

Mr. Shaun Thomas, Director
State of Michigan Department of Licensing and Regulatory Affairs
Unemployment Insurance Agency,
State of Michigan Office of the Auditor General
State of Michigan Office of Financial Management

In planning and performing our audit of the financial statements of the State of Michigan Department of Licensing and Regulatory Affairs, Unemployment Insurance Agency – Unemployment Compensation Fund, Contingent Fund, and Obligation Trust Fund (Funds) as of and for the year ended September 30, 2013, in accordance with auditing standards generally accepted in the United States of America, we considered the Funds' internal control over financial reporting (internal control) as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Funds' internal control. Accordingly, we do not express an opinion on the effectiveness of the Funds' internal control.

However, during our audit, we became aware of certain matters that are opportunities for strengthening internal control and operating efficiency. These matters are included within this letter.

We would be pleased to discuss these matters in further detail at your convenience, to perform any study of these matters, or to assist you in implementing the recommendations.

This communication is intended solely for the information and use of management of the Funds, the Office of the Auditor General, the Office of Financial Management, and others within the organization, and is not intended to be and should not be used by anyone other than these specified parties.

Andrews Hooper Pavlik PLC

December 12, 2013
Auburn Hills, Michigan

Current Year Recommendations

Control Review of Actiondata, Inc.

We noted during our tests of internal controls that control procedures in place at Actiondata, Inc., subcontractor for data entry of UIA forms 1020, 1020R, 1021, and 1017 have not been tested by the agency since 2008. It is our understanding that the agency's procedures include testing the control procedures at Actiondata on a biannual basis. Due to the volume of transactions processed by Actiondata and the sensitivity of the information processed, we recommend that the agency resume its review of this subcontractor on a biannual basis, beginning in the next fiscal year.

Management's Response:

Forms UIA 1020, 1020R, 1021 and 1017 have been discontinued and replaced with Form UIA 1028, *Employer's Quarterly Wage/Tax Report*. During the transition period between August 2012 and May 2013 all aspects of the tax lockbox process – at both Chase and Action Data – were very closely monitored. This monitoring consisted of an on-site visit by agency management at both Chase and Action Data; daily/weekly conference calls during peak processing; and quarterly, in person meetings to address processing concerns. All of the processing instructions were revised, and several additional edits and controls were put in place. In addition, in February 2013 the agency's field audit management performed a comprehensive review of processed tax returns to assess the quality of the information keyed.

The agency concurs that the lockbox activity is critical to the agency operations and that the process should be closely monitored. On-site verification of control procedures will be performed on the lockbox operations on a biannual basis.

Monarch Reporting

We utilize the Monarch reporting system used by the agency to generate reports of benefit payments paid to claimants by benefit program. During our tests of the Extended Benefit (EB) Program, we noted 10 instances out of 77 tested where the claimant selected for EB testing from the Monarch report did not qualify for EB in the benefits system. We recommend that the agency perform a review of the Monarch and benefit system to determine the cause for the inconsistencies noted and correct any errors.

Management's Response:

Monarch is a tool utilized by the accounting section to capture activity processed through the Trust Fund Accounting System. The exceptions noted were due to improper coding being applied when the payments were made. All 10 instances were reviewed and corrected. The implementation of the agency's new system will eliminate the need for staff to manually enter federal program codes and improve the accuracy of the benefit charging.

Experience Rate Testing and Documentation

During our testing of internal controls, we noted that the number of the experience rate tests performed by the agency was approximately half of the amount performed in the previous year. In addition, documentation was not maintained by 3 out of the 7 technicians performing the tests. We recommend that the agency implement a policy that establishes the required number or percentage of employers to be tested for experience rate accuracy and documents the rationale for this number or percentage. In addition, we recommend that the agency document and retain documentation for all experience rate testing performed.

Management's Response:

Several factors contributed to the reduction in the number of rate tests performed by the agency. The agency implemented the new automated tax system in August 2012, and the rates were generated in December 2012. Staff inexperience and expanded testing on the new system increased the amount of time needed for each sample item. Adding to the complexity, a recent law change eliminated the need to test the rates for employers in 2 out of the 7 groups; and the 'look back' period for the calculation of the CBC was changed from 48 to 36 months.

The Agency agrees the sample of rates tested was less than in previous years. However the testing was extremely thorough and provided the quality assurance needed to release the rates. The procedure in place for the selection process and the testing process has not changed from previous years. However, the agency agrees documentation should have been maintained by all of the technicians that performed the testing. The procedure will be reviewed to ensure this documentation is retained and staff is appropriately trained.

Non-chargeable Benefits Account Testing

During our testing of the non-chargeable benefits account (NBA), we noted 7 out of the 77 claimants selected for testing had wages in excess of \$200 and the separation reason was noted as 1. It is our understanding that amounts are only charged to NBA if an employee has wages less than \$200 or has wages in excess of \$200 and a separation reason for something other than 1. We recommend that the agency set a review policy to ensure that the amounts charged to NBA are properly recorded in the system to reflect the appropriate separation reason and add notes related to any exceptions outside of the agency's policy.

Management's Response:

The charge to the NBA occurs if a) the separating employer's wages are less than or equal to \$200.00 or b) regardless of the separation reason indicated on the initial claim finding if the claimant was found to be disqualified regarding the employer and subsequently satisfied a rework (or would have satisfied a rework in the case of a re-determination of charges). The agency reviewed the seven exceptions noted; most of these exceptions were due to adjudication. One of the items will require a correction.

All benefit charging criteria were reviewed and validated during the new system development. The agency performs on-going monitoring of its automated systems to ensure the integrity and accuracy of benefit charges. Procedures will be developed to require the documentation of any deviations from the automated calculations.

Status of Prior Year Recommendations

Bank Reconciliations

We previously recommended that the agency complete all bank reconciliations and have the reconciliations reviewed and adjusted to general ledger within approximately 45 days of month end. We noted in the current year that the Fund has completed and reviewed all bank reconciliations within 45 days of month end. This comment has been adequately resolved and we make no further recommendation in this area.

Management's Response:

No further action is required.

Receivable and Allowance Accounts

We previously recommended the receivable and allowance accounts be "cleaned up" by writing off old receivable balances that will most likely not be collected or enforcement procedures be implemented to collect these amounts.

We repeat our recommendation in this area.

Management's Response:

During FY 2013 the UIA focused it's 'clean up' efforts on employer receivables. A significant amount of staff effort was utilized to review old receivable balances most likely not to be collected and confirmed that the accounts met the statutory guidelines to be written off. This review also validated the 'automated write off' process in the new system. In addition, the agency obtained the approval of the state administrative board to streamline it's write off approval process for both employer and restitution receivables. The agency will direct it's efforts to validating the automated write off process for the Restitution accounts in FY 2014.

Reimbursing Employer

We previously recommended that the agency correct posting errors and reconciling items between deposit log sheets and the deposit amount the MiDAS system for the August 15, 2012 deposit. This comment has been adequately resolved and we make no further recommendation in this area.

Management's Response:

No further action is required.

Revenue Receipt

We previously recommended that the agency maintain documentation in FileNet for revenue receipts, including Forms 1020, 1763-1, and checks to confirm that payments received were applied to the correct quarter. This comment has been adequately resolved and we make no further recommendation in this area.

Management's Response:

No further action is required.