

Independent Auditor's 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
Department of Labor and Economic Opportunity,
Unemployment Insurance Agency,
Office of the Auditor General and
State Budget Office

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 Labor and Economic Opportunity, Unemployment Insurance Agency – Compensation Fund (Fund), as of and for the year ended September 30, 2024, and the related notes to the financial statements, which collectively comprise the Fund's basic financial statements, and have issued our report thereon dated December 11, 2024.

Report on 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) as a basis for designing 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 a 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 a 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. As described below, we did identify a deficiency in internal control that we consider to be a material weakness.

Finding 2024-001: Claim Progression and Eligibility Requirements

Criteria: The federal government set a prescribed claim progression and eligibility requirements for federal programs resulting from the Coronavirus pandemic. If a claimant is eligible for regular unemployment compensation, the claimant is ineligible for receiving benefits under the Pandemic Unemployment Assistance (PUA), Pandemic Emergency Unemployment Compensation (PEUC), or Extended Benefits (EB) programs. In addition, claimants must exhaust all rights to benefits under the previous claim type within the progression to become eligible for the subsequent claim type.

Condition: In certain instances, the benefit system allowed for the payment of benefits under the PUA, PEUC, and EB programs when claimants were eligible for regular unemployment compensation or prior to the exhaustion of the previous claim type within the progression.

Cause: Proper controls were not set within the benefit system to ensure proper eligibility and claim progression.

Effect: Payments of benefits under federal programs have no net effect on the net position of the Fund since the expenditure is offset by a reimbursing federal revenue, whereas payments under regular unemployment compensation reduce the net position of the Fund. Additionally, improper payments of benefits under federal programs create unallowed federal costs.

Recommendation: We recommend that the Agency improve controls in the benefit system to ensure proper eligibility and claim progression.

Views of Responsible Officials and Planned Corrective Actions: Management agrees with the finding. This issue was also raised by the U.S. Department of Labor (DOL), Employment and Training Administration (ETA) in an enhanced desk monitoring review titled *The State of Michigan's Pandemic Unemployment Assistance (PUA) and Federal Pandemic Unemployment Compensation (FPUC) programs*. Based on correspondence with U.S. DOL, these findings were deemed resolved with no further action required due to the significant administrative burden involved in correcting the payment sequencing. All claimants were paid the proper benefits, but the federal program charged was incorrect in some instances.

Regarding improvements to the controls to prevent a future issue such as this, along with plans to dedicate sufficient resources to timely audit new programs for compliance, the Agency has revised its process for prioritizing and completing necessary system updates. Effective May 2023, Agency Services implemented an SQR prioritization process for the Agency. When an SQR is opened, it is the responsibility of the applicable division to ensure the request is added to their division priority list and given a priority score (from one to five with one as the highest priority). Meetings are held monthly between Agency

Services and division representatives to discuss and review the status of each SQR until the change is migrated to production.

Report on 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 financial statements. 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 instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* and which are described below.

Finding 2024-002: Nonresponsive Employer – Relief of Charges

Criteria: States are prohibited from providing relief from charges to an employer's unemployment compensation account when the benefit overpayments are the result of the employer's failure to respond timely or adequately to a request for information.

Condition: The Agency elected to relieve charges to an employer's unemployment compensation account when the benefit payment was the result of the employer's failure to respond timely or adequately due to the Covid-19 Pandemic causing unforeseen difficulties for employers within the State.

Cause: The Agency implemented an SQR to credit the charges that would have typically been charged to the nonresponsive employer's unemployment compensation account during the Covid-19 Pandemic. However, there was an error in the logic of the SQR and certain employers did not have their charges associated with Covid-19 claims relieved.

Effect: Certain nonresponsive employers incorrectly had their unemployment compensation account charged for benefits during the Covid-19 Pandemic. The Agency's policy to provide relief for employers during the Pandemic was not applied consistently to each employer.

Recommendation: We recommend that the Agency review the logic of the SQR that was implemented to credit the charges that would have typically been charged to the nonresponsive employer's unemployment compensation account during the Covid-19 Pandemic and review the benefits that were charged to employer accounts throughout the Covid-19 Pandemic to determine which employers were erroneously charged.

Views of Responsible Officials and Planned Corrective Actions: Management agrees with the finding. Our analysis included reviewing benefit charges on the employer account, which showed credit has been applied when appropriate to do so. A SQR was created to research the matter. The SQR found there were nonmonetary cases which were omitted, but their omission was correct because the specific cases cited were not labeled as nonresponsive in our database. In certain instances, identified by the Auditor, the entity first charged for the benefits was the nonchargeable benefit account (NBA) and not the employer's account. It would be incorrect to give the employer credit when they were not charged for the benefits. In other situations where the employer was adversely

impacted by subsequent adjudication, the review showed the credit is associated with restitution becoming active. Due to the collection pause, restitution in certain situations has not become active in the system. As a result, credit has not been applied. Once the collection pause is lifted, credit allowable to the employer should be processed systematically.

Finding 2024-003: Offsets of Future Unemployment Compensation Payments

Criteria: Offsets of future unemployment compensation payments to recover prior overpayments are limited to the recovery of the prior overpayment amount in accordance with federal guidance.

Condition: Unapplied offset recoveries attributable to subsequent period adjustments to the original benefit overpayment were used to recover penalties and interest.

Cause: Due to the continual movement of monies as a result of changes in amounts due resulting from corrections or appeal decisions, a parameter has not been established in the benefit system to account for every possible scenario to prevent the allocation of unapplied recoveries to penalties and interest after overpayment amounts due were satisfied.

Effect: Interest and penalties due under federal and state law were recovered from offsets of unemployment compensation payments.

Recommendation: We recommend that the Agency add a parameter to the automated system to ensure adjustments to benefit offsets are only applied to the recovery of prior overpayment amounts.

Views of Responsible Officials and Planned Corrective Actions: Management agrees with the finding. The necessary parameter was previously implemented that prevented the inappropriate allocations on current and subsequent benefit payment recoveries; however, subsequent reallocations of monies under specific circumstance caused prior recoupments to improperly reallocate. The Trust Fund Accounting section will perform a monthly review to confirm that no prior period adjustments reallocated recoupments to penalty and interest. The review to date has determined that the adjustment amounts are immaterial. An automated solution does not appear obtainable in the current system. The Agency is in the process of implementing a new automated system and will ensure these adjustments are programmed correctly.

Finding 2024-001 is also considered an instance of noncompliance or other matter required to be reported under *Government Auditing Standards*.

Fund's Response to Findings

Government Auditing Standards requires the auditor to perform limited procedures on the Fund's response to the findings identified in our audit and described above. The Fund's response was not subjected to the other auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on the response.

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 Fund'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 Fund's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Andrews Hooper Pavlik PLC

Bloomfield Hills, Michigan
December 11, 2024