



A REPORT
TO THE
ARIZONA LEGISLATURE

Financial Audit Division

Procedural Review

Department of Economic Security—

Division of Employment and
Rehabilitation Services

March • 2013



Debra K. Davenport
Auditor General

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March 29, 2013

Clarence H. Carter, Director
Arizona Department of Economic Security
1717 West Jefferson, Site Code 010A
Phoenix, AZ 85007

Dear Mr. Carter:

We have performed a procedural review of the Department's internal controls in effect as of December 31, 2012. Our review consisted primarily of inquiries, observations, and selected tests of internal control policies and procedures, accounting records, and related documents. The review was more limited than would be necessary to give an opinion on internal controls. Accordingly, we do not express an opinion on the effectiveness of internal controls or ensure that all deficiencies in internal controls are disclosed.

We reviewed the Department of Economic Security's, Division of Employment and Rehabilitation Services' nonmonetary eligibility determinations, specifically employment separation requirements for the Unemployment Insurance benefit program.

As a result of our review, we noted certain deficiencies in internal controls that the Department's management should correct to ensure that it fulfills its responsibility to establish and maintain adequate internal controls. Our findings and recommendations concerning these deficiencies are described in the accompanying summary.

Should you have any questions concerning our procedural review, please let us know.

Sincerely,

Debbie Davenport
Auditor General

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INTRODUCTION & BACKGROUND

The Department of Economic Security, Division of Employment and Rehabilitation Services (Division), manages Arizona's Unemployment Insurance (UI) benefit program. UI program benefit payments are intended to provide financial assistance to unemployed workers who are temporarily unemployed through no fault of their own and attempting to re-enter the labor force. Arizona's UI program is based on the Federal Unemployment Tax Act (FUTA) and the Social Security Act. Each state, including Arizona, administers a separate unemployment insurance program according to its own state laws. The U.S. Secretary of Labor approves state laws under FUTA to ensure they are within the guidelines established by federal law.

Division responsible for determining UI benefits eligibility

The Division is responsible for determining eligibility for UI benefits. Each state, according to its own state laws, determines a claimant's eligibility for unemployment insurance, benefit amounts, and the length of time benefits are available. To receive UI program benefit payments, all claimants must satisfy various monetary and nonmonetary eligibility requirements. Arizona's monetary and nonmonetary eligibility requirements are outlined below.

Monetary eligibility requirements—In Arizona, a claimant must meet the monetary requirements for wages earned and time worked during an established period. Monetary eligibility is based on wages paid to the claimant by an employer who paid unemployment taxes during a one-year period called the base period. In most instances, the base period will be the first four of the last five completed quarters prior to the date the claimant first applied for UI benefits. To qualify for benefits, the claimant must have wages meeting calculated thresholds that are based on the claimant's base period earnings. If the claimant does not meet these monetary eligibility requirements, benefits will be denied.

If the claimant is determined monetarily eligible, the claimant must meet the nonmonetary eligibility requirements.

Nonmonetary eligibility requirements—Nonmonetary eligibility requirements include the claimant's reasons for separating from work, ability to work, and efforts made to seek full-time employment. A key nonmonetary eligibility requirement is the claimant's reasons for separating from work and whether those reasons qualify the claimant for UI benefits. According to Arizona Administrative Code (AAC) R6-3-50135, the Division is required to consider all relevant factors to determine whether the claimant voluntarily quit or was discharged from his/her last place of employment (see textbox for definitions).

Voluntary quit—Results from a worker's actions to end employment; separation is the worker's intended result.

Discharge—Results from an employer's actions to end employment; separation is the employer's intended result. A discharge includes:

- A layoff for lack of work, and
- A request by the employer for the worker's resignation.

Source: AAC R6-3-50135.

The Division must consider three main factors:

- The claimant's and employer's remarks and actions;
- Who initiated the separation; and
- The claimant's and employer's intentions when determining if the claimant was unemployed through no fault of his/her own.

In addition, in accordance with federal regulations, the Division must obtain or make a reasonable attempt to obtain all material facts and evidence to assess a claimant's eligibility. According to AAC R6-3-50190, evidence supporting material facts is usually in the form of oral or written statements given by the claimant, employer, and/or witnesses. Some examples of documentary evidence include the following:

- Resignation or termination letter;
- Employer attendance records and company policies;
- Disciplinary documents;
- Physician's statement;
- Contract; or
- A written statement, signed by the claimant or employer, which provides sufficient details of the facts and circumstances for separation of employment.

The Division must make an eligibility decision based on the facts and evidence provided. This determination may be appealed by either the claimant or employer.

Claimants who voluntarily quit or were discharged may be eligible for UI benefits if the reason the claimant voluntarily quit was for good cause (see textbox), or if the claimant was discharged through no fault of his/her own. Therefore, once the Division determines the separation was a voluntary quit or discharge, it must determine if the separation meets the criteria for good cause or being unemployed through no fault of the claimant's own. Further, if the Division determines the claimant is eligible for UI benefits, the claimant must still complete a weekly UI benefits claim form attesting that he/she was able and available to work and made efforts to seek full-time employment.

Commonly accepted test of good cause—A reasonable worker would have done the same thing under similar circumstances.

Source: AAC R6-3-50210.

Audit Scope

The scope of this procedural review was limited to determining if the Division's policies and procedures for nonmonetary eligibility determination, specifically employment separation requirements, were followed during calendar year 2012.¹

¹ As of the date of this report, the Arizona Legislature has passed a bill that would make changes to existing nonmonetary eligibility requirements. House Bill 2147 would provide guidance to claimants and employers regarding the documentation that is required to allow the Division to determine a claimant's eligibility for UI benefits. The bill provides some examples of appropriate documentary evidence that may be submitted. The bill has been transmitted to the Governor.

Finding 1

Division should improve UI claims instructions so claimants and employers know to provide necessary facts and evidence for Division to make better-informed initial eligibility decisions

To help the Department of Economic Security's Division of Employment and Rehabilitation Services (Division) make better-informed initial unemployment insurance (UI) eligibility decisions and help prevent more cases from entering the appeals process, it should improve its UI claims instructions so claimants and employers know to provide the necessary facts and evidence for the Division to determine UI benefits eligibility. In accordance with federal requirements, the Division must obtain or make a reasonable attempt to obtain all material facts to assess a claimant's eligibility. To ensure that the Division's decision complies with state laws, the facts and documentation should be sufficient to support the reasons for its eligibility decision. However, this review found that, despite the Division's attempts to obtain facts and evidence, claimants and employers did not always provide all relevant facts or the necessary evidence for the Division's initial UI benefits eligibility decision, which may have caused some cases to enter the appeals process. A reason for claimants and employers not providing this information may be that the Division's UI response form instructions and Web site do not inform claimants and employers that they should provide evidence to substantiate any statements made on the response form and what is considered adequate evidence in order for the Division to make an appropriate initial eligibility determination.

Claimants and employers did not always provide all relevant facts or evidence for Division's initial UI benefits eligibility decisions

According to Arizona Administrative Code (AAC) R6-3-50190, the Division must evaluate all documentary and oral evidence. For some examples of adequate documentary evidence, see Introduction & Background, page 2. However, this review found that claimants and employers did not always provide all relevant facts and evidence requested by the Division for it to make fully informed initial eligibility decisions and the appeals process may have been avoided, if they had. To determine if the Division followed its policies and procedures and attempted to obtain information, facts, and evidence from the claimant and employer to make an eligibility determination, specifically related to the employment separation requirements, auditors examined 60 claimant files from calendar year 2012. These files included claimants who received benefits payments, claims that had appeals, and claims that were initially denied. In each case the Division made an appropriate initial eligibility determination based on the information, as well as facts and evidence, if any, provided by the claimant and employer. However, despite the Division's attempts to obtain facts and evidence from claimants and employers prior to its initial UI eligibility determinations for the 60 cases evaluated, the review found that in only 32 of the cases the claimant, employer, or both parties adequately responded to the Division and provided the material facts and evidence requested. Of the 28 cases where the claimant, employer, or both parties did not respond to the Division's attempts to obtain facts and evidence to support their statements, only 10 cases were appealed. The review found that the Division may have made a different decision in 5 of these cases if the claimant, employer, or both parties had provided the requested facts and evidence to support their statements before the Division made its initial eligibility determination, as evidenced by the appeals' outcomes. These cases had the following results:

- In four cases, the employers did not provide evidence to support their statements prior to the Division's initial UI eligibility determinations, despite the Division's attempts to obtain evidence from the employers. The Division followed its policies and procedures and awarded the four claimants UI benefits since the employers did not provide the necessary evidence. However, during the appeals process the employers provided evidence that the claimants voluntarily quit, but the claimants did not provide evidence that it was for good cause and the \$5,520 in UI benefits that was already paid to the claimants was determined to be disallowed. The Division is attempting to recover the disallowed payments.
- In one case, the employer did not provide evidence to support its statement prior to the Division's initial UI eligibility determinations, despite the Division's attempts to obtain evidence from the employer. The Division followed its policies and procedures and awarded the claimant benefits because the employer did not provide evidence that the discharge was for misconduct. However, during

the appeals process, the employer provided evidence to support that the discharge was due to misconduct and the \$720 of UI benefits paid to the claimant was determined to be disallowed. The Division is attempting to recover the disallowed payments.

Had the claimants and employers provided all relevant facts and documentary evidence to support their statements before the Division made its initial UI benefits determination, the Division may have had the information needed to make a better-informed initial UI eligibility decision and the appeals process may have been avoided.

Division should better inform claimants and employers of evidence needs when responding to UI claims

A reason claimants and employers may not be providing all relevant facts and evidence for the Division's initial UI eligibility decisions is that the Division's response forms and Web site do not provide adequate instructions to claimants and employers responding to UI claims. Specifically, auditors noted that the claimant's and employer's forms do not inform them that oral or documentary evidence must be provided to support their response. The claimant response form asks claimants to answer a series of specific questions concerning their unemployment. However, it does not inform claimants to provide evidence, such as witness statements, letters of dismissal, or other documentation to support their response. Regarding employers, they may respond to UI eligibility claims information requests using either the Division's employer response form or the national UI State Information Data Exchange System (SIDES) E-Response Employer Web site, which is a Web site maintained by a third party. The employer response form and SIDES require employers to submit any separation or eligibility facts or statements that would have a bearing on a claimant's qualifications for UI benefits. The SIDES allows the employer to submit supporting documentation. However, the instructions do not inform employers that evidence must be provided to support their responses. Because the Division does not maintain SIDES and cannot alter the form or information on SIDES, the Division should inform employers of the evidence requirements through the Department of Economic Security's (Department) Web site.

Recommendations

1. To help it make better-informed initial UI eligibility decisions and help prevent more cases from entering the appeals process, the Division should inform claimants and employers of the evidence rule in AAC R6-3-50190 by:
 - a. Including a statement on its claimant and employer response forms that all evidence supporting statements made when filing a claim or responding to a separation notice should be supplied to the Division when requested, and that not submitting adequate evidence could result in unemployment benefits being erroneously approved or denied. In addition, the instructions on the forms should include examples of what is considered adequate evidence, especially in situations where written documents are not available.
 - b. Including a statement of the Department's Web site to inform employers using SIDES that all evidence supporting statements made when responding to a separation notice should be supplied to the Division when requested, and that not submitting adequate evidence could result in unemployment benefits being erroneously approved or denied. In addition, the Web site should provide examples of what is considered adequate evidence.



DEPARTMENT OF ECONOMIC SECURITY

Your Partner For A Stronger Arizona

Janice K. Brewer
Governor

Clarence H. Carter
Director

MAR 29 2013

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

Dear Ms. Davenport:

The Division concurs with the Auditor General recommendation to include additional information in its forms and online application for the reporting of separation information by employers and claimants. The Department will review existing forms and the online State Information Data Exchange System (SIDES) to determine what changes will be made to clarify the need for claimants and employers to submit supporting documentation when requested and at the time of application for benefits.

As noted in the Auditor General's report, the SIDES system is a national data system that is maintained by a third party vendor. The Department will work with the vendor to determine what changes can be made and a timeline for those changes. The hard copy forms will be reviewed and changes implemented as resources are available. Due to recent federal funding reductions, the Department's resources are limited in making changes to the automated system for the Unemployment Insurance program. The Department will work to implement the form changes by January 2014.

Sincerely,

Clarence H. Carter
Director

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DEPARTMENT RESPONSE

