

Report on Audits of Financial Statements of
South Carolina Employment Security Commission
Unemployment Compensation Fund
for the years ended June 30, 2007 and 2006

State of South Carolina



Office of the State Auditor

1401 MAIN STREET, SUITE 1200
COLUMBIA, S.C. 29201

RICHARD H. GILBERT, JR., CPA
DEPUTY STATE AUDITOR

(803) 253-4160
FAX (803) 343-0723

October 1, 2007

The Honorable Mark Sanford, Governor
and
Members of the South Carolina Employment Security Commission
Unemployment Compensation Fund
Columbia, South Carolina

This report on the audit of the financial statements of the South Carolina Employment Security Commission Unemployment Compensation Fund for the fiscal year ended June 30, 2007 was issued by Scott McElveen, L.L.P., Certified Public Accountants, under contract with the South Carolina Office of the State Auditor.

If you have any questions regarding this report, please let us know.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Richard H. Gilbert, Jr." with a stylized flourish at the end.

Richard H. Gilbert, Jr., CPA
Deputy State Auditor

RHGjr/trb

South Carolina Employment Security Commission
Unemployment Compensation Fund
Notes to Financial Statements

Note 1. Summary of Significant Accounting Policies (continued)

Invested in capital assets, net of related debt – This component of net assets consists of capital assets, net of accumulated depreciation, reduced by the outstanding balances of any bonds, mortgages, notes or other borrowings that are attributable to the acquisition, construction, or improvement of those assets. If there are significant unspent related debt proceeds at year-end, the portion of the debt attributable to the unspent proceeds is not included in the calculation of invested in capital assets, net of related debt. Rather, that portion of the debt is included in the same net assets component as the unspent proceeds.

Restricted net assets – This component of net assets consists of constraints placed on net assets used through external constraints imposed by creditors (such as through debt covenants), contributors, or laws or regulations of other governments or constraints imposed by law through constitutional provisions or enabling legislation.

Unrestricted net assets – This component of net assets consists of net assets that do not meet the definition of "restricted net assets" or "invested in capital assets, net of related debt".

All of the Fund's net assets are considered to be restricted for unemployment benefit payments.

The financial statements of the Fund are prepared as an enterprise fund using the accrual basis of accounting. Revenues are recognized when earned and expenses are recognized when incurred. The Fund applies all applicable GASB pronouncements and has elected to apply only those standards issued by the Financial Accounting Standards Board ("FASB") on or before November 30, 1989 unless those pronouncements conflict or contradict GASB pronouncements.

Cash and Cash Equivalents - The amounts shown in the financial statements as cash and cash equivalents represent cash on hand with the State Treasurer, cash invested in various instruments by the State Treasurer as part of the State's internal cash management pool and cash on deposit with the U.S. Treasury and in various banks.

Most State agencies, including the Commission, participate in the State's internal cash management pool. Because the cash management pool operates as a demand deposit account, amounts invested in the pool are classified as cash and cash equivalents. The State Treasurer administers the cash management pool. The pool includes some long-term investments such as obligations of the United States and certain agencies of the United States, obligations of the State of South Carolina and certain of its political subdivisions, certificates of deposit, collateralized repurchase agreements, and certain corporate bonds. The pool operates as a demand deposit.

The State's internal cash management pool consists of a general deposit account and several special deposit accounts. The State records each fund's equity interest in the general deposit account; however, all earnings on that account are credited to the General Fund of the State. The Commission records and reports its deposits in the general deposit account at cost.

Some State Treasurer accounts are not included in the State's internal cash management pool because of restrictions on the use of the funds. For those accounts, cash equivalents include investments in short-term highly liquid securities having an initial maturity of three months or less.

South Carolina Employment Security Commission
Unemployment Compensation Fund
Notes to Financial Statements

Note 1. Summary of Significant Accounting Policies (continued)

Receivables - Receivables consist of the following:

Assessments Receivable - Unemployment tax contributions are assessed each quarter based on covered wages during the quarter. Taxes for a quarter are due on or before the end of the month following the close of the quarter. Amounts not paid by such date are considered delinquent and the Commission is required to notify employers of such tax delinquencies. If the delinquent amount is not paid within ten days thereafter, the Commission is directed to issue a warrant of execution upon real and personal property of the employer.

Benefit Overpayments Receivable - Overpayments of unemployment compensation benefits occur due to changes in facts or estimates upon which benefits were originally paid or by claimant fraud. Overpayments are due upon detection or discovery and are recovered by cash recoupments or withheld from subsequent benefits due the claimants. During 1986, the State enacted a law which provides for recovery of overpayments by the South Carolina Department of Revenue from State income tax refunds. Benefit overpayment recoupments attributable to reimbursable employers or Federal programs are due to such employers or the Federal government. Refunds are made only when there are no current benefit obligations.

Due from Reimbursable Employers - The amounts due from reimbursable employers include those amounts attributable to the actual benefits paid on behalf of certain non-profit employers to former employees.

Intergovernmental Receivables, Federal - The Federal receivable amount represents reimbursements due under various Federal grant programs in which the Commission participates. Revenues and related receivables are recognized at the time and to the extent that allowable expenditures are incurred under such programs.

Intergovernmental Receivables, State Agencies - The amounts due from the State represent unemployment benefit reimbursements due from other South Carolina state agencies.

Intergovernmental Receivables, Other States and Local Governments - The benefit reimbursement receivable from other states and local governments is based on the prorata share of wages earned by the employees to whom benefits are being paid by South Carolina in those states and localities.

Payables – Payables consist of the following:

Benefits Payable - Benefits payable represent amounts paid after year-end for unemployment compensation benefits for periods ending prior to June 30.

Contributions Payable - Contributions payable includes amounts received from employers in excess of current unemployment tax liabilities. The Commission maintains the "credits" on account to cover future tax liabilities.

Intergovernmental Payables - The amounts reported as intergovernmental payables – states represents amounts due as reimbursements to other states as reimbursements for benefits paid by those states to South Carolina claimants.

Use of Estimates - The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

South Carolina Employment Security Commission
 Unemployment Compensation Fund
 Notes to Financial Statements

Note 2. Cash and Cash Equivalents

The amounts shown as cash and cash equivalents on the balance sheet at June 30, are composed of the following:

	2007	2006
Deposits held by State Treasurer	\$ 16,366,670	\$ 2,673,495
Deposits held by U.S. Treasury	269,362,836	314,184,987
Other deposits	4,690,402	5,963,736
Total	\$ 290,419,908	\$ 322,822,218

Deposits held by State Treasurer - State law requires full collateralization of all State Treasurer bank balances. The State Treasurer must correct any deficiencies in collateral within seven days.

With respect to investments in the State's internal cash management pool, all of the State Treasurer's investments are required to be insured or registered or are investments for which the securities are held by the State or its agent in the State's name. Information pertaining to the reported amounts, fair values, and credit risk of the State Treasurer's investments is disclosed in the Comprehensive Annual Financial Report of the State of South Carolina.

Deposits held by U.S. Treasury - Under the provisions of Section 904(e) of the Social Security Act, the Secretary of the Treasury is authorized to credit to the account of each state agency, on a quarterly basis, a proportionate part of the earnings of the Unemployment Trust Fund.

Other Deposits - Custodial credit risk for deposits is the risk that in the event of a bank failure, the Fund's deposits may not be returned or the Fund will not be able to recover collateral securities in the possession of an outside party. Section 11-13-60 of the South Carolina Code of Laws requires these funds be fully insured or collateralized. All deposits of the Fund met these requirements and are either covered by federal depository insurance or collateralized with securities held by the depository financial institution's trust department or agent in the Fund's name.

Note 3. Payable to Commission

The amount shown on the financial statements as being payable to Commission represents amounts which were collected for penalties and interest and contingency assessments in tax remittances from employers. In addition, the Fund has not transferred all of the Reed Act Funds which were appropriated to the Commission as of June 30, 2007. Amounts due to the Commission as of June 30, 2007 and 2006 are as follows:

	2007	2006
Reed Act Funds	\$ 544,730	\$ 1,676,282
Contingency Assessments	2,965,707	25,228
Penalty and Interest	287,894	71,234
Total	\$ 3,798,331	\$ 1,772,744

South Carolina Employment Security Commission
Unemployment Compensation Fund
Notes to Financial Statements

Note 4. Reed Act Funds

The Commission has funds totaling approximately \$98,499,446 available under the Reed Act as of June 30, 2007. These funds are granted to the Fund from the Federal government from Federal unemployment tax collections to be used for unemployment benefits if they are needed. Upon appropriation by the State legislature and after approval of the Governor, these funds can be used for other purposes. Of these funds \$13,327,461 were appropriated by the General Assembly in prior fiscal years to partially fund the purchase of new software and information technology equipment, land acquisition, and office expansion. The \$13,327,461 was shown as a transfer from the Unemployment Compensation Fund to the Commission upon Legislative appropriation in 2002. As of June 30, 2007, \$13,282,731 of the appropriated amount under this appropriation had been transferred. During the fiscal year ended June 30, 2007, another \$500,000 appropriation was made by the General Assembly for the purchase of land. This amount is included in Transfer to Commission on the Statement of Revenues, Expenses, and Changes in Fund Balance for 2007. Of the funds appropriated, \$544,730 and \$1,676,282 had not been transferred to the Commission as of June 30, 2007 and 2006, respectively and are included in interfund payable – Commission on the Statements of Net Assets.

Note 5. Receivables

The receivable balances at June 30, and the related amounts for the allowances for uncollectibles are as follows:

	2007		
	Receivables at June 30, 2007	Allowance for Uncollectibles	Net Receivables
Assessments receivable (UI)	\$ 56,700,825	\$ 6,498,365	\$ 50,202,460
Benefit overpayments receivable:			
Basic unemployment compensation (UI)	5,903,933	2,277,913	3,626,020
Federal employees (UCFE)	27,522	13,623	13,899
Ex-servicemen (UCX)	83,100	35,577	47,523
Trade readjustment (TRA)	72,160	40,944	31,216
Emergency Unemployment Compensation (EUC)	190,603	42,522	148,081
Totals	\$ 6,277,318	\$ 2,410,579	\$ 3,866,739
Due from reimbursable employers (UI)	\$ 645,252	\$ 12,261	\$ 632,991
Intergovernmental receivables (UI):			
Local governments	\$ 1,505,341	\$ 19,645	\$ 1,485,696
Other states	\$ 1,512,839	\$ —	\$ 1,512,839
State agencies	\$ 998,273	\$ —	\$ 998,273
Federal	\$ 490,972	\$ —	\$ 490,972

South Carolina Employment Security Commission
Unemployment Compensation Fund
Notes to Financial Statements

Note 5. Receivables (continued)

	2006		
	Receivables at June 30, 2006	Allowance for Uncollectibles	Net Receivables
Assessments receivable (UI)	\$ 57,663,272	\$ 5,233,010	\$ 52,430,262
Benefit overpayments receivable:			
Basic unemployment compensation (UI)	5,374,796	1,953,111	3,421,685
Federal employees (UCFE)	20,758	7,856	12,902
Ex-servicemen (UCX)	79,460	44,077	35,383
Trade readjustment (TRA)	103,449	45,714	57,735
Emergency Unemployment Compensation (EUC)	239,160	3,546	235,614
Totals	<u>\$ 5,817,623</u>	<u>\$ 2,054,304</u>	<u>\$ 3,763,319</u>
Due from reimbursable employers (UI)	<u>\$ 996,803</u>	<u>\$ 12,233</u>	<u>\$ 984,570</u>
Intergovernmental receivables (UI):			
Local governments	<u>\$ 1,727,510</u>	<u>\$ 19,645</u>	<u>\$ 1,707,865</u>
Other states	<u>\$ 1,500,177</u>	<u>\$ —</u>	<u>\$ 1,500,177</u>
State agencies	<u>\$ 916,643</u>	<u>\$ —</u>	<u>\$ 916,643</u>
Federal	<u>\$ 226,999</u>	<u>\$ —</u>	<u>\$ 226,999</u>

Note 6. Information on Business-Type Activities

The following information is provided for incorporation in the State of South Carolina Comprehensive Annual Financial Report for the year ended June 30, 2007 and 2006:

	2007	2006
Charges for services	\$ 338,470,410	\$ 332,208,460
Interest income	12,621,783	13,718,890
Less: expenses	(389,823,906)	(364,828,359)
Net program expense	<u>(38,731,713)</u>	<u>(18,901,009)</u>
Transfers:		
Transfer to Commission	<u>(604,927)</u>	<u>—</u>
Total transfers	<u>(604,927)</u>	<u>—</u>
Change in net assets	(39,336,640)	(18,901,909)
Net assets-beginning of year	366,115,753	385,016,762
Net assets-end of year	<u>\$ 326,779,113</u>	<u>\$ 366,115,753</u>

Note 7. Subsequent Event

On July 1, 2007, a law became effective to increase the maximum weekly benefit amount that a claimant can receive from \$303 to \$326.

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*

**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***

The Office of the State Auditor and Board of Commissioners
South Carolina Employment Security Commission Unemployment Compensation Fund
Columbia, South Carolina

We have audited the accompanying financial statements of the South Carolina Employment Security Commission Unemployment Compensation Fund (the "Fund") as of and for the year ended June 30, 2007, and have issued our report thereon dated September 12, 2007. We conducted our audit in accordance with 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.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Fund's internal control over financial reporting as a basis for designing our auditing procedures 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 over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, we identified a certain deficiency in internal control over financial reporting that we consider to be a significant deficiency.

A control deficiency 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 misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the Fund's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepting accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control. We consider the deficiency described as item 2007-01 in the accompanying schedule of findings to be a significant deficiency in internal control over financial reporting.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the Fund's internal control.

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. We consider finding 2007-01 to be a material weakness.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Fund's financial statements are free of 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 no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

The Fund's response to the findings identified in our audit is described in the accompanying schedule of findings. We did not audit the Fund's response and, accordingly, we express no opinion on it.

This report is intended solely for the information and use of the Office of the State Auditor, Board of Commissioners, management of the Fund, and the elected officials and management of the State of South Carolina and is not intended to be and should not be used by anyone other than these specified parties.

Scott McElveen, L.L.P.

Columbia, South Carolina
September 12, 2007

Schedule of Findings

2007-01 – Cash Basis Accounting Records

Condition: The Fund keeps its accounting system on a cash basis of accounting, does not record any audit adjustments, and does not prepare its own financial statements.

Cause: Keeping the accounting system on a cash basis makes it more practical for the Fund to report its cash receipts and expenditures relating to its Federal programs.

Effect: The Fund must make numerous journal entries to its accounting records at year-end to adjust its records to the accrual basis of accounting. Some of the required journal entries were not made by management and adjustments were found by the independent auditors and agreed by management to be made. In addition, additional audit adjustments found by the independent auditors were not made by management which in turn caused the beginning fund balances to be incorrect in the next audit year, which in the current year resulted in an audit difference of almost \$475,000. Because management does not prepare the financial statements, errors are not detected and the independent auditors find numerous audit adjustments.

Criteria: In accordance with generally accepted accounting principles, financial statements should be prepared by management using the accrual basis of accounting.

Recommendation: The Fund's accounting system must be converted to the accrual basis of accounting at year-end for financial reporting purposes. This conversion should be performed by management so that no significant audit adjustments result from the Fund's year-end audit. If the independent auditors find audit adjustments management must understand and agree with these adjustments before they are booked and financial statements issued.

COMMISSIONERS
J. William McLeod
Becky D. Richardson
McKinley Washington, Jr.

EXECUTIVE DIRECTOR
Roosevelt T. Halley
803.737.2617



Your
onestop
for Workforce Solutions!
www.sces.org

1550 Gadsden Street
Post Office Box 995
Columbia, South Carolina 29202

September 24, 2007

Mr. Richard H. Gilbert, Jr., CPA
Deputy State Auditor
SC Office of the State Auditor
1401 Main Street, Suite 1200
Columbia, SC 29201

Dear Mr. Gilbert:

The South Carolina Employment Security Commission respectfully submits the following comments and Corrective Action Plan for the audit of the Unemployment Compensation Fund for the year ended June 30, 2007.

Name and address of the independent public accounting firm: Scott McElveen, LLP, 1441 Main Street, Suite 800, Columbia, South Carolina 29202.

Audit period: July 1, 2006 through June 30, 2007

NOTES TO FINANCIAL STATEMENTS

2007-01= Cash Basis Accounting Records

Condition: The Fund keeps its accounting system on a cash basis of accounting

Recommendation: The Fund's accounting system should be kept on the accrual basis of accounting for financial reporting purposes. Accordingly, a separate set of records should be maintained to report cash receipts and expenditures of Federal program funds.

Response: The Commission's UI Fund has monthly federal reporting requirements that are prepared using a cash basis accounting system. We feel it would be too time consuming to operate on a dual accounting system as well as not have the appropriate information monthly to record the accruals. We will work with the independent auditors to determine the appropriate accrual entries to make at year end to the trial balances to ensure that the year end financial reports are prepared on an accrual basis.

Corrective Action Plan
September 24, 2007
Page 2

If there are any questions, or if additional information is needed, please contact James Singleton,
UI Tax Director, at (803) 737-3070.

Sincerely,



Roosevelt T. Halley
Executive Director

RTH:jbw

UI-4