



ARIZONA DEPARTMENT OF ECONOMIC SECURITY

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Janet Napolitano
Governor

David A. Berns
Director

Ms. Debra K. Davenport
Auditor General
Office of the Auditor General
2910 North 44th Street, Suite 410
Phoenix, Arizona 85018

Dear Ms. Davenport:

We have completed our review of the revised draft performance audit report of the Department's Unemployment Insurance (UI) program. We have revised our response initially sent to you on December 7, 2004, and this letter and the attachment reflect those changes. The enclosure includes our response to the recommendations outlined in the draft report.

The Department has already begun implementing the recommendations contained in your report. In addition, DES is exploring the use of federal Reed Act funds for major improvements to the technological infrastructure that supports the UI program, which will assist in the Department's improvements to timeliness and accuracy.

We appreciate the cooperation of your staff throughout the performance audit process. If you have any questions regarding the response, please contact Patrick F. Harrington, Assistant Director, Division of Employment and Rehabilitation Services at (602) 542-4910 or Thomas Colombo, Program Administrator for the Employment Administration at (602) 542-3667.

Thank you for the opportunity to review the revised draft report.

Sincerely,

David A. Berns

Enclosure

**ARIZONA DEPARTMENT OF ECONOMIC SECURITY
SUNSET REVIEW DRAFT REPORT
RESPONSE TO AUDITOR GENERAL'S REVISED RECOMMENDATIONS**

SECTION I-Response to Findings

Finding 1: Division should improve eligibility determination accuracy.

The finding of the Auditor General is agreed to and the audit recommendation is being implemented. In addition, DES is exploring the use of federal Reed Act funds for major improvements to the technological infrastructure that supports the UI program, which will assist in the Department's improvements to timeliness and accuracy.

Auditor General Recommendations:

- 1. The Division should regularly analyze data from the BAM program to determine the causes of errors and use the results to train staff in an effort to reduce errors.**

The Department concurs with the recommendation of the Auditor General. The recommendation has been implemented and will result in reduced process errors and overpayment estimates.

On September 1, 2004, the Benefit Accuracy Measurement (BAM) staff and Policy and Training staff reviewed and updated BAM procedures to address collection and dissemination of data. The Department of Labor reviewed and approved the updated procedures on October 15, 2004.

On September 7, 2004, BAM staff created a detailed monthly report that provided reasons for improper payment or denial of claims. Policy and Training staff reviewed the report and determined trends of common errors from October 7, 2004 through November 5, 2004.

Based on data provided by the BAM Unit, Policy and Training staff created a training curriculum to address errors and began classes to educate UI Benefits staff on November 18, 2004. The classes were completed November 30, 2004.

On November 17, 2004, Training and Policy staff also reviewed client caused errors and identified methods to reduce client error. The work search log was the most common source of client error. Policy and Training staff members are currently revising the form for simplicity and clarity. The form redesign will be completed by January 2005.

Ongoing analysis of data from the Benefit Accuracy Measurement program will continue monthly to determine common errors and be used to update training curriculum as needed. BAM Unit data will

also be utilized by supervisors to coach and train staff individually to improve the accuracy of their determinations.

2. The Division should simplify and reduce the number of reasons adjudicators must select from in making determinations.

The Department concurs with the recommendation of the Auditor General. The Division has implemented the recommendation to simplify complex statements supporting determinations.

On March 10, 2004, Policy and Training staff requested UI Benefits staff to provide recommended changes to reduce the number of reasons adjudicators could select when making determinations.

On June 1, 2004, Policy and Training staff began consolidating and simplifying the reasons adjudicators must select from in making determinations. The revised statements were shared with UI Benefits staff for comments on December 28, 2004. The system handbook will be updated by January 2005. Training of call center staff will occur by February 2005.

3. The Division should establish supervisory review standards in its formal policies and procedures.

The Department concurs with the recommendation of the Auditor General. The recommendation has been implemented to increase supervisory review of cases.

On May 10, 2003, the department established a supervisor review standard. Supervisors have been expected to review four cases per month for each agent since that time.

On December 2, 2004, the Division developed a formal policy to include written performance standards which require supervisors to conduct four reviews per month for each agent. Written acknowledgement of these procedures was obtained in December 2004 and has been included in the supervisors' performance expectations.

4. The Division should continue its efforts to provide additional training for supervisors on the Benefits Timeliness and Quality (BTQ) standards to ensure that they apply them correctly during supervisory reviews.

The Department concurs with the recommendation of the Auditor General. The recommendation has been implemented to ensure supervisors apply correct review criteria to sampled cases.

On September 13, 2004, UI Benefits management staff requested specific feedback from the internal appeals unit regarding common error trends.

Policy and Training staff reviewed the error analyses and developed training curriculum to address Benefits Timeliness and Quality standards (BTQ). Policy and Training staff began refresher training for managers to apply review criteria correctly on November 18, 2004 and completed classes on December 2, 2004. This training will be an ongoing process based on analysis of BTQ errors.

5. The Division should consider cross-training adjudicators and claims agents and rotating them through the adjudications and initial claims units in the call centers.

The Department concurs with the recommendation of the Auditor General. The recommendation is being implemented to ensure cross training and rotation of staff.

A thirteen week series of classes was developed for cross training of staff. Training will begin January 14, 2005, and is scheduled for completion by April 2005. The Division will begin rotation of cross-trained staff by April 2005.

6. The Division should consider turning some of its current, temporary part-time positions into permanent full-time or part-time positions that would qualify for employee benefits and hiring qualified individuals from outside the UI program as adjudicators.

The Department concurs with the recommendation of the Auditor General. The recommendation is being implemented.

To the extent possible within budgetary constraints, the Division will convert some temporary positions to full time permanent positions. Workload projections will be monitored and duties assigned according to the agency's needs to maintain effective staffing levels.

Finding 2: Division provided inaccurate employer tax information to IRS.

The finding of the Auditor General is agreed to and the audit recommendation will be implemented. In addition, DES is exploring the use of federal Reed Act funds for major improvements to the technological infrastructure that supports the UI program, which will assist in the Department's improvements to timeliness and accuracy.

Auditor General Recommendations:

- 1. The Division should implement a quality control program to improve the accuracy of data it submits to the IRS by:**
 - a. Following IRS requirements to conduct an annual quality review of its FUTA certification computer program;**
 - b. Conducting a targeted review related to errors discovered during the audit;**
 - c. Documenting the results of its reviews;**
 - d. Correcting errors discovered in its reviews; and**
 - e. Carefully testing any program changes made to correct these errors.**

The Department concurs with the recommendation of the Auditor General. The recommendation is being implemented.

During the audit, the Division was informed by the Auditor General that errors existed in the tape provided to the IRS. Initial attempts to correct the programming still revealed errors during validation by the department. DES completed additional corrective programming and performed further validation of the data. After validation, a corrected copy was provided to the IRS on July 15, 2004.

Upon further review, on September 13, 2004, the Division determined that the entire Federal Unemployment Tax Act (FUTA) Certification computer program should be rewritten.

This rewrite is necessary to ensure that the business requirements of the FUTA program are properly satisfied and supported. This will ensure that the program is properly documented and contains only clean, logical, and functional code. The rewrite began on September 13, 2004.

The rewrite of this program includes functionality that will allow for the identification of the source of the data that is used to produce the IRS annual tape. It also includes the ability to validate the data sent to the IRS through sampling of data from a file that will be created for such purposes.

The Division will ensure that both the Employment Administration Management Information Systems and Policy and Training Unit work collaboratively to develop processes and procedures to ensure an annual quality review of the computer program is conducted. Errors discovered during this quality review will be addressed and corrected. The Division will complete the FUTA program rewrite and associated validation tasks by February 2005.

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The impact of the Department providing inaccurate information to the IRS is limited to the employer receiving notification from the IRS to contact the Department regarding their tax account to resolve a discrepancy. Once the employer contacts the Department, the tax record will be reviewed to determine the source of the discrepancy and the record will be corrected at that time. If the employer is liable for additional taxes, written notification will be provided. If the employer overpaid, a credit balance will be established or a refund will be issued at the employer's request.

- 2. The Division should develop a system to track information related to FUTA recertification requests, including employer state account number, federal identification number, and the reason for the FUTA recertification. The Division should use this information to determine if any programming errors exist and then correct them.**

The Department concurs with the recommendation of the Auditor General. The recommendation will be implemented.

Beginning in February 2005, Management Information Systems (MIS) will develop and test a new automated system to track information related to FUTA recertification requests, including employer state account number, federal identification number, and the reason for the FUTA recertification. MIS and the Policy and Training Unit will ensure that impacted staff members receive training on the new system. The Division will use this information to determine if any programming errors exist and then correct them. The Division will implement this tracking system in March 2005.

- 3. The Division should update and revise its FUTA certification policies and procedures and ensure that staff follow them.**

The Department concurs with the recommendation of the Auditor General. The recommendation will be implemented.

Beginning in January 2005, the Division will create an on-line handbook that incorporates FUTA policies and procedures, along with a monitoring plan to ensure staff compliance with policies and procedures. The Division will complete this task by June 2005. Training will be provided to staff members by July 2005.

Finding 3: Division should improve process for determining employer tax liability.

The finding of the Auditor General is agreed to and the audit recommendation is being implemented.

Auditor General Recommendations:

- 1. To help improve timeliness, the Division should continue its efforts to implement an automated application transmittal system.**

The Department concurs with the recommendation of the Auditor General. The recommendation is being implemented.

On June 17, 2004, a collaborative effort between UI Tax staff, Management Information Systems (MIS), and the Policy and Training Unit began to determine system and business requirements for an automated application transmittal system.

The Division is currently testing the Joint Tax Application process developed in conjunction with the Department of Revenue. The new web based system will distribute Joint Tax Applications to UI Tax Employer Status Examiners for assignment of an employer account number and tax liability determinations.

The Division's MIS and Policy and Training Unit began development of the training plan and curriculum on December 2, 2004. Training is scheduled to begin January 2005. The system implementation date is February 2005.

An inventory reduction plan was deployed and untimely actions from 2003 were processed by November 30, 2004. The Status Unit is currently working on 2004 inventory. The Division recognizes that a delayed determination can have negative results for employers and claimants and result in a loss of state tax revenue. Additional staff members are being hired to focus on completing the oldest applications as a priority assignment to reduce this impact. Workload projections indicate that the inventory will be current by June 2005 which is a year earlier than anticipated in the State Quality Service Plan.

- 2. The Division should develop and implement a formal policies and procedures manual for tax liability determinations to help improve timeliness and to help ensure that staff consistently apply state and federal requirements.**

The Department concurs with the recommendation of the Auditor General. The recommendation is being implemented.

Beginning January 2005, the Division will develop a comprehensive on-line policies and procedures handbook, which will be completed by June 2005. Training will be provided by July 2005.

3. The Division should implement an ongoing training program to help ensure that staff are consistently and accurately following procedures when making tax liability determinations.

The Department concurs with the recommendation of the Auditor General. The recommendation is being implemented.

Status Unit management began monthly meetings to review unit processes and procedures on October 6, 2004. Common liability issues and error trend analysis was also conducted. Status Unit management will continue to conduct bi-monthly work reviews of each Status Unit Examiner's product.

On November 16, 2004, topical refresher training was conducted to address common misapplication of policy and to develop error trends. Monthly training sessions during unit meetings reinforce the correct application of policy to ensure that staff members are consistently and accurately following procedures. In addition, a monitoring component will be added to ensure that staff members are following policies and procedures. The monitoring tool will be in place by February 2005.

4. The Division should continue its efforts to fill tax determination management and supervisory positions to help ensure that procedures are followed and to verify compliance with state and federal requirements.

The Department concurs with recommendation of the Auditor General. The recommendation has been implemented.

On August 29, 2004, UI Tax management submitted hiring requests to fill management and supervisory positions. The Status Manager position has been posted. The Status Unit Supervisor position has been filled and all Program Service Evaluators.

On November 18-19, 2004, new management staff members were provided an orientation that included a review of performance expectations, Department of Labor requirements, and local office procedures. All management staff hired will be provided with this orientation. The review of performance expectations will also be provided to the current management staff which will ensure complete awareness of program requirements.

5. The Division should establish a policy to fully document its reasons for removing cases from the TPS list of failed cases to ensure that outside parties can confirm that its decisions to do so are valid and appropriate.

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The Department concurs with the recommendation of the Auditor General. The recommendation has been implemented.

The Tax Performance System (TPS) review process is based on U. S. Department of Labor ET Handbook 407. The TPS Manager has implemented an internal policy which fully documents why cases are removed from the TPS list of failed cases. This policy is effective for the testing sample for calendar year 2004. To date, no cases have been removed from the sample but the documentation process has been established.

Finding 4: Division should improve management of employer refunds and audits.

The Department concurs with the finding.

- 1. To help reduce staff time in reviewing data entry errors and to ensure that employers are notified of legitimate refunds, the Division should conduct a comprehensive analysis of its pending refunds list to verify that it is accurate and current with the employer database.**

The Department concurs with the recommendation of the Auditor General. The recommendation is being implemented to notify employers of their credit balances. Employer requests for a refund rather than a credit will be processed upon receipt.

The Division began examining the refund process in May 2004. The TPS Manager worked with the appropriate Units to devise a system that emphasized a credit balance. The Division notes that not all employer payables are refunds since the employer may owe past UI taxes or will soon be liable for another quarter.

On November 15, 2004, two staff members were assigned to conduct a comprehensive review of each pending refund to verify accuracy prior to establishing a credit balance.

The UI Employer Accounting Unit Management is working with Management Information Systems (MIS) to modify programming so that credit balances may be reflected on the employer's Tax and Wage Report, Form UC-018. The final specifications to change Form UC-18 have been submitted to MIS for action. The Division will complete the changes necessary to implement this recommendation by April 2005.

- 2. To help ensure that refunds are efficiently and accurately issued to employers, the Division should update its procedures, fill vacant positions, and provide ongoing training to experienced staff.**

The Department concurs with the recommendation of the Auditor General. The recommendation is being implemented.

By June 2005, Employer Accounting Unit Management, MIS, and the Policy and Training Unit will create an on-line handbook of policies and procedures that will incorporate the refund process. Training will be provided by July 2005.

The Accounting Unit Manager and two Accounting Supervisors have been hired. Accounting Unit Management has hired one accounting technician and has requested that 5 accounting technician positions be filled. The Status Unit Manager position has been posted. A Status Unit Supervisor has been hired. Management has hired six Program Service Evaluators and all vacancies have been filled.

Refresher training for experienced staff is scheduled for March 2005.

- 3. Once the Division has verified the accuracy of its pending refunds list, it should develop an effective system to notify employers of credit balances to ensure that they receive refunds in a timely manner.**

The Department concurs with the recommendation of the Auditor General. The recommendation is being implemented.

Employers will be notified of credit balances on the Tax and Wage Report, Form UC-18. This report is mailed quarterly to registered employers. The Division began requirements documentation in November 2004. The requirement specifications were completed on January 3, 2005 and sent to Management Information Systems (MIS) for action. The Division will implement this recommendation by April 2005.

- 4. To help improve its process for conducting employer audits, the Division should continue its efforts to provide ongoing training to its auditors.**

The Department concurs with the recommendation of the Auditor General. The recommendation has been implemented and is an ongoing activity.

The Division conducted refresher and TPS field audit review orientation on June 15, 2004. The Field Audit Manager now requires supervisory review of audits for all Field Audit offices.

Training and modification of audit forms for the Field Auditor's use began July 7, 2004. Revisions to audit forms will be completed by January 2005.

- 5. The Division should continue its efforts to implement an automated audit system to help ensure that audit standards and practices are followed and help allow for more efficient processing of employer audit data.**

The Department concurs with the recommendation of the Auditor General. The recommendation is being implemented.

The Division's UI Field Audit staff, MIS, and the Policy and Training Unit have been working collaboratively to develop, test, and implement an automated audit system since June 1, 2003. The Division will complete system and end user testing, training, and implementation by June 2005.