

Report on Expenditures of Federal Awards

State of Michigan
Department of Licensing and Regulatory Affairs
Unemployment Insurance Agency –
Unemployment Compensation Fund

Year Ended September 30, 2014

State of Michigan
Department of Licensing and Regulatory Affairs
Unemployment Insurance Agency –
Unemployment Compensation Fund

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Independent Auditors' Report on Internal Control Over Financial Reporting and on
Compliance and Other Matters Based on an Audit of Financial Statements
Performed in Accordance with *Government Auditing Standards*

State of Michigan
Office of the Auditor General,
Office of Financial Management and
Department of Licensing and Regulatory Affairs,
Unemployment Insurance Agency

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the State of Michigan, Department of Licensing and Regulatory Affairs, Unemployment Insurance Agency – Unemployment Compensation Fund (Fund), as of and for the year ended September 30, 2014, and the related notes to the financial statements, and have issued our report thereon dated December 5, 2014.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Fund's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances 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 Fund's internal control. Accordingly, we do not express an opinion on the effectiveness of the Fund's internal control.

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

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. We did identify a deficiency in internal control, described in the accompanying schedule of findings and questioned costs as item 14-01, that we consider to be a significant deficiency.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Fund's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed an instance of noncompliance or other matters that are required to be reported under *Government Auditing Standards* and which are described in the accompanying schedule of findings and questioned costs as item 14-01.

The Fund's Response to Findings

The Fund's response to the findings identified in our audit is described in the accompanying schedule of findings and questioned costs. The Fund's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Andrews Hooper Paulik PLC

Auburn Hills, Michigan
December 5, 2014

Independent Auditors' Report on Compliance For Each Major Federal Program; Report on Internal Control Over Compliance; and Report on Schedule of Expenditures of Federal Awards Required by OMB Circular A-133

State of Michigan
Office of the Auditor General,
Office of Financial Management and
Department of Licensing and Regulatory Affairs,
Unemployment Insurance Agency

Report on Compliance for Each Major Federal Program

We have audited the State of Michigan, Department of Licensing and Regulatory Affairs, Unemployment Insurance Agency – Unemployment Compensation Fund's (Fund) compliance with the types of compliance requirements described in the *OMB Circular A-133 Compliance Supplement* that could have a direct and material effect on the Fund's major federal program for the year ended September 30, 2014. The Fund's major federal program is identified in the summary of auditors' results section of the accompanying schedule of findings and questioned costs.

Management's Responsibility

Management is responsible for compliance with the requirements of laws, regulations, contracts, and grants applicable to its federal programs.

Auditors' Responsibility

Our responsibility is to express an opinion on compliance for the Fund's major federal program based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the Fund's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

We believe that our audit provides a reasonable basis for our opinion on compliance for each major federal program. However, our audit does not provide a legal determination of the Fund's compliance.

Opinion on Each Major Federal Program

In our opinion, the Fund complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on its major federal program for the year ended September 30, 2014.

Other Matters

The results of our auditing procedures disclosed an instance of noncompliance, which is required to be reported in accordance with OMB Circular A-133 and which is described in the accompanying schedule of findings and questioned costs item 14-01. Our opinion on each major federal program is not modified with respect to this matter.

The Fund's response to the noncompliance finding identified in our audit is described in the accompanying schedule of findings and questioned costs. The Fund's response was not subjected to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on the response.

Report on Internal Control Over Compliance

Management of the Fund is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit over compliance, we considered the Fund's internal control over compliance with the types of requirements that could have a direct and material effect on the major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major federal program and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the Fund's internal control over compliance.

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

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, we identified a deficiency in internal control over compliance, as described in the accompanying schedule of findings and questioned costs as item 14-01, that we consider to be a significant deficiency.

The Fund's response to the internal control over compliance findings identified in our audit is described in the accompanying schedule of findings and questioned costs. The Fund's response was not subjected to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on the response.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of OMB Circular A-133. Accordingly, this report is not suitable for any other purpose.

Report on Schedule of Expenditures of Federal Awards Required by OMB Circular A-133

We have audited the financial statements of the Fund as of and for the year ended September 30, 2014, and the related notes to the financial statements. We issued our report thereon dated December 5, 2014, which contained an unmodified opinion on those financial statements. Our audit was conducted for the purpose of forming an opinion on the financial statements as a whole. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by OMB Circular A-133 and is not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the schedule of expenditures of federal awards is fairly stated in all material respects in relation to the financial statements as a whole.

Andrews Hooper Pavlik PLC

Auburn Hills, Michigan

December 5, 2014, except for our report on the Schedule of Expenditures of Federal Awards, for which the date is February 26, 2015

State of Michigan
 Department of Licensing and Regulatory Affairs
 Unemployment Insurance Agency –
 Unemployment Compensation Fund

Schedule of Expenditures of Federal Awards

Year Ended September 30, 2014

Federal Agency / Program Title	Catalog of Federal Domestic Assistance Number	Grant Number	Expenditures
Department of Labor – Employment and Training Administration:			
Unemployment Insurance	17.225	UI-25211- 14-55-A-26	\$ 1,182,557,045
Alternative Trade Adjustment Assistance / Trade Benefits	17.225	UI-25211- 14-55-A-26	11,999,146
American Recovery and Reinvestment Act – Unemployment Insurance	17.225	UI-25211- 14-55-A-26	66,360,900
Total Federal Financial Assistance			<u>\$ 1,260,917,091</u>

See accompanying notes to schedule of expenditures of federal awards.

State of Michigan
Department of Licensing and Regulatory Affairs
Unemployment Insurance Agency –
Unemployment Compensation Fund

Notes to Schedule of Expenditures of Federal Awards

Year Ended September 30, 2014

(1) General

The accompanying Schedule of Expenditures of Federal Awards (SEFA) presents the activity of federal financial assistance programs of the State of Michigan Department of Licensing and Regulatory Affairs, Unemployment Insurance Agency Unemployment Compensation Fund (Fund). The operations of the Fund are recorded as described in Note 1 of the Fund's financial statements.

(2) Basis of Accounting

The accompanying SEFA is presented using the modified accrual basis of accounting.

(3) ARRA Funds

The Fund included \$14,430,613 of ARRA Administration and Modernization expenditures on the SEFA in the Unemployment Insurance Program (CFDA No. 17.225). This entire expenditure was passed through to other State of Michigan agencies.

State of Michigan
Department of Licensing and Regulatory Affairs
Unemployment Insurance Agency –
Unemployment Compensation Fund

Schedule of Findings and Questioned Costs

Year Ended September 30, 2014

Section I – Summary of Auditors’ Results

Financial Statements

(a) The type of report issued on the financial statements: **Unmodified Opinion**

(b) Internal control over financial reporting:

- i. Material weaknesses identified? **No**
- ii. Significant deficiencies identified that are not considered material weaknesses?
Yes

(c) Noncompliance material to financial statements noted? **No**

Federal Awards

(a) Internal control over major programs:

- i. Material weaknesses identified? **No**
- ii. Significant deficiencies identified that are not considered material weaknesses?
Yes

(b) The type of report issued on compliance for major programs: **Unmodified Opinion**

(c) Any audit findings which are required to be reported under Section 510(a) of OMB Circular A-133? **Yes**

(d) Major program: **Unemployment Insurance/17.225**

(e) Dollar threshold used to distinguish between Type A and Type B programs: **\$3,782,751**

(f) Auditee qualified as a low-risk auditee under Section 530 of OMB Circular A-133? **No**

State of Michigan
Department of Licensing and Regulatory Affairs
Unemployment Insurance Agency –
Unemployment Compensation Fund

Schedule of Findings and Questioned Costs (continued)

Year Ended September 30, 2014

Section II – Findings Relating to the Financial Statements Reported in Accordance with Government Auditing Standards

Finding 14-01

Grant Program/CFDA #: Unemployment Insurance/17.225

Criteria: A strong system of internal controls mandates that general ledger account balances are properly reconciled to a subsidiary ledger or other adequate supporting documentation on a periodic basis.

Condition: Federal program account balances on the general ledger did not reconcile to the actual revenue and expenditure activity for the year due to erroneous adjustments posted to the accounts. These errors went undetected by management due to the fact that the Agency was not reconciling federal revenue and expenditure accounts throughout the year.

Questioned Costs: None.

Systemic or Isolated: Systemic.

Effect: Federal revenue and expenditures were initially misstated on the general ledger.

Recommendation: We recommend that the Agency implement procedures to reconcile activity in the federal revenue and expenditure accounts on a monthly basis throughout the fiscal year.

Response: The coding problem with restitution write-offs has been identified. The automated process will be re-configured to accurately account for the federal programs. The accounting section is scheduled to do a full review and reconciliation of all the activity accounts during Fiscal Year 2015.

Section III – Findings and Questioned Costs Relating to Federal Awards

Finding 14-01 is also considered to be a federal award finding.

State of Michigan
Department of Licensing and Regulatory Affairs
Unemployment Insurance Agency –
Unemployment Compensation Fund

Summary Schedule of Prior Audit Findings

Year Ended September 30, 2014

Finding 13-01

Grant Program/CFDA #: Unemployment Insurance/17.225

Criteria: Eligibility. Under the Extended Benefits (EB) program, claimants must document contact with three potential employers per week. This documentation must be filed with the Unemployment Compensation Fund (Fund) prior to the payment of benefits for the week under consideration.

Condition: The Fund did not maintain documentation of the work search requirement for 45 claimants out of 77 tested.

Questioned Costs: \$11,439

Systemic or Isolated: Systemic.

Effect: We were unable to determine if these claimants were eligible for benefits.

Recommendation: The Fund should maintain documentation of claimants' work search efforts in accordance with program requirements.

Response: Management agrees that work search documentation should be retained for all EB claims. All of the exceptions identified will be reviewed to ensure required documentation is received. A determination will be issued for claimants not meeting the work search requirement and restitution established.

The Fund is required to do a quarterly random audit on work search documents for the U.S. Department of Labor. During the review, claimants are contacted for any missing documentation. In addition, any problems with the receipt and processing of the work search documentation are addressed when identified.

Current Status: This finding was adequately resolved and is no longer considered a finding.

State of Michigan
Department of Licensing and Regulatory Affairs
Unemployment Insurance Agency –
Unemployment Compensation Fund

Summary Schedule of Prior Audit Findings (continued)

Year Ended September 30, 2014

Finding 13-02

Grant Program/CFDA #: Unemployment Insurance/17.225

Criteria: *Eligibility.* Under the EB and Emergency Unemployment Compensation (EUC) programs, the Fund must retain application documentation for all claimants.

Condition: The Fund did not retain application documentation for 35 claimants out of 77 tested for the EB program and 8 claimants out of 30 tested for the EUC program.

Questioned Costs: \$11,595

Systemic or Isolated: Systemic.

Effect: We were unable to determine if these claimants were eligible for benefits.

Recommendation: The Fund should retain application documentation in accordance with program requirements.

Response: Management agrees that application documentation should be retained for all EB claims. All of the exceptions identified will be reviewed to ensure all required documentation is received. A determination will be issued for any claimant not meeting the application requirement.

The Unemployment Agency implemented a new automated Benefit System at the end of September 2013. The capabilities of the new system are greatly enhanced and the Agency issue of application retention has been fully addressed.

Current Status: This finding was adequately resolved and is no longer considered a finding.