Management of the Workforce Services Division should work with the Fiscal Services Section to ensure that the LWIAs' requests for cash advances are only for the immediate cash needs of the agency's WIA programs. Division management should also ensure that the LWIAs keep all accounting records at the contract level and that they maintain documentation in support of drawdown requests. If necessary, the department should require that the LWIAs submit this documentation with their drawdown requests. Finally, management of the Program Accountability Review Office should revise its monitoring procedures to verify that the amounts of the LWIAs' drawdown requests are limited to the expenditures and immediate cash needs for the specific WIA contracts.
- b. The commissioner and the Workforce Services Division administrators should ensure that the LWIAs are fully aware of the allowable uses of grant funds and that program monitors adequately assess the allowability of local area expenditures.

Management's Comment

We concur in part.

We do not concur with the auditor's assessment that LWIA 3 food expenditures are an unallowable activity. LWIA 3 food expenditures were related to the SNAAP (Science, Nature, Arts, Adventure, and Proficiency) weeklong Youth event that required participation in the activities, including field trips and the youth Senior Banquet. The department's management feels the provision of food was justified, since it included sharing of technical data. We do not concur with the auditor's assertion regarding the allowability of the event costs of \$2,420 included in the expanded test work for LWIA 11. The Workforce Services Division already has provided supporting documentation regarding these costs showing the dissemination of technical information. We also feel that a welding cap and welding jacket are necessary for a participant receiving training in welding. For other questioned costs the division will be in contact with the applicable LWIA and US DOL.

We do concur with needed improvements with the drawdown request process and monitoring. The department has made the following improvements:

- First, beginning on January 7, 2015, the Workforce Services Grants & Budget Unit has implemented a process to match individual drawdown requests to the LWIA's expenditures for the WIA programs. This review occurs on a consistent (usually weekly) basis to help identify possible unallowable charges incurred for LWIA activities prior to any drawdown from the state. The process includes a review of general ledgers, as well as other supporting documentation (e.g., aging reports and items to support accrued expenses) that help justify the immediate cash needs of the WIA program.
- Second, each LWIA has submitted their written procedures documenting their immediate cash needs.

- Third, LWIA 8 is now maintaining the aging reports and documentation showing how the amounts from the aging report are allocated to the respective contracts.
- Fourth, Workforce Services Division has communicated with the other division regarding the applicable sub-recipient's cash needs. LWIA 10 has entered journal entries showing WIA funds were reimbursed from the other non-WIA program.

Lastly, to improve the monitoring efforts regarding drawdowns, the Program Accountability Review Office (PAR) has added steps to their *Detail Review Guide* to evaluate the process used to calculate the individual requested drawdown amounts. Monitoring efforts do not provide absolute assurance regarding the allowability of local area expenditures. PAR examines the applicable general ledgers and, if unusual vendors are noticed, a sample of expenditure transactions with those vendors are selected for detailed testing. PAR also selects a sample of WIA participants' files to determine whether expenditures on behalf of the selected participants are allowable. We feel this level of monitoring is sufficient and adequately monitors the local area expenditures.

Auditor's Comment

In accordance with Office of Management and Budget Circular A-133, we are required to report all known questioned costs which are greater than \$10,000. Office of Management and Budget Circular A-133 defines questioned costs as "a cost that is questioned by the auditor...(2) Where the costs, at the time of the audit are not supported by adequate documentation."

Regarding management's comment for the drawdown request process and monitoring, while we recognize absolute assurance is not possible, the Program Accountability Review Office's monitoring activities should be designed to provide reasonable assurance to detect unallowable costs and based on the process through which the subrecipients receive federal funds. The department issued payments to local areas based on their drawdown requests – not based on general ledger reports or participants' files.

Finding Number	2014-050
CFDA Number	17.258, 17.259 and 17.278
Program Name	Workforce Investment Act Cluster
Federal Agency	Department of Labor
State Agency	Department of Labor and Workforce Development
Grant/Contract No.	AA-25381-14-55-A-47
Federal Award Year	2013 through 2014
Finding Type	Significant Deficiency and Noncompliance
Compliance Requirement	Reporting
Questioned Costs	N/A
Repeat Finding	2013-034

Participant data for the Workforce Investment Act Annual Performance Report did not comply with reporting requirements

Background

The Department of Labor and Workforce Development administers the Workforce Investment Act (WIA) cluster of programs through 13 subrecipients, or Local Workforce Investment Areas. The department negotiates performance levels annually with the U.S. Department of Labor and is required to annually report participant performance for the WIA Annual Performance Report in terms of participant activity, progress, and outcome. When a WIA program participant completes an activity (e.g., training), subrecipients are required to update their records to document that the participant completed the activity and is no longer receiving services funded by the WIA program.

In order to report its annual performance, the department submits the WIA Standardized Reporting Data (WIASRD), an extract of participant data from its electronic Case Management and Activity Tracking System (eCMATS). The U.S. Department of Labor reviews WIASRD's accuracy by selecting a sample of data elements from the file and requiring the department to validate the elements with documentation from eCMATS or the participants' files. The department has also implemented a peer review process, whereby the Local Workforce Investment Areas review and validate the data element samples for each other. In addition, the U.S. Department of Labor conducts periodic comprehensive reviews of departments that operate the WIA program. The U.S. Department of Labor performed a comprehensive review of the department during the audit period and released a report in September 2014. For the program year 2012 data element validation, which was the most recent data element validation submitted, the U.S. Department of Labor selected 233 data elements for review for the Adult, Dislocated Worker, and Youth programs.

Condition

As stated in the 2012 and 2013 *Single Audit Reports*, department management and management at its Local Workforce Investment Areas did not comply with the U.S. Department of Labor's Training and Employment Guidance Letter (TEGL) 17-05. While we found some improvement in reporting participant exits from the program compared to the prior-year audit, we still found

notable errors in our testwork. Based on our nonstatistical random sample²⁷ of 135 WIA participant files from 9 of the 13 Local Workforce Investment Areas that were included on the program year 2013²⁸ WIASRD file, we noted the following:

- For 27 of 135 participants tested (20%), department staff did not exit the participants timely from the program or did not exit the participants at all. See Table 1 for results.

**Table 1
WIA PARTICIPANT EXITS**

Program	Number Tested	Number of Errors	Percentage of Errors	Prior-Year Error Percentage
Adult	45	5	11%	28%
Dislocated	45	9	20%	12%
Youth	45	13	29%	12%
Total	135	27		

In addition, we found that for 4 of 64 participants (6%) who received training, LWIA staff did not accurately report the participants' education status in eCMATS to reflect proper credentialing attainment in the participants' files. The participants' paper files contained evidence that two of the participants received Cardiopulmonary Resuscitation (CPR) certificates; one participant received an Occupational Safety and Health Administration (OSHA) certificate; and one participant only completed a few courses at a local college but did not actually attain any certificate or credential. The CPR and OSHA certifications should not have been considered occupational skills certification for the degree/certificate measure.

During our review, we also noted that WIASRD contained information that was inconsistent with information in eCMATS. For 6 of 135 participants in our sample (4%), the exit date listed in WIASRD was later than the exit date listed in eCMATS, creating the appearance that the participants were not exited timely and calling into question the accuracy of the WIASRD, even though WIASRD is an extract of eCMATS.

We also reviewed errors noted in our prior-year testwork to ensure those participants were subsequently exited from the program during the current audit period. We determined at the time of our follow-up that

- 5 of 46 participants (11%) identified in the prior audit were still listed as active and had not been exited from the program.

We also performed an analysis of the department's most recent U.S. Department of Labor data element validation results by comparing the program year 2012 results to the program year 2011 results. While we found a year-over-year improvement, we noted the following:

²⁷ Our sample consisted of the following: 135 participants from a population of 35,276 were tested from 9 Local Workforce Investment Areas. Of those 135 sampled participants, 54 of the 8,667 WIA participants entered the program during the period July 1, 2013, through June 30, 2014, and 81 of 26,609 WIA participants were either exited from the WIA program prior to March 31, 2014, or had not yet been exited from the program.

²⁸ The program year extends from July 1, 2013, through June 30, 2014.

- For program year 2012, the department exceeded a 5% error rate threshold for 56 of 215²⁹ data elements tested (26%). Additionally, 29 of 56 data elements that exceeded the 5% error rate (52%) had error rates that did not improve from program year 2011 to program year 2012.

The U.S. Department of Labor also examined the program year 2012 data element validation results as part of its on-site comprehensive review. Based on its review, the U.S. Department of Labor noted that the department continues to have high error rates (in excess of the 5% allowable error) in the data elements.

Criteria

The U.S. Department of Labor's TEGL 17-05 states, "The term program exit means a participant has not received a service funded by the program or funded by a partner program for 90 consecutive calendar days, and is not scheduled for future services."

TEGL 6-14, Attachment A, EDRVS Field Number 151, "Source Documentation Requirements," states that if a participant has obtained a credential, receipt of the credential must be verified by documentation such as "transcripts, certificates, diploma, surveys, [and] case notes."

The validation instructions in TEGL 6-14, Attachment A, Section C(4), state that if case notes are used, they must contain "a participant's status for a specific data element, the date on which the information was obtained, and the case manager who obtained the information."

By definition in TEGL 15-10, "A credential is awarded in recognition of an individual's attainment of measurable technical or occupational skills necessary to obtain employment or advance within an occupation." According to the U.S. Department of Labor's website under Program Reporting and Record Keeping Information, which includes the WIA program, "While CPR or OSHA training may provide a benefit to participants as they begin to gain general knowledge about occupations and occupational standards, participants are unlikely to gain employment or advance within an occupation based solely upon receiving a CPR or an OSHA certificate."

According to its comprehensive review report, the U.S. Department of Labor noted "high error rates for critical data elements in excess of the 5% percent threshold."

According to Title 20, *Code of Federal Regulations*, Section 667.300(e)(2),

States submitting annual performance progress reports that cannot be validated or verified as accurately counting and reporting activities in accordance with the reporting instructions, may be treated as failing to submit annual reports, and be subject to sanction. . . . Any sanction would be in addition to having to repay the amount of any incentive funds granted based on the invalid report.

²⁹ The U.S. Department of Labor selected 233 data elements for their review, but we only analyzed 215 data elements since 18 of the data elements had no data to validate, and therefore no error rates to analyze.

Cause

Based on discussions with staff at Local Workforce Investment Areas (LWIAs) during our on-site visits, LWIAs failed to properly exit participants due to a lack of understanding of which program activities extend participation in the program, and supervisors did not ensure that the case managers were following up with the participants and updating eCMATS timely. In addition, we found that LWIA staff did not understand what qualified as an education credential. In response to a comprehensive review performed by the U.S. Department of Labor, department management stated that they had conducted case management training with LWIA staffs in order to reduce the data element validation error rates, further suggesting that the errors we noted were the result of a lack of training.

We were unable to determine the cause of the errors in WIASRD.

Effect

By not ensuring staff are properly trained and have adequate knowledge of program requirements, and by not ensuring the data reported accurately reflects supporting data, the department increases the risk of submitting inaccurate performance data in the WIA Annual Performance Report.

Recommendation

Management of the Department of Labor's Workforce Services Division should ensure that the LWIAs report accurate and up-to-date information for use in federally required reports. The commissioner or his designee should ensure that personnel at the LWIAs are provided sufficient and proper case management training. Division management should determine the cause of the inaccuracies in WIASRD and take appropriate corrective action. Finally, division management should continue efforts to reduce data element validation error rates to below the 5% threshold.

Management's Comment

We do not concur.

To ensure accuracy of reporting, US DOL established guidelines for WIA services that extend participation. Thus, the finding's assertion is incorrect that, after one service ends, sub-recipients are required to update records that the participant is no longer receiving services funded by the WIA program. These guidelines state that needs-related payments across several program areas may continue beyond training service end dates, as well as all partner program services.

Furthermore, when a program participant is engaged by Workforce Services (WFS) staff, WIA provides for three levels of services: core, intensive, and training. And according to US DOL (20 CFR Part 652 et al., p. 49318 Preamble), it is up to the state and local workforce boards to develop a mix of activities that will best serve the participants to achieve employment goals, and that local program operators are best positioned to determine the appropriate mix and duration of services. For example, there is no minimum duration for intensive or training services.

Also, US DOL's initial determination for the *2013 Single Audit Report* indicates the participant's exit date issue has been corrected, since WFS is continuing to use Participant Tenure Reports to analyze and adjust service end dates. This statement also applies to the current finding, since the final Participant Tenure Report was executed in October 2014. WFS also has launched its new Virtual One-Stop data tracking system that specifically implements a mandatory exit, when there are no services that extend participation in the system.

The data validation error rates cited in the finding are for the 2012 program year, and do not reflect the outcomes for the period under audit (i.e., July 1, 2013, through June 30, 2014). By using data element validation error results for the current audit period, the data element validation results have significantly improved. For program year 2013 the department exceeded a 5% error rate threshold for 13 of 215 data elements (6%), which is a 20% improvement over PY 2012. Also, the finding states that 29 data elements did not improve from program year 2011 to program year 2013; however, we show that only five (5) did not improve. USDOL has confirmed the data element validation error results for program year 2013.

The Workforce Services Division always is focused on accurate and timely reporting for all our programs. The state office staff and the field staff are fully committed to serving Tennesseans to the best of our ability. To this end, the division is and has been delivering in-person training and virtual training to all our staff statewide, especially with regard to compliance in all program areas.

Regarding the US DOL comprehensive review, the Workforce Services Division has provided responses to all points indicated in the comprehensive review report. However, we have not as yet received a response from US DOL.

Auditor's Comment

We performed our participant testwork based on Workforce Investment Act guidance as published in the Training and Employment Guidance Letter 17-05 (as cited in the "Criteria" section) which defines a program exit and specifically names activities that do not extend participation in the program. Our conclusions as stated in the finding were that department staff did not properly exit participants in accordance with federal guidance.

The U.S. Department of Labor issued its Final Determination of Tennessee Department of Labor and Workforce Development's *2013 Single Audit* findings based on the department's submission of documentation and correspondence relevant to correct any unresolved or pending issues from that audit. The U.S. Department of Labor has notified the department that its submission of corrective actions was accepted and will be monitored to ensure effective implementation. The Office of Management and Budget Circular A-133 Compliance Supplement for 2014 requires us to test the WIA Annual Performance Report annually as part of the 2014 Single Audit, and our current audit results demonstrate that management has not corrected all prior conditions – and that new conditions exist.

We could evaluate only data validation error rates for program year 2012 as those were the only rates available to us during our current audit period. Management submitted the data validation

error rates for program year 2012 to U.S. DOL during the current audit period, July 1, 2013, through June 30, 2014. We did not claim to review any rates other than those submitted for program year 2012; therefore, management is incorrect in stating we reviewed program year 2013.

The department's comment did not address all conditions identified in the finding.

Finding Number	2014-051
CFDA Number	84.002
Program Name	Adult Education – Basic Grants to States
Federal Agency	Department of Education
State Agency	Department of Labor and Workforce Development
Grant/Contract No.	V002A110043, V002A120043, V002A130043
Federal Award Year	2011 through 2013
Finding Type	Material Weakness and Noncompliance
Compliance Requirement	Matching, Level of Effort, Earmarking Subrecipient Monitoring
Questioned Costs	\$18,542
Repeat Finding	N/A

Department staff did not review subrecipients’ matching expenditures to ensure the expenditures were allowable under the grant

Condition

The Department of Labor and Workforce Development’s Adult Education Division administers the Adult Education (AE) – Basic Grants to States federal grant program through 45 local area organizations that serve as program subrecipients. The subrecipients received approximately \$9.5 million in federal funding during fiscal year ended June 30, 2014. Based on our analysis, the department’s subrecipients are expected to fund approximately \$1.6 million per award through their match amounts.

The AE Division did not require subrecipients to submit documentation to support the subrecipients’ required match and, therefore, did not ensure that the subrecipients’ matching expenditures were allowable grant expenditures. Furthermore, even though the division required subrecipients to maintain documentation at their respective locations, the department’s monitoring activities were not sufficient to ensure subrecipients’ matches were based on allowable costs.

Due to restructuring of the AE program, the department experienced a reduction in the number of subrecipients, and division management requested that the Program Accountability and Review (PAR) Office only conduct “close-out” reviews of the subrecipients that would no longer receive AE grant funds. PAR did not review the matches claimed by any of the subrecipients remaining in the program (see finding 2014-053).

Our review of a sample of 60 expenditures for the period July 1, 2013, through June 30, 2014, included 10 subrecipient reimbursement requests. These reimbursement requests also included information for the subrecipients’ required grant matching amounts. Based on our testwork and review of the requested documentation, we were unable to determine whether \$18,542 of \$20,842 (89%) matching amounts reported (by nine of the ten subrecipients) were allowable based on the documentation provided by the subrecipients.

In addition, we also found that department management did not identify or assess any risks related to the federal and non-federal matching requirements in its annual risk assessment.

Criteria

The Adult Education and Family Literacy Act (Title II of the Workforce Investment Act of 1998) requires that each state agency providing adult education and literacy services contribute a non-federal contribution (match) of at least 25%. Title 34, *Code of Federal Regulations* (CFR), Section 80.24, states, “Third party in-kind contributions count towards satisfying a cost sharing or matching requirement only where, if the party receiving the contributions were to pay for them, the payments would be allowable costs.”

In addition, 34 CFR 80.24 states the following:

Costs and third party in-kind contributions counting towards satisfying a cost sharing or matching requirement must be verifiable from the records of grantees and subgrantee or cost-type contractors. These records must show how the value placed on third party in-kind contributions was derived.

Cause

The AE Division, which administers the Adult Education – Basic Grants to States program, required the subrecipients to maintain documentation to support the reported match, but did not require subrecipients to submit it. Instead, the division relied on PAR to verify the reported matches as a part of its subrecipient monitoring activities; however, PAR did not conduct monitoring activities specifically designed to ensure the subrecipients’ matching contributions were based on allowable expenditures.

Effect

The department cannot ensure that it meets the federal matching requirements because it has not ensured that subrecipients properly submitted qualified and sufficient (at least 25%) matching expenditures. Without verification that its subrecipients provided allowable matching funds, the state would be unlikely to meet the match requirements, thus limiting the department’s participation in this federal award.

Recommendation

The commissioner and the Adult Education division administrator should ensure that subrecipients are required to provide support for their reported matches and that staff review this documentation to verify that the match amounts claimed are allowable.

Management should assess all significant risks, including the risks noted in this finding, in management’s documented risk assessment. The commissioner should ensure management implements effective controls in order to comply with applicable requirements; assign staff to be

responsible for ongoing monitoring of the risks and any mitigating controls; and take action if deficiencies occur.

Management's Comment

We concur. In July 2013 the division, recognizing that additional safeguards needed to be in place regarding verification of matching expenditures, provided training to sub-recipients regarding what constitutes an allowable expense for matching expenditure purposes. In July 2014 the division went a step further and began requiring sub-recipients to submit supporting documentation for matching expenditures. Since that time, the supporting documentation for matching expenditures has been reviewed by the division and verified as allowable under the grant.

Finding Number	2014-052
CFDA Number	84.002
Program Name	Adult Education – Basic Grants to States
Federal Agency	Department of Education
State Agency	Department of Labor and Workforce Development
Grant/Contract No.	V002A110043 and V002A120043
Federal Award Year	2011 and 2012
Finding Type	Material Weakness and Noncompliance
Compliance Requirement	Reporting
Questioned Costs	N/A
Repeat Finding	N/A

Federal Financial Reports were not accurate

Background

For the Adult Education – Basic Grants to States program, Fiscal Services staff from the Department of Finance and Administration (F&A) prepare the annual Federal Financial Reports. (Per executive order, the Department of Labor and Workforce Development [LWD] has an agreement with F&A that financial accounting and reporting functions of LWD will be managed and operated by F&A. This agreement includes F&A’s completion of federal reporting for LWD.) F&A Fiscal Services staff prepares both initial and final Federal Financial Reports on the overall status of the Adult Education awards and the English Literacy and Civics portions of the awards. (Congress reserves a percentage of each year’s federal grant award for English Literacy and Civics activities.) An initial report covers the first 15 months of an award, and a final report covers the entire 27-month award period.

Condition

Our review of all four Federal Financial Reports (FFRs) due for the period July 1, 2013, through June 30, 2014, disclosed that federal cash receipts were understated by a total of \$127,311; federal cash disbursements were understated by a total of \$1,129,419; the federal share of expenditures was overstated by a total of \$288,824; and the recipient share of expenditures was understated by a total of \$342,539. The four FFRs were for program year 2011 (final) and 2012 (initial) reports.

In addition, we found that

- both the federal share of expenditures and the recipient share of expenditures classifications were reported based on allocations of total expenditures, instead of actual outlays of federal and state expenditures in the accounting records;
- on the 2012 federal award, the recipient share of expenditures was not reported on the correct line for the English Literacy and Civics report;
- Fiscal Services staff did not perform a reconciliation between accounting records and the amounts reported on the FFRs;

- only one individual possesses the knowledge to complete the FFRs; and
- no supervisory review was performed on the reports prior to submission.

Criteria

Title 34, *Code of Federal Regulations* (CFR), Section 461.10, states that recipients of the Adult Education federal grant award are required to report information annually about the state's program expenditures. The National Reporting System's *Implementation Guidelines: Measures and Methods for the National Reporting System for Adult Education* contains instructions for the Adult Education financial reporting and indicates that the department is required to prepare the financial reports using actual disbursements or outlays for federal and recipient expenditures.

Federal regulations 2 CFR 200.61 and 200.303 require non-federal entities to implement and maintain internal controls to reasonably ensure compliance with federal laws, regulations, and program compliance requirements, as well as to provide reasonable assurance regarding the reliability of reporting for internal and external use.

Cause

Based on our assessment of internal controls related to the department's preparation and submission of its financial reports, we determined that because management and staff did not reconcile amounts reported in the FFRs to the accounting records and did not review the reports prior to submission, they submitted inaccurate reports to the federal grantor.

Effect

According to 34 CFR 76.720, failure to submit reports "at the quality level specified in the data collection instrument . . . constitutes a failure . . . to comply substantially with a requirement of law applicable to the funds made available under [the Adult Education] program." In addition, incorrect financial reporting to the federal government may result in a future reduction in funding.

Recommendation

The Department of Finance and Administration should ensure that Fiscal Services staff have the proper training to prepare the Federal Financial Reports and that an adequate review of these reports, including review and sign off by LWD management, is completed prior to submission. Fiscal Services staff should properly report expenditures based on amounts in the accounting records or reconcile any other data sources used to the accounting records. Fiscal Services staff should request that the U.S. Department of Education reopen the 2011 final reports so that necessary corrections can be made. As business partners, it is the responsibility of both F&A and LWD to ensure a mutual exchange of accounting, financial, and program information that will result in proper federal financial reporting.

Managements' Comments

Department of Labor and Workforce Development

We concur. Where applicable, we will work with the Department of Finance and Administration to ensure proper financial reporting.

Department of Finance and Administration

We concur. The Department of Finance and Administration (F&A) fiscal staff has corrected and resubmitted the four Federal Financial Reports (FFRs) identified in the finding and has implemented controls to ensure errors are detected, and reconciliations and reviews occur prior to the submittal of the FFRs. F&A will work with LWD to improve the current review process as necessary to ensure proper federal financial reporting.

Finding Number	2014-053
CFDA Number	84.002
Program Name	Adult Education – Basic Grants to States
Federal Agency	Department of Education
State Agency	Department of Labor and Workforce Development
Grant/Contract No.	V002A110043, V002A120043, V002A130043
Federal Award Year	2011 through 2013
Finding Type	Material Weakness and Noncompliance
Compliance Requirement	Subrecipient Monitoring
Questioned Costs	N/A
Repeat Finding	N/A

The department did not comply with monitoring requirements

Condition

The Department of Labor and Workforce Development’s Adult Education Division administers the Adult Education – Basic Grants to States federal grant program through 45 local area organizations that serve as program subrecipients. The organizations received approximately \$9.5 million in federal funding during fiscal year ended June 30, 2014. The Adult Education Division and the Program Accountability Review (PAR) Office are each responsible for a part of the subrecipient monitoring for the Adult Education program. Based on our audit work, we found that the division did not obtain subrecipients’ A-133 audit reports or complete a subrecipient monitoring plan. We also found that the PAR Office did not include all of the required compliance requirements in its monitoring activities.

In addition, management did not identify and assess any risks related to its failure to obtain A-133 audit reports or complete monitoring plans in its risk assessment. Although management included the risk of not monitoring subrecipients “in accordance with the requirements of A-133” in the annual risk assessment, they did not develop control activities sufficient to ensure that the PAR Office addressed all required core monitoring requirements.

Criteria

According to Office of Management and Budget (OMB) Circular No. A-133, pass-through entities such as the department are required to monitor subrecipients’ activities to ensure that federal awards are used for authorized purposes and that performance goals are achieved. They must also ensure that subrecipients expending \$500,000 or more in federal awards during their fiscal year have obtained A-133 audits. State monitoring requirements are set forth in Central Procurement Office (CPO) Policy 2013-007, which applies “to all State agencies that award State or federal funds.” Policy 2013-007 requires state agencies to submit an annual monitoring plan to the CPO by October 1 of each year.

Cause

Based on our discussions with the Adult Education division administrator, the division did not obtain A-133 audit reports from its subrecipients, nor did it complete a monitoring plan for the period July 1, 2013, through June 30, 2014. The administrator stated that she was unaware that the A-133 reports had not been obtained. She noted that the division had a designated employee to perform the division's monitoring activities several years ago and that the responsibility for obtaining the A-133 reports may not have been reassigned when the position was eliminated.³⁰ With regard to the completion of the monitoring plan, the administrator stated that she was unaware of the CPO policy requiring the preparation and submission of an annual monitoring plan.

Due to a reduction in the number of subrecipients awarded program funds, approximately half of the Adult Education subrecipients ceased participating in the grant program. As a result, the department limited its monitoring to "close-out" reviews of these entities during the audit period. Based on discussion with the director of the Program Accountability Review (PAR) Office, the office's close-out reviews did not include any monitoring of activities allowed or unallowed, cash management, earmarking, or Title VI compliance. Both the PAR director and the Adult Education division administrator indicated that the close-out reviews did not include these compliance requirements because only a review of fiscal compliance requirements (e.g., allowable costs/cost principles and equipment management) was the main priority for the close-out reviews. Although the PAR Office's Detailed Review Guide (DRG) does not require that the cash management compliance requirement be tested since subrecipients do not receive cash advances, we believe that without testing the requirement, the PAR Office cannot obtain adequate assurance that subrecipients are operating on a reimbursement basis.

Effect

By not obtaining A-133 audit reports for subrecipients, not completing formal monitoring plans and related documented risk assessments, and not monitoring all applicable compliance requirements, the department increases the risk that noncompliance, fraud, waste, and abuse could occur and not be detected and resolved appropriately and timely.

Recommendation

The commissioner and the Adult Education division administrator should ensure that Adult Education program subrecipients' A-133 audit reports are obtained and reviewed, and that the annual monitoring plans are properly completed. If necessary, the commissioner should require the department's PAR Office to obtain subrecipients' audit reports and complete a comprehensive monitoring plan for the department. In addition, the PAR director and the Adult

³⁰ According to the director of Internal Audit, he reviews the A-133 reports available through the Local Government Division of the Comptroller's Office to identify any Adult Education program findings. However, he does not ensure that all of the Adult Education program subrecipients receive A-133 reports or provide copies of the reports to Adult Education Division staff unless they include findings that relate specifically to the Adult Education program.

Education division administrator should ensure that all applicable compliance requirements are included in the department's subrecipient monitoring activities.

Management should assess all significant risks, including the risks noted in this finding, in management's documented risk assessment. The commissioner should ensure management implements effective controls in order to comply with applicable requirements; assign staff to be responsible for ongoing monitoring of the risks and any mitigating controls; and take action if deficiencies occur.

Management's Comment

We concur. A sub-recipient monitoring plan was not completed in accordance with Central Procurement Office (CPO) Policy 2013-007. Once the division became aware of this policy, a monitoring plan was submitted on October 1, 2014, in compliance with Policy 2013-007. CPO approved the monitoring plan on October 17, 2014.

We also concur that a copy of each sub-recipient's A-133 audit report was not obtained directly by the Adult Education Division. However, many of the A-133 audits have been completed by the Comptroller's Division of Local Government Audit. The Director of Internal Audit received a summary of the results of the A-133 audits performed by the Comptroller's Division of Local Government Audit. These summary reports are reviewed for findings applicable to Adult Education and, if any are found, they are reported to the division. These summary reports have been and remain on file in the Office of Internal Audit. In response to this finding, the division has started receiving, reviewing, and maintaining the summary reports, in addition to that kept by the Office of Internal Audit.

Finally, the division hired an employee on December 1, 2014, with duties regarding performance monitoring. This individual will direct all fiscal and programmatic monitoring activities, including those addressed in this audit.