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State Auditor

A Follow-up Audit Report on Unemployment Insurance Tax at the Texas Workforce Commission

September 11, 2012

Members of the Legislative Audit Committee:

The Texas Workforce Commission (Commission) fully or substantially implemented all 11 of the recommendations that auditors selected for follow-up from *An Audit Report on Unemployment Insurance Tax at the Texas Workforce Commission* (State Auditor's Office Report No. 11-042, July 2011). (See text boxes for background information on the prior audit report and implementation status definitions).

Of the six recommendations fully implemented:

- The Commission fully implemented four recommendations related to its tax audit process and system.
- The Commission fully implemented a recommendation that it properly review delinquent employer accounts before issuing a tax lien.
- The Commission fully implemented a recommendation related to its disposition of complaint referrals.

While the Commission has made significant progress in implementing the 11 prior audit recommendations selected for follow-up, it should continue its efforts to improve controls related to its delinquent employer contacts, tax audit reviews, and records retention schedule. Specifically:

- The Commission did not consistently contact delinquent employers within the time frames required by its policies and procedures.
- The Commission did not consistently ensure that tax audit results entered into its tax system were accurate and agreed with audit documentation.
- The Commission did not consistently document supervisory approval of tax audit rejections that its account examiners made. In addition, the tax examiners did not consistently include documentation in the Commission's tax system to support why they rejected a tax audit.
- The Commission had not completed updating its records retention schedule for documentation of payments from service agents.

Background Information

In July 2011, the State Auditor's Office issued *An Audit Report on Unemployment Insurance Tax at the Texas Workforce Commission* (State Auditor's Office Report No. 11-042). Auditors selected 11 of the 16 recommendations in that report for follow-up based on Texas Workforce Commission (Commission) management's original responses to the recommendations, the Commission's subsequent self-reported recommendation implementation status and implementation dates, and the level of risk.

Implementation Status Definitions

Fully Implemented - Successful development and use of a process, system, or policy to implement a prior recommendation.

Substantially Implemented - Successful development but inconsistent use of a process, system, or policy to implement a prior recommendation.

Incomplete/Ongoing - Ongoing development of a process, system, or policy to address a prior recommendation.

Not Implemented - Lack of a formal process, system, or policy to address a prior recommendation.

SAO Report No. 13-001

Table 1 provides additional details on the Commission’s implementation of prior State Auditor’s Office recommendations.

Table 1

Status of Implementation of Prior Audit Recommendations				
No.	Recommendation	Implementation Status as Reported by the Commission	Implementation Status as Determined by Auditors	Auditor Comments
1	The Commission should specify in its record retention schedule a retention period for supporting documentation of payments from service agents that is consistent with the retention period for other electronic payments’ supporting documentation, and retain supporting documentation for all service agent payments in compliance with retention schedule.	Fully Implemented	Substantially Implemented	The Commission had not completed updating the records retention schedule it filed with the Library and Archives Commission. However, it expanded the retention period from 60 days to 600 days for supporting documentation in its tax system related to payments made by service agents. Auditors were unable to verify the Commission’s compliance with that new retention period because not enough time had elapsed since the new retention period was implemented on July 14, 2011. However, auditors verified that the supporting documentation for the first two service agent payment allocation files that the Commission backed up after the reported implementation of this recommendation were still available.
2	The Commission should ensure that account examiners monitor their collection work lists and make adequate contact with delinquent employers as required.	Fully Implemented	Substantially Implemented	The Commission provided training to field tax examiners to help ensure that they monitor their collection work lists and make adequate contact with delinquent employers. However, tax examiners did not consistently make contact with delinquent employers within the time frame required by Commission policies and procedures. For 2 (7 percent) of 30 delinquent employer accounts tested, the tax examiner did not contact the delinquent employer within the required time frame.
3	The Commission should ensure that it properly reviews delinquent employer accounts when determining whether tax liens should be issued.	Fully Implemented	Fully Implemented	For all 30 delinquent employer accounts that auditors tested, the Commission had evidence that it made appropriate contacts prior to issuing a tax lien.
4	The Commission should require a review of tax audit results entered into the tax system to ensure accuracy and agreement with audit documentation.	Fully Implemented	Substantially Implemented	The Commission updated its policies and procedures and provided training to staff on the requirement for a supervisory review of tax audit results entered into its tax system. However, the Commission did not consistently follow its policies and procedures for the review of tax audits. For 4 (13 percent) of 30 tax audits that auditors tested, data in the tax system was not accurate and/or did not agree with tax audit documentation.

Status of Implementation of Prior Audit Recommendations				
No.	Recommendation	Implementation Status as Reported by the Commission	Implementation Status as Determined by Auditors	Auditor Comments
5	The Commission should retain documentation of tax audit reviews and include the documentation in the tax audit package.	Fully Implemented	Fully Implemented	The Commission provided training to its audit supervisors regarding documentation of tax audit reviews and the requirement that they record their review score and supervisor number on the audit report form. Auditors tested a sample of tax audits and determined that the Commission retained documentation of reviews in tax audit packages.
6	The Commission should develop a formal policy to clarify how approvals of exceptions to the Commission's policy on the frequency of tax audits should be approved and documented.	Fully Implemented	Fully Implemented	The Commission updated its policies and procedures to require supervisor approval and account documentation for any audit that it conducts within 36 months of a prior audit.
7	The Commission should implement controls to monitor all tax audit rejections to ensure compliance with agency policy.	Fully Implemented	Substantially Implemented	While the Commission developed policies and procedures to require supervisory approval of all audit rejections, it did not consistently follow those procedures. For 6 (33 percent) of 18 audit rejections tested, the Commission did not have evidence of supervisory review. Further, for 4 (22 percent) of the 18 audit rejections tested, the Commission did not have sufficient information in its tax system to support the audit rejection.
8	The Commission should restrict the number of tax audits that an account examiner may reject during the yearly refresh.	Fully Implemented	Substantially Implemented	The Commission implemented changes in its tax system to remove account examiners' rights to reject their entire work list of audits during the yearly refresh by requiring its Information Technology Department to perform the annual refresh. However, the Commission determined it cannot restrict the number of tax audits that an account examiner may reject during the yearly refresh because there may be valid reasons for rejections. The Commission implemented a control to monitor tax examiner rejections by requiring a supervisory review of all audits rejected in its tax system. However, auditors found that the Commission did not consistently document the supervisory reviews, as discussed in recommendation number 7 above.
9	The Commission should expand current policies and procedures to require (1) documentation of a tax audit rejection reason be created and retained for audit rejections that are not part of the annual refresh period and (2) a review of all tax audit rejections that are not part of the annual refresh period to ensure the tax audit rejections are appropriately coded and supported.	Fully Implemented	Fully Implemented	The Commission updated its policies and procedures to require an account examiner's supervisor or manager to approve and document the justification for rejecting all audits that are not part of the annual refresh.

Status of Implementation of Prior Audit Recommendations				
No.	Recommendation	Implementation Status as Reported by the Commission	Implementation Status as Determined by Auditors	Auditor Comments
10	The Commission should develop detailed procedures that fully address the recording, processing, and disposition of complaint referrals.	Fully Implemented	Fully Implemented	The Commission developed detailed procedures that fully address the recording, processing, and disposition of complaint referrals.
11	The Commission should implement input controls over its tax system to prevent account examiners from entering a total taxable wage amount that is higher than the total wages entered for tax audits.	Fully Implemented	Fully Implemented	The Commission added an edit check to its tax system that prevents account examiners from entering a total taxable wage amount that is higher than the total wages entered for tax audits.

Recommendations

The Commission should:

- Update its records retention schedule with the retention period for service agent payment allocation files and ensure that it retains those files in accordance with its records retention schedule.
- Ensure that account examiners monitor their collection work lists and make adequate contact with delinquent employers as required by its policies and procedures.
- Ensure that supervisors review tax audit results entered into its tax system for accuracy and consistency with audit documentation.
- Ensure that supervisors consistently document their approval of tax audit rejections.

The Commission agreed with the above recommendations, and its management's response is in the attachment to this letter.

Sincerely,

John Keel, CPA
 State Auditor

Attachment

cc: Members of the Texas Workforce Commission
 Mr. Andres Alcantar, Chair
 Mr. Ronald G. Congleton
 Mr. Tom Pauken
 Mr. Larry Temple, Executive Director



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Attachment

Section 1

Objective, Scope, and Methodology

Objective

The objective of this audit was to determine the implementation status of prior State Auditor's Office recommendations and evaluate whether management has taken corrective actions to address selected recommendations in *An Audit of Unemployment Insurance Tax at the Texas Workforce Commission* (State Auditor's Office Report No. 11-042, July 2011).

Scope

The scope of this audit included reviewing the implementation status of the Texas Workforce Commission's (Commission) prior audit recommendations in *An Audit of Unemployment Insurance Tax at the Texas Workforce Commission* (State Auditor's Office Report No. 11-042, July 2011). Auditors considered information reported from December 2011 through May 2012.

Methodology

The audit methodology included identifying and collecting information on the implementation of the prior audit recommendations. To determine the implementation status of the recommendations, auditors conducted interviews, reviewed the Commission's policies and procedures, and performed selected tests and other procedures.

Auditors assessed the reliability of Commission data associated with sampling tax audits, audit rejections, tax liens, and service agent payments by (1) reviewing query language used to pull data from the Commission's tax system, (2) analyzing key data elements for completeness and reasonableness, (3) interviewing Commission employees knowledgeable about the data, and (4) reviewing a prior State Auditor's Office report and audit documents related to information technology. Auditors determined that the data was sufficiently reliable for the purpose of this audit.

Information collected and reviewed included the following:

- *An Audit Report on Unemployment Insurance Tax at the Texas Workforce Commission* (State Auditor's Office Report No. 11-042, July 2011) and related audit working papers.

- Commission policies and procedures for unemployment insurance tax payments, tax audits, complaint referrals, and collection of delinquent payments.
- Unemployment insurance tax payments, tax audits, delinquent accounts, and tax liens.
- Information in the Commission's tax system.
- Commission tax audit reports and supporting documentation.
- Commission service agent payment allocation files.
- Commission field tax department training documentation.
- Commission records retention schedule.

Procedures and tests conducted included the following:

- Interviewed management and key personnel at the Commission.
- Reviewed the Commission's records retention schedule to determine whether it included a retention period for service agent payment allocation files.
- Reviewed language in the automated program the Commission used to back up service agent payment allocation files that it received electronically.
- Reviewed service agent payment allocation files to determine how long the Commission retained them.
- Tested a sample of delinquent employer accounts to determine whether the Commission complied with its policies and procedures for contacting delinquent employers.
- Tested a sample of tax liens on delinquent employer accounts to determine whether the Commission complied with its policies and procedures when placing tax liens on employers.
- Tested a sample of completed tax audits to determine whether the Commission properly reviewed and recorded the audit results in its tax system.
- Tested a sample of rejected tax audits to determine whether the Commission properly approved and documented the rejections.

- Reviewed the population of rejection codes entered into the tax system to determine whether rejections were performed by the information technology division.
- Reviewed the Commission's complaint referral procedures to determine whether the procedures fully addressed the recording, processing, and disposition of complaint referrals.
- Reviewed Commission training material and policies and procedures for the areas within the scope of this audit.
- Tested edit checks to determine whether the Commission could enter total taxable wage amounts that exceeded the total wages entered for tax audits.

Criteria used included the following:

- Texas Labor Code, Chapter 201 (Texas Unemployment Compensation Act).
- Commission policies and procedures including:
 - ♦ *Audit Systems Manual.*
 - ♦ *Field Tax Procedures Manual.*
 - ♦ *Field Tax User's Guide.*
 - ♦ *Training and Evaluation Unit User's Guide.*
- The Commission's records retention schedule.
- The Commission's field tax department training curriculum.

Project Information

Audit fieldwork was conducted from June 2012 through July 2012. We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

The following members of the State Auditor's staff performed the audit:

- Stacey Williams, CGAP (Project Manager)
- Isaac Barajas (Assistant Project Manager)

- Rachel Lynne Goldman, CPA
- Lisa M. Thompson
- Michael C. Apperley, CPA (Quality Control Reviewer)
- Ralph McClendon, CISSP, CCP, CISA (Audit Manager)

Management's Responses

Recommendation No. 1

The Commission should update its records retention schedule with the retention period for service agent payment allocation files and ensure that it retains those files in accordance with its records retention schedule.

Management Response

The Agency agrees with the audit finding and recommendation. The Records Retention Schedule pertaining to supporting documentation of payments from service agents was updated June 28, 2012 and filed with the Texas State Library and Archives Commission. The retention period is consistent with the period for supporting documentation of other electronic payments.

Recommendation No. 2

The Commission should ensure that account examiners monitor their collection work lists and make adequate contact with delinquent employers as required by its policies and procedures.

Management Response

The UI Tax Department agrees with the audit finding and recommendation. The department would like to note that the finding was due to failure by individual examiners to properly follow established procedures. The procedures themselves have been fully implemented; however, an acceptable percentage of error is to be expected. The recommendations as noted in the original review were implemented as stated, including training examiners on monitoring their collection work lists and contacting delinquent employers. One of the errors in the State Auditor's Office report was noted by the Field Supervisor and addressed prior to the State Auditor's review. The remaining error will be addressed with the accounts examiner. Additional training will be provided to both examiners.

Implementation Date: September 30, 2012

Responsible Person: Director of Tax

Recommendation No. 3

The Commission should ensure that supervisors review tax audit results entered into its tax system for accuracy and consistency with audit documentation.

Management Response

The UI Tax Department agrees with the audit finding and recommendation. The finding was due to failure by individual staff to properly follow established procedures for supervisory review of audit results entered in the tax system. The procedures themselves have been fully implemented and training was provided requiring the supervisory review. Additional training will be provided to supervisors to ensure accuracy of data entered in the tax system.

Implementation Date: September 30, 2012

Responsible Person: Director of Tax

Recommendation No. 4

The Commission should ensure that supervisors consistently document their approval of tax audit rejections.

Management Response

The UI Tax Department agrees with the audit findings and recommendation. The findings were due to failure by individual staff to properly follow established procedures. The procedures themselves have been fully implemented, including system changes that removed account examiner's rights to reject entire audit work lists, updated policies and procedures and training requiring documented supervisory review of audit rejections. Additional training will be provided to supervisors to ensure accuracy and completeness of data entered in the tax system and documentation of supervisory review.

Implementation Date: September 30, 2012

Responsible Person: Director of Tax