

South Carolina
Employment Security Commission
Columbia, South Carolina
Financial Statements
and Independent Auditors' Reports
Year Ended June 30, 2009

State of South Carolina



Office of the State Auditor

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April 2, 2010

The Honorable Mark Sanford, Governor
and
Management
South Carolina Employment Security Commission
Columbia, South Carolina

This report on the audit of the financial statements of the South Carolina Employment Security Commission for the fiscal year ended June 30, 2009, and the accompanying schedule of expenditures of federal awards as required by OMB Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations, was issued by Scott McElveen, LLP, 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.", written in a cursive style.

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

RHGjr/trb

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Independent Auditors' Report

The Office of the State Auditor and Management
South Carolina Employment Security Commission
Columbia, South Carolina

We have audited the accompanying financial statements of the governmental activities, the business-type activities, and each major fund of the South Carolina Employment Security Commission (the "Commission") as of and for the year ended June 30, 2009, which collectively comprise the Commission's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Commission's management. Our responsibility is to express opinions on these financial statements based on our audit.

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. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As described in Note 2, the financial statements of the Commission are intended to present the financial position and results of operations of only that portion of the financial reporting entity of the State of South Carolina (the "State") that is attributable to the transactions of the Commission. They do not purport to and do not present the financial position of the State as of June 30, 2009, and results of its operations, for the year then ended in conformity with accounting principles generally accepted in the United States of America and do not include other agencies, divisions, or component units of the State.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, and the major funds of the Commission as of June 30, 2009, and the respective changes in financial position and cash flows, where applicable, for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated March 31, 2010 on our consideration of the Commission's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and important for assessing the results of our audit.

The management's discussion and analysis on pages three through eight is not a required part of the basic financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise the Commission's basic financial statements. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget ("OMB") Circular A-133, *Audits of State, Local Governments, and Non-Profit Organizations* and is not a required part of the basic financial statements of the Commission. The schedule of expenditures of federal awards has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

Scott McElveen, L.L.P.

Columbia, South Carolina
March 31, 2010

MANAGEMENT'S DISCUSSION AND ANALYSIS

Management of the Commission offers readers of this narrative overview and analysis of the financial activities for the year ended June 30, 2009. Please read this information in conjunction with the Commission's financial statements and accompanying notes.

Financial Highlights

- The overall financial condition of the Commission declined during the fiscal year ended June 30, 2009. The Commission's liabilities exceeded its assets at fiscal year ending June 30, 2009 by \$285,375,829 (shown as "total net deficit"), which is a decrease of \$544,776,701 from the prior year.
- Total Unemployment Compensation benefits paid were \$1,332,327,180 and \$449,511,155 during the years ended June 30, 2009 and 2008, respectively.
- On March 30, 2010, the Governor of South Carolina signed into law Act 159 restructuring the Commission into a State cabinet agency under the Governor. The Commission merged with the Workforce Investment Act division of the South Carolina Department of Commerce to become the South Carolina Department of Employment and Workforce. The three member Board of Commissioners was replaced by an appellate board and the Governor will appoint a new Executive Director. The changes that could result from this restructuring are not fully known at this time.

Overview/Discussion of the Annual Financial Report

The discussion and analysis provides an introduction to the Commission's basic financial statements, which include the following parts: (1) entity-wide financial statements; (2) fund financial statements; and (3) notes to the financial statements.

Entity-wide Financial Statements

The entity-wide financial statements present a longer-term view of the Commission's finances as a whole, using accrual-basis accounting; the same accounting methods that most businesses use. There are two entity-wide financial statements:

Statement of Net Assets: This statement presents information on all of the Commission's assets and liabilities, both short-term (current) and long-term (non-current). The statement also reports the differences between assets and liabilities as net assets (deficit). Over time, increases or decreases in net assets may indicate whether the Commission's financial health (financial position) is strengthening or weakening. But in order to assess the Commission's overall financial health, you would also need to consider factors such as the State's economy and the condition of the entity's capital assets, such as its buildings.

Statement of Activities: This statement presents information showing how the entities overall net assets changed during the year. The statement of activities can help to show how much it costs the Commission to provide various services. It also can help show the extent to which each entity function covers its own costs through user fees, charges or grants. The net (expense) revenue column on the far right of this statement shows how much a particular function relies on operating and capital grants and contributions.

The entity-wide statements report two different kinds of activities:

Governmental Activities:

Most of the Commission's basic services are included here, such as general administration and employment and training services. Federal grants finance most of these services.

Business-type Activities:

These activities usually recover all or a significant portion of the costs of their services or goods by charging fees to customers. The South Carolina Employment Security Commission Unemployment Compensation Fund (the "Trust Fund") is included in these business-type activities. This fund collects money from several different sources but the largest source generally is federal grant revenue.

Fund Financial Statements

The fund financial statements provide detailed information about the Commission's most significant funds, not the entity as a whole. Funds are accounting devices that the Commission uses to track specific funding sources and spending for particular purposes. The Commission uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

Governmental Funds:

The Commission reports most of its basic services in governmental funds. Governmental funds account for activities that the entity reports as governmental activities in its entity-wide financial statements. These funds focus on short-term inflows and outflows of expendable resources. All of the Commission's governmental funds are accounted for in the Special Revenue Fund.

The Special Revenue Fund accounts for the various federal grants and other revenue which the Commission receives for administration purposes and special projects.

Proprietary Funds:

Proprietary funds charge customers for the services they provide to generate operating revenue. The principle operating revenue of the Commission's proprietary funds is from assessments to employers and reimbursement from the federal government for the payment of unemployment benefits. The Commission's proprietary fund is used to account for the Trust Fund.

A brief description of the fund financial statements is as follows:

The balance sheet is the statement of expendable assets which are assigned to the various governmental and proprietary funds according to the purposes for which they may or may not be used; current liabilities are assigned to the fund for which they are to be paid; and the difference between assets and liabilities is the fund balance.

The statement of revenues, expenses, and changes in fund balances presents the results of the governmental and proprietary activities over the course of the fiscal year and information as to how the net assets changed during the year.

The statement of cash flows presents changes in cash and cash equivalents resulting from operational, financing, and investing activities for the proprietary fund. This statement presents cash receipts and cash disbursements information.

Notes to the Financial Statements

The notes to the financial statements provide required disclosures and other information that is essential to a full understanding of material data provided in the statements. These notes present information about the accounting policies, significant account balances, and activities.

Entity-wide Financial Analysis

As noted earlier, net assets may serve over time as a useful indicator of a government's financial position. In the case of the Commission, liabilities exceeded assets by \$285,375,829 at the year-ended June 30, 2009. In the prior year, assets exceeded liabilities by \$259,400,872.

The Commission's net deficit can be attributed to the Trust Fund. In response to the net deficit, the Commission has taken advances from the Federal Government to provide unemployment benefits to the citizens of South Carolina.

At the end of the current fiscal year, the Commission is able to report positive net asset balances in the governmental activities which represent capital assets and unrestricted net assets.

Governmental Activities

Total assets decreased by approximately \$510,000 (-1.1%) from last year due largely to a decrease in cash balances and a decrease in the State agency revenue receivables as well as an increase in the internal balances.

There was an increase in federal grant activity, increasing revenue by approximately \$8.9 million.

South Carolina Employment Security Commission
Entity-Wide Financial Analysis
(Condensed Financial Data)
Statement of Net Assets
June 30, 2009 and 2008

	Governmental Activities		Business-Type Activities		Total	
	2009	2008	2009	2008	2009	2008
Assets:						
Current & other assets	\$ 23,637,012	\$ 21,799,166	\$ 73,899,330	\$244,786,511	\$97,536,342	\$266,585,677
Capital assets	21,088,765	23,436,636	—	—	21,088,765	23,436,636
Total assets	<u>\$ 44,725,777</u>	<u>\$ 45,235,802</u>	<u>\$ 73,899,330</u>	<u>\$244,786,511</u>	<u>\$118,625,107</u>	<u>\$290,022,313</u>
Liabilities:						
Current	\$ 11,335,457	\$ 13,181,826	\$ 46,284,800	\$15,780,029	\$57,620,257	\$28,961,855
Non-current	1,499,174	1,659,586	344,881,505	—	346,380,679	1,659,586
Total liabilities	<u>12,834,631</u>	<u>14,841,412</u>	<u>391,166,305</u>	<u>15,780,029</u>	<u>404,000,936</u>	<u>30,621,441</u>
Net assets:						
Invested in capital assets, net of related debt	20,759,788	23,009,737	—	—	20,759,788	23,009,737
Restricted for unemployment benefits	—	—	—	229,006,482	—	229,006,482
Unrestricted	11,131,358	7,384,653	(317,266,975)	—	(306,135,617)	7,384,653
Total net assets	<u>31,891,146</u>	<u>30,394,390</u>	<u>(317,266,975)</u>	<u>229,006,482</u>	<u>(285,375,829)</u>	<u>259,400,872</u>
Total liabilities & net assets	<u>\$ 44,725,777</u>	<u>\$ 45,235,802</u>	<u>\$ 73,899,330</u>	<u>\$244,786,511</u>	<u>\$118,625,107</u>	<u>\$290,022,313</u>

Statement of Activities

	Governmental Activities		Business-Type Activities		Total	
	2009	2008	2009	2008	2009	2008
Revenues:						
Program revenues:						
Charges for services	\$ 6,719,491	\$ 6,466,653	\$ 249,914,068	\$280,544,018	\$ 256,633,559	\$ 348,164,824
Operating grants & contributions	81,365,985	69,611,727	533,426,265	61,154,153	614,792,250	79,652,080
General revenues:						
Interest income	—	—	2,326,473	10,040,353	2,326,473	—
State appropriations	650,443	823,157	—	—	650,443	823,157
Total revenues	<u>88,735,919</u>	<u>76,901,537</u>	<u>785,666,806</u>	<u>351,738,524</u>	<u>874,402,725</u>	<u>428,640,061</u>
Expenses:						
Employment & training services	86,629,530	79,107,125	—	—	86,629,530	79,107,125
Unemployment compensation	—	—	1,332,327,180	449,511,155	1,332,327,180	449,511,155
Total expenses	<u>86,629,530</u>	<u>79,107,125</u>	<u>1,332,327,180</u>	<u>449,511,155</u>	<u>1,418,956,710</u>	<u>528,618,280</u>
Transfers between funds	(386,917)	—	386,917	—	—	—
Gain (loss) on sale of capital assets	(5,962)	348,220	—	—	(5,962)	348,220
Indirect cost remitted to general fund of the State	<u>(216,754)</u>	<u>(264,899)</u>	<u>—</u>	<u>—</u>	<u>(216,754)</u>	<u>(264,899)</u>
(Decrease) increase in net assets	1,496,756	(2,122,267)	(546,273,457)	(97,772,631)	(544,776,701)	(99,894,898)
Net assets – beginning	<u>30,394,390</u>	<u>32,516,657</u>	<u>229,006,482</u>	<u>326,779,113</u>	<u>259,400,872</u>	<u>359,295,770</u>
Net assets (deficit) – ending	<u>\$ 31,891,146</u>	<u>\$ 30,394,390</u>	<u>\$ (317,266,975)</u>	<u>\$229,006,482</u>	<u>\$ (285,375,829)</u>	<u>\$ 259,400,872</u>

Business-Type Activities

Statements of Net Assets:

Total assets declined by approximately \$171 million due primarily to the decline in the cash balance, as a result of the increase in unemployment benefit claims paid. Unemployment significantly increased and claimants are filing for a longer period of time, as required by the Federal government.

Net assets declined by approximately \$546 million, which is the result of the significant increase in benefits paid.

Revenues, Expenses and Changes in Net Assets:

Assessments decreased by approximately \$33 million as compared to last year due to the current recession, increased unemployment, and rate adjustments on employer accounts.

Total revenue increased by approximately \$434 million primarily due to an increase in Federal grants relating to federally funded unemployment programs.

Unemployment Compensation Benefits increased by approximately \$883 million due to increased unemployment and increases in the period of time over which benefits are paid as mandated by the Federal government.

Operating loss for 2009 was approximately \$546 million as compared to \$98 million loss for the prior year, which was due to the increase in total benefits paid, as discussed above.

Interest income decreased approximately \$8 million due to a lower amount of cash and cash equivalents.

Ending Net Assets for 2009 decreased by approximately \$546 million as compared to a \$98 million decrease for the prior year, as a result of expenditures exceeding revenues.

To date, the Trust Fund has generated substantial operating losses and has been required to use all of its cash resources to fund its operations. Due to the increasing unemployment rate and the resulting increased amount of unemployment benefits, and the increased length of time over which the benefits are paid, the Trust Fund has been required to obtain advances from the Federal Unemployment Fund of \$344,881,505 during the year ended June 30, 2009. Management plans to continue to borrow from the Federal government to fund its deficits for the foreseeable future. The Federal government has not established a maximum amount that the Trust Fund can borrow. At this time, the means of repayment of these advances has not been determined.

Financial Analysis of the Governments Funds

The Commission uses fund accounting to ensure and demonstrate compliance with finance related legal requirements.

Governmental Funds

The focus of the Commission's government fund is to provide information on near-term inflows, outflows, and balances of spendable resources. Such information is useful in assessing the Commission's financing requirements. The unreserved fund balances may serve as a useful measure of an entity's net resources available for spending at the end of the fiscal year. As of the end of the current fiscal year, the Commission's governmental fund reported combined ending fund balances of \$15,857,084, an increase of approximately \$3.7 million for the year. Approximately 95% of this total amount (\$15.0 million) constitutes unreserved fund balance, which is available for spending at the Commission's discretion. The remainder of fund balance is reserved to indicate that it is not available for new spending because they are segregated for specific future uses.

Proprietary Fund

The Commission's proprietary fund provides the same type of information found in the entity-wide financial statements, but in more detail. Unrestricted net deficit of the Commission at the end of the year amounted to approximately \$317 million. Other information concerning this fund has been addressed in the discussion of the Commission's business-type activities.

Capital Assets and Debt Administration

Primary changes in capital amounts during the year were related to construction in progress for buildings and software.

Long-term liabilities fell into two areas as follows:

Capital leases payable; and
Accrued compensated absences and related benefits.

Long-term liabilities are primarily comprised of accrued compensated absences.

More detailed information about the Commission's capital assets is presented in Note 6 to the financial statements. More detailed information about the Commission's debt administration is presented in Notes 7, 8 and 9 to the financial statements.

Economic Factors and Next Year's Rate

The Trust Fund's reserves do not meet the 2.0% requirement of law. The base rates for employer contributions will continue to include a .7% surcharge, as called for by law. Based on current economic conditions, if nothing is done to increase the Trust Fund's assessments in the coming year, the Trust Fund's net assets are projected to continue to decrease significantly. Subsequent to year-end the benefit period has been extended to a maximum of 99 weeks and the balance in the net assets of the Trust Fund has significantly decreased.

Request for Information

This financial report is designed to provide a general overview of the South Carolina Employment Security Commission's finances for all those with interest in the Commission's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the Director of Fiscal Affairs, 1550 Gadsden Street, Post Office Box 995, Columbia, South Carolina 29202.

South Carolina Employment Security Commission
Statement of Net Assets
June 30, 2009

	Governmental Activities	Business-type Activities	Totals
Assets:			
Current assets:			
Cash and cash equivalents	\$ 9,829,739	\$ 7,532,195	\$ 17,361,934
Assessments receivable, net	1,668,093	41,754,037	43,422,130
Benefit overpayments receivable, net	—	7,640,290	7,640,290
Due from reimbursable employers, net	—	1,824,889	1,824,889
Internal balances	9,468,948	(9,468,948)	—
Intergovernmental receivables, net:			
Federal	172,710	13,733,429	13,906,139
State agencies	2,202,245	2,710,676	4,912,921
Local governments	—	3,709,385	3,709,385
Other states	—	4,463,377	4,463,377
Prepaid items	295,277	—	295,277
Total current assets	<u>23,637,012</u>	<u>73,899,330</u>	<u>97,536,342</u>
Non-current assets:			
Capital assets, net of accumulated depreciation	<u>21,088,765</u>	<u>—</u>	<u>21,088,765</u>
Total assets	<u>\$ 44,725,777</u>	<u>\$ 73,899,330</u>	<u>\$ 118,625,107</u>
Liabilities:			
Current liabilities:			
Benefits payable	\$ —	\$ 7,796,013	\$ 7,796,013
Accounts payable	3,189,733	—	3,189,733
Tax withholdings payable	—	22,822,761	22,822,761
Contributions payable	—	8,806,606	8,806,606
Accrued salaries and related benefits	4,590,195	—	4,590,195
Intergovernmental payables:			
Other states	—	6,859,420	6,859,420
Current portion of capital leases payable	102,094	—	102,094
Current portion of accrued compensated absences and related benefits	<u>3,453,435</u>	<u>—</u>	<u>3,453,435</u>
Total current liabilities	<u>11,335,457</u>	<u>46,284,800</u>	<u>57,620,257</u>
Non-current liabilities:			
Advances from Federal government	—	344,881,505	344,881,505
Non-current portion of capital leases payable	226,883	—	226,883
Accrued compensated absences and related benefits	<u>1,272,291</u>	<u>—</u>	<u>1,272,291</u>
Total non-current liabilities	<u>1,499,174</u>	<u>344,881,505</u>	<u>346,380,679</u>
Total liabilities	<u>12,834,631</u>	<u>391,166,305</u>	<u>404,000,936</u>
Net Assets:			
Invested in capital assets, net of related debt	20,759,788	—	20,759,788
Unrestricted	<u>11,131,358</u>	<u>(317,266,975)</u>	<u>(306,135,617)</u>
Total net assets (deficit)	<u>31,891,146</u>	<u>(317,266,975)</u>	<u>(285,375,829)</u>
Total liabilities and net assets	<u>\$ 44,725,777</u>	<u>\$ 73,899,330</u>	<u>\$ 118,625,107</u>

The accompanying notes are an integral part of these financial statements.

South Carolina Employment Security Commission
Statement of Activities
Year ended June 30, 2009

Function/Program	Expenses	Program Revenues		Net (Expense) Revenue and Changes in Net Assets	
		Charges for Services	Operating Grants and Contributions	Governmental Activities	Business-type Activities
Governmental activities:					
Employment and training services	\$ 86,629,530	\$ 6,719,491	\$ 81,365,985	\$ 1,455,946	\$ —
Business-type activities:					
Unemployment benefits	1,332,327,180	249,914,068	533,426,265	—	(548,986,847)
Totals	<u>\$ 1,418,956,710</u>	<u>\$ 256,633,559</u>	<u>\$ 614,792,250</u>	<u>1,455,946</u>	<u>(548,986,847)</u>
General revenues:					
		Interest income		—	2,326,473
		State appropriations		650,443	—
		Loss on sale of capital assets		(5,962)	—
		Transfers		(386,917)	386,917
		Indirect costs remitted to General Fund of the State		(216,754)	—
		Total general revenue (expenses) and transfers		<u>40,810</u>	<u>2,713,390</u>
		Increase (decrease) in net assets		1,496,756	(546,273,457)
		Net assets - beginning		<u>30,394,390</u>	<u>229,006,482</u>
		Net assets (deficit) - ending		<u>\$ 31,891,146</u>	<u>\$ (317,266,975)</u>

The accompanying notes are an integral part of these financial statements.

South Carolina Employment Security Commission
Balance Sheet
Governmental Fund – Special Revenue
June 30, 2009

Assets:

Cash and cash equivalents	\$ 9,829,739
Assessments receivable, net	1,668,093
Intergovernmental receivables, net:	
Federal	172,710
State agencies	2,202,245
Interfund receivable – unemployment compensation fund	9,468,948
Prepaid items	<u>295,277</u>
 Total assets	 <u>\$ 23,637,012</u>

Liabilities and Fund Balances:

Liabilities:

Accounts payable	\$ 3,189,733
Accrued salaries and related benefits	<u>4,590,195</u>
 Total liabilities	 <u>7,779,928</u>

Fund balances:

Reserved:

Reed Act expenditures	305,000
Prepaid items	295,277
South Carolina Occupational Information Coordinating Committee	222,226
Unreserved fund balances:	
Undesignated fund balance	<u>15,034,581</u>
 Total fund balances	 <u>15,857,084</u>
 Total liabilities and fund balances	 <u>\$ 23,637,012</u>

The accompanying notes are an integral part of these financial statements.

South Carolina Employment Security Commission
Balance Sheet
Governmental Fund – Special Revenue (Continued)
June 30, 2009

Reconciliation to the Statements of Net Assets:

Fund balances – governmental funds		\$ 15,857,084
Amounts reported for governmental activities in the statement of net assets are different because:		
Liabilities that are not due and payable in the current period are not reported in the fund:		
Capital leases payable	\$ (328,977)	
Accrued compensated absences	<u>(4,725,726)</u>	(5,054,703)
Assets are capitalized and depreciated in statement of net assets and charged to expenditures in the governmental fund:		
Capital assets, net of accumulated depreciation		<u>21,088,765</u>
Net assets – governmental activities		<u>\$ 31,891,146</u>

The accompanying notes are an integral part of these financial statements.

South Carolina Employment Security Commission
Statement of Revenues, Expenditures and Changes in Fund Balances
Governmental Fund – Special Revenue
Year ended June 30, 2009

Revenues:

Employer tax contingency assessments	\$ 5,490,139
Employer tax penalties and interest	1,135,549
User fees	25,966
Intergovernmental:	
Federal	59,957,487
State of South Carolina	650,443
Local	21,408,498
Other	67,837
Total Revenues	<u>88,735,919</u>

Expenditures:

Employment and training administration	48,949,385
Contingency assessments	6,237,019
Penalties and interest	269,474
Workforce Investment Act	484,589
Trade Act Adjustment	6,314,639
Other federal programs	4,118,742
Other non-federal programs	15,405,252
Parking	60,737
Occupational Information Coordinating Committee	791,275
South Carolina Enterprise Information System	933,189
Capital outlay	787,212
Debt service:	
Principal	97,922
Interest	15,982
Total Expenditures	<u>84,465,417</u>

Excess of Expenditures Over Revenues	<u>4,270,502</u>
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Other Financing Sources (Uses):

Proceeds from sale of capital assets	900
Indirect costs remitted to General Fund of the State	(216,754)
Intergovernmental expenses - Fund	<u>(386,917)</u>

Total Other Financing Sources	<u>(602,771)</u>
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Excess of Expenditures Over Revenues and Other Financing Sources	3,667,731
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Beginning Fund Balance	<u>12,189,353</u>
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Ending Fund Balance	<u>\$ 15,857,084</u>
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The accompanying notes are an integral part of these financial statements.

South Carolina Employment Security Commission
Statement of Revenues, Expenditures and Changes in Fund Balances
Governmental Fund – Special Revenue (Continued)
Year ended June 30, 2009

Reconciliation to the Statement of Activities:

Expenditures and other financing uses over revenues and other financing sources for the governmental fund	\$ 3,667,731
Amounts reported for governmental activities in the statement of activities are different because:	
Costs of capital assets are reported as expenditures in the governmental funds and are reported as capital asset additions in the statement of net assets	787,212
Depreciation of capital assets is reported as an expense in the statement of activities	(3,390,305)
Repayments of long-term debt are reported as expenditures in the governmental funds and are reported as a reduction of liabilities in the statement of net assets	
Capital leases payable	97,922
Decrease in accrued compensated absences is reported as an increase of expenses in the statement of activities	78,974
The carrying values of capital assets disposed of are reported as expenses in the statement of activities	<u>255,222</u>
Increase in net assets	<u>\$ 1,496,756</u>

The accompanying notes are an integral part of these financial statements.

South Carolina Employment Security Commission
Statement of Net Assets
Proprietary Fund
June 30, 2009

Assets:

Current assets:

Cash and cash equivalents	\$ 7,532,195
Assessments receivable, net	41,754,037
Benefit overpayments receivable, net	7,640,290
Due from reimbursable employers, net	1,824,889
Intergovernmental receivables, net	
Local governments	3,709,385
State agencies	2,710,676
Other states	4,463,377
Federal	13,733,429
Total assets	<u>\$ 83,368,278</u>

Liabilities:

Current liabilities:

Benefits payable	\$ 7,796,013
Tax withholdings payable	22,822,761
Contributions payable	8,806,606
Intergovernmental payables:	
Other states	6,859,420
Interfund payable – Commission	9,468,948
Total current liabilities	<u>55,753,748</u>

Advances from Federal government	<u>344,881,505</u>
Total liabilities	<u>400,635,253</u>

Net (Deficit) Assets:

Unrestricted	<u>(317,266,975)</u>
Total liabilities and net assets	<u>\$ 83,368,278</u>

The accompanying notes are an integral part of these financial statements.

South Carolina Employment Security Commission
Statement of Revenues, Expenses and Changes in Fund Net Assets
Proprietary Fund
Year ended June 30, 2009

Operating Revenues:

Assessments	\$ 238,176,573
Reimbursement of unemployment compensation benefits from employers	5,088,872
Benefit overpayment recoveries	6,648,623
Intergovernmental:	
Federal	496,578,757
State agencies	7,269,078
Other states	15,925,297
Local governments	13,653,133
Total operating revenues	<u>783,340,333</u>

Operating Expenses:

Unemployment compensation benefits	1,332,327,180
Total operating expenses	<u>1,332,327,180</u>

Operating loss	<u>(548,986,847)</u>
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Non-operating Revenues (Expenses):

Interest income	2,326,473
Intergovernmental revenues – Commission	386,917
Total non-operating revenues	<u>2,713,390</u>

Changes in net assets	(546,273,457)
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Total net assets – beginning	<u>229,006,482</u>
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Total net assets (deficit) – ending	<u><u>\$ (317,266,975)</u></u>
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The accompanying notes are an integral part of these financial statements.

South Carolina Employment Security Commission
Statement of Cash Flows
Proprietary Fund
Year ended June 30, 2009

Cash flows used by operating activities:	
Cash received from assessments	\$ 249,274,102
Cash received from employers	4,083,774
Cash received from benefit overpayment recoveries	4,267,695
Cash received from Federal, state and local agencies	520,923,478
Benefits paid	(1,301,678,576)
Refund overpayment of assessments	(2,012,556)
Net cash used by operating activities	<u>(525,142,083)</u>
Cash flows provided (used) by non-capital financing activities:	
Proceeds from advances from Federal government	344,881,505
Cash received from Commission	2,125,900
Cash paid to Commission	(1,738,983)
Net cash provided by non-capital financing activities	<u>345,268,422</u>
Cash flows provided by investing activities:	
Interest received	<u>2,326,473</u>
Net cash provided by investing activities	<u>2,326,473</u>
Net decrease in cash	(177,547,188)
Cash and cash equivalents – beginning	<u>185,079,383</u>
Cash and cash equivalents – ending	<u><u>\$ 7,532,195</u></u>
Reconciliation of operating loss to net cash	
used by operating activities:	
Operating loss	\$ (548,986,847)
Net changes in assets and liabilities:	
Decrease in assessments receivable	8,283,767
Increase in Benefit overpayments receivable	(2,380,928)
Increase in Due from reimbursable employers	(1,005,098)
Increase in intergovernmental receivables:	
Local governments	(2,116,970)
State agencies	(348,103)
Other states	(3,398,268)
Federal	(13,600,839)
Increase in benefits payable	5,121,185
Increase in tax withholdings payable	21,230,215
Increase in contributions payable	991,386
Increase in interfund payable – Commission	7,762,598
Increase in intergovernmental payable:	
Other states	<u>3,305,819</u>
Net cash used by operating activities	<u><u>\$ (525,142,083)</u></u>

The accompanying notes are an integral part of these financial statements.

South Carolina Employment Security Commission

Notes to Financial Statements

Note 1. Liquidity

To date, the Commission has generated substantial operating losses and has been required to use most of its cash resources to fund its operations. Due to the increasing unemployment rate and the resulting increased amount of unemployment benefits, and the increased length of time over which the benefits are paid, the Commission has been required to obtain advances from the Federal Unemployment Fund of \$344,881,505 during the year ended June 30, 2009.

Management plans to continue to borrow from the Federal government to fund its deficits for the foreseeable future. The Federal government has not established a maximum amount that the Commission can borrow. At this time, the means of repayment of these advances has not been determined. See note 15 for further information about the advances.

Note 2. Summary of Significant Accounting Policies

Reporting Entity

The accounting policies of the Commission conform to accounting principles generally accepted in the United States of America ("GAAP") as applied to governmental units. The Governmental Accounting Standards Board ("GASB") is the accepted standard-setting body in the United States of America for establishing governmental accounting and financial reporting principles. The more significant of the Commission's accounting principles are described below.

The core of the financial reporting entity is the primary government, which has a separately elected governing body. As required by GAAP, the financial reporting entity includes both the primary government and all of its component units. Component units are legally separate organizations for which the elected officials of the primary government are financially accountable. The Commission has determined it has no component units. The primary government is the State of South Carolina. The State has determined that the Commission is a part of the primary government. An organization other than a primary government may serve as a nucleus for a reporting entity when it issues separate financial statements. That organization is identified herein as a primary entity.

The primary government or entity is financially accountable if it appoints a voting majority of the organization's governing body, including situations in which the voting majority consists of the primary entity's officials serving as required by law (e.g., employees who serve in an ex-officio capacity on the component unit's board are considered appointments by the primary entity) and (1) it is able to impose its will on that organization or (2) there is a potential for the organization to provide specific financial benefits to, or impose specific financial burdens on, the primary entity. The primary entity also may be financially accountable if an organization is fiscally dependent on it even if it does not appoint a voting majority of the board. An organization is fiscally independent if it holds all three of the following powers:

- (1) Determines its budget without another government having the authority to approve and modify that budget;
- (2) Levies taxes or sets rates or charges without approval by another government; and,
- (3) Issues bonded debt without approval by another government.

Otherwise, the organization is fiscally dependent on the primary entity that holds one or more of these powers. An organization may also be considered a component unit if the omission of its financial statements from the primary entity's financial statements would be misleading to the user of the financial statements.

South Carolina Employment Security Commission

Notes to Financial Statements

Note 2. Summary of Significant Accounting Policies (continued)

Reporting Entity (continued)

Enactment of the first South Carolina Unemployment Compensation Law followed action by Congress in passing the Social Security Act on August 14, 1935. The original South Carolina law, which established a free public employment service and a system of unemployment insurance, became effective June 6, 1936. In 1966, the name of the law was changed to the South Carolina Employment Security Law.

The Commission was created by Section 41-29-10 of the South Carolina Code of Laws to administer the South Carolina Employment Security Law which provides for the payment of unemployment insurance benefits, the collection of the unemployment tax from subject employers, and the operation of a statewide employment service. The administrative costs of the Commission are paid from grants primarily from the U.S. Department of Labor. The Unemployment Insurance Program collects taxes from employers covered by the law, and pays out unemployment benefits to unemployed workers under both state and federal law.

The Employment Service Program operates as a free labor exchange where workers and jobs are brought together from local offices located throughout the State. Workers of all skills, professions, and types, including veterans, migrant and seasonal farm workers, youth, older workers, and the disabled are placed in suitable jobs by the local State Employment Service/Job Service. Special emphasis is given to the job placement of Unemployment Insurance claimants. The Employment Service Program is affiliated with the U.S. Employment Service. In addition, the Commission maintains a comprehensive Labor Market Information Program.

The Commission is granted an annual appropriation for operating purposes as authorized by the South Carolina General Assembly. The appropriation, as enacted, becomes the legal operating budget for the Commission. The Appropriations Act authorizes expenditures from the General Fund of the State and authorizes expenditures of total funds.

The laws of the State and the policies and procedures specified by the State for State agencies are applicable to the activities of this entity. The reporting entity operates somewhat autonomously, but lacks full corporate powers. The accompanying financial statements present the financial position and results of operations and note disclosures of only those transactions of the State of South Carolina, the primary government, that are attributable to the Commission reporting entity defined above.

Governmental Funds

Governmental funds are used to account for the government's general government activities. Expendable assets are assigned to the various governmental funds according to the purposes for which they may or must be used; current liabilities are assigned to the fund from which they are to be paid; and the differences between the assets and liabilities is the fund balance. All of the Commission's governmental funds are accounted for in the special revenue fund.

The special revenue fund accounts for the various federal grants and other revenue which the Commission receives for administrative purposes and special projects. Federal grants received for unemployment compensation benefits are accounted for in the proprietary fund. The primary accounts included in the special revenue fund are as follows:

South Carolina Employment Security Commission

Notes to Financial Statements

Note 2. Summary of Significant Accounting Policies (continued)

Governmental Funds (continued)

Employment and Training Administration (“ETA Administrative”) – The division of the U.S. Department of Labor which administers Employment Services and Unemployment Insurance includes administrative funds in the Unemployment Insurance, Employment Service (“ES”), and ES Reimbursable Programs.

Employment Security Administrative Contingency Assessment (“UI Contingency Assessment”) – The assessment was established by the Legislature in 1986 in response to federal budget cuts which would have forced office closing and reductions in staff. The contingency assessment portion of the tax is accounted for in the special revenue fund which is used primarily to fund administrative costs and employment services, whereas the unemployment tax is used to fund unemployment compensation benefits in the proprietary fund.

Special Administrative Account (“UI Penalties and Interest”) – Employers who do not submit any reports required by the date such reports are due are subject to a penalty and must pay interest on unpaid contributions. The monies are transferred to the Administrative Account each month.

Unemployment Compensation Modernization Incentive Payments (“Modernization”) – This is a special transfer of funds from the Department of Labor to the Commission’s account at the Federal Unemployment Trust Fund to be used for certain administrative purposes. Administrative purposes include the improvement of unemployment compensation benefit and tax operations, including responding to increased demand for unemployment compensation and staff-assisted reemployment services for unemployment compensation claimants.

South Carolina Occupational Information Coordinating Committee (“SCOICC”) – SCOICC is a consortium of agencies mandated by the Carl D. Perkins Vocational Education Act. The Commission is one of eight South Carolina participating agencies. The SCOICC is chaired by the Executive Director of the Commission, and the Commission acts as fiscal agent. The primary function of the SCOICC is to improve coordination, communication, and cooperation in the development and use of occupational information to meet the common occupational information and data needs of the vocational education programs and the employment and training programs at national, state, and local levels. In addition, the SCOICC is charged with giving special attention to the career and educational needs of individuals involved in career decision making. The SCOICC user fees are collected from each site that participates in the statewide telephone dial-up network. The network delivers up-to-date occupational, educational, employment and career guidance information to career decision makers and job seekers. These user fees are used to pay for program expenses such as personal services, telephone connect charges, supplies, etc. SCOICC also receives an appropriation from the State of South Carolina to support its operations.

Proprietary Funds

Proprietary funds distinguish operating revenues from non-operating items. Operating revenues and expenses generally result from providing services in connection with a proprietary fund’s principle ongoing operations. The principle operating revenue of the Commission’s proprietary funds is from assessments to employers and reimbursement from the federal government for the payment of unemployment benefits. The Commission’s proprietary fund is used to account for the Trust Fund.

South Carolina Employment Security Commission

Notes to Financial Statements

Note 2. Summary of Significant Accounting Policies (continued)

Proprietary Funds (continued)

The Trust Fund accounts for all financial transactions related to employer tax contributions, employer reimbursements in lieu of tax contributions, and federal and other funds used for the payment of unemployment compensation benefits. Interest income earned on excess funds on deposit with the U.S. Treasury is retained in the fund for the payment of unemployment compensation benefits.

The Trust Fund includes the following accounts:

Basic Unemployment Compensation (“UI”) – This accounts for regular unemployment benefits paid to individuals. It is funded by quarterly tax remittances from employers within the State as well as reimbursement from other states, recoupment on overpayments, and interest received on the Trust Fund.

Unemployment Compensation for Federal Employees (“UCFE”) – This accounts for unemployment paid to ex-federal employees and is funded by the Federal government.

Unemployment Compensation for Ex-Servicemen (“UCX”) – This accounts for unemployment paid to ex-servicemen and is funded by the Federal government. It is funded by the Federal government through stimulus funds under the American Recovery and Reinvestment Act of 2009 (“ARRA”).

Trade Readjustment Allowance (“TRA”) – This fund accounts for unemployment paid to individuals who have lost their jobs due to foreign trade. These payments are made after regular UI benefits and extended benefits have been exhausted. It is funded by the Federal government.

Emergency Unemployment Compensation Tier I (“EUC”) - This provides unemployment benefits to individuals who had no rights to the regular, extended, or additional benefits under State law.

Emergency Unemployment Compensation Tier II (“EUC”) - This is an expansion of the Emergency Unemployment Compensation Tier I for individuals who had no rights to regular, extended, or additional benefits under State law. The extension for new EUC claims is through December 31, 2009 with payments on those claims ending on May 31, 2010. It is funded by the Federal government through stimulus funds under ARRA.

Alternative Trade Adjustment Assistance Program (“ATAA”) - This account provides eligible individuals over the age of 50 who obtain new employment within 26 weeks of their separation with a wage subsidy to help bridge the salary gap between their old and new employment. It is funded by the Federal government by funds other than ARRA.

Disaster Unemployment Assistance (“DUA”) - This account provides unemployment benefits to individuals who have lost their jobs due to a disaster, such as, hurricane or flood. It is funded by the Federal government by funds other than ARRA.

Extended Benefits (“EB”) - This is a permanent program to pay benefits to unemployed workers who are no longer eligible for other types of unemployment claims during times of high unemployment. This program is available when the state insured unemployment rate reaches a predetermined level and stops when the level drops below this level. The minimum time period for these benefits is a thirteen week period. This program is funded by the Federal government through stimulus funds under ARRA.

Federal Additional Compensation (“FAC”) - This provides a \$25 weekly supplement to the unemployment compensation of eligible claimants. It is funded by Federal government through stimulus funds under ARRA.

South Carolina Employment Security Commission

Notes to Financial Statements

Note 2. Summary of Significant Accounting Policies (continued)

Government-wide and Fund Financial Statements

The financial statements of the Commission are presented in accordance with GAAP applicable to state and local governmental units. The GASB is the accepted standard-setting body in the United States of America for establishing governmental accounting and financial reporting principles. The statement of activities demonstrates the degree to which the direct expenses of a given function or segment is offset by program revenues. Direct expenses are those that are clearly identifiable with a specific function or segment. Program revenues include (1) charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges provided by a given function or segment and (2) grants and contributions that are restricted to meeting the operational or capital requirements of a particular function or segment. Other items not properly included among program revenues are reported instead as general revenues.

Measurement Focus, Basis of accounting, and Financial Statement Presentation

The government-wide financial statements are reported using the economic resources measurement focus and the accrual basis method of accounting. Revenues are recorded when earned and expenses are recorded when liabilities are incurred, regardless of the timing of the cash flows.

Grants and similar items are recognized as revenues as soon as all eligibility requirements imposed by the provider have been met.

Governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis method of accounting. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the Commission considers revenues to be available if they are collected within one year of the end of the current reporting period.

Expenditures generally are recorded when liabilities are incurred, as under the accrual basis method of accounting.

The proprietary fund financial statements are reported using the accrual basis method of accounting. For the business-type activities, the Commission 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.

Non-exchange Transactions

Non-exchange transactions involving financial or capital resources are transactions in which the Commission either gives value to another party without directly receiving equal value in exchange or receives value from another party without directly giving equal value in exchange. The Commission mainly engages in voluntary non-exchange transactions. This type of transaction includes most federal grants and State Capital Improvement bond proceeds. Voluntary non-exchange transactions usually involve eligibility requirements that must be met before transactions are recognized. The eligibility requirements can include one or more of the following:

- a) The recipient has met the characteristics specified by the provider;
- b) The recipient has met the time requirements specified by the provider;
- c) The provider offers resources on a reimbursement basis and the recipient has incurred the allowable costs under the applicable program;
- d) The provider's offer of resources is contingent upon a specified action of the recipient and that action has occurred.

South Carolina Employment Security Commission

Notes to Financial Statements

Note 2. Summary of Significant Accounting Policies (continued)

Budget Policy

The Commission is granted an annual appropriation for operating purposes by the General Assembly. The appropriation as enacted becomes the legal operating budget for the Commission. The Appropriation Act authorizes expenditures from funds appropriated from the General Fund of the State and authorizes expenditures of total funds. The Total Funds column in the Appropriation Act for each individual budgetary unit authorizes expenditures from all budgeted resources. A revenue budget is not adopted for individual budgetary units. The General Assembly enacts the budget through passage of line-item appropriations by program within budgetary unit within budgetary fund category, State General Fund, or other budgeted funds. Budgetary control is maintained at the line-item level of the budgetary entity. Agencies may process disbursement vouchers in the State's budgetary accounting system only if enough cash and appropriation authorization exist.

The Commission's budget is not presented for comparison purposes because GASB 34 calls for only major special revenue funds of the State to present such information. Since the Commission is not a major special revenue fund of the State, budgetary comparison information is excluded from the basic financial statements.

Cash and Cash Equivalents

The amounts shown in the financial statements as "cash and cash equivalents" represent petty cash, 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 depository financial institutions.

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. For credit risk information pertaining to the cash management pool, see the deposits disclosure in Note 3.

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

Notes to Financial Statements

Note 2. Summary of Significant Accounting Policies (continued)

Receivables

Receivables consist primarily of the following:

Assessments Receivable

Assessments receivable includes employer tax contributions, contingency assessments and related penalties, and interest and collection charges, net of the allowance for uncollectibles.

Unemployment tax contributions are assessed each quarter based on covered wages during the quarter. Also, effective January 1, 1986, most covered employers are assessed a special contingency assessment at the rate of six one-hundredths of one percent upon all covered wages. This contingency assessment is due in the same time and manner as the unemployment tax contribution.

Taxes and contingency assessments 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.

Various penalties and interest are levied on delinquent employer tax receivables for failure to timely file quarterly wage reports and timely make the required payments.

Receivables are written off by reducing the allowance account and the corresponding receivable.

Due from Reimbursable Employers

The amounts due from reimbursable employers includes those amounts attributable to the actual benefits paid on behalf of certain non-profit and governmental employers to former employees net of the allowance for uncollectibles.

Intergovernmental Receivables

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.

The amounts due from the State in the proprietary fund represent unemployment benefit reimbursements due from other South Carolina state agencies. The benefit reimbursement receivable from other states and local governments is based on the prorata share of wages earned by the employees in those states and localities for which benefits are being paid by the Commission.

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 overpayments attributable to reimbursable employers or federal programs are due to such employers or the federal government. The Commission generally uses collection on overpayments to fund current benefit obligations. Refunds are made only when there are no current benefit obligations. Benefit overpayment receivables are recorded net of an allowance for uncollectibles.

South Carolina Employment Security Commission

Notes to Financial Statements

Note 2. Summary of Significant Accounting Policies (continued)

Capital Assets

Capital assets are recorded at cost at the date of acquisition or fair market value at the date of donation in the case of gifts. The Commission follows capitalization guidelines established by the State of South Carolina. All land is capitalized, regardless of cost. Qualifying improvements that rest in or on the land itself are recorded as depreciable land improvements. Major additions and renovations and other improvements that add to the usable space, prepare existing buildings for new uses, or extend the useful life of an existing building are capitalized.

The Commission capitalizes movable personal property with a unit value in excess of \$5,000 and a useful life in excess of two years and depreciable land improvements, buildings and improvements, and intangible assets costing in excess of \$100,000. Routine repairs and maintenance are charged to operating expenses in the year in which the expense was incurred.

Depreciation is computed using the straight-line method over the estimated useful lives of the assets, generally 20 to 50 years for buildings and improvements and land improvements and 3 to 25 years for software, machinery, equipment, furniture, and vehicles.

Benefits Payable

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

Compensated Absences

Generally all permanent full-time State employees and certain part-time employees scheduled to work at least one-half of the agency's work week are entitled to accrue and carry forward at calendar year-end up to maximums of 180 days sick leave and 45 days annual vacation leave. Upon termination of State employment, employees are entitled to be paid for accumulated unused annual vacation leave up to the maximum, but are not entitled to any payment for unused sick leave. The compensated absences liability includes accrued annual leave earned for which the employees are entitled to paid time off or payment at termination.

The Commission calculates the gross compensated absences liability based on recorded balances of unused leave. The entire unpaid liability for which the employer expects to compensate employees through paid time off or cash payments, inventoried at fiscal year-end current salary costs and the cost of the salary-related benefit payments, is recorded in the statement of net assets.

Indirect Cost

The Commission recovers indirect cost from federal funding sources based on a negotiated indirect cost agreement approved by the U.S. Department of Labor, Office of Cost Determination. The indirect cost recovered from this agreement is used to offset the administrative costs of the Commission and services provided by other State agencies. During the period July 1, 2008 through June 30, 2009, the Commission recovered approximately \$9,151,000 of indirect cost from the indirect cost agreement. Of this amount, approximately \$217,000 was remitted to the State and approximately \$8,934,000 was retained by the Commission. Indirect cost recoveries are reported as federal revenues.

South Carolina Employment Security Commission

Notes to Financial Statements

Note 2. Summary of Significant Accounting Policies (continued)

Interfund Transactions

Expenditures are initially recorded in the fund making the disbursement. However, if they are properly applicable to another fund, a reimbursement must be recorded. Reimbursements from one fund to another are treated as expenditures of the reimbursing fund and a reduction of the expenditures or expenses of the reimbursed fund. The primary transaction that falls into this category is indirect costs, which are allocated to the various funds through the Commission's cost allocation system.

Transfers from funds receiving revenues to funds through which the resources are to be expended are classified as operating transfers.

Prepaid Items

Payments made to vendors for services that will benefit periods beyond the fiscal year-end are recorded as prepaid items. Prepaid items benefiting more than one accounting period are accounted for under the consumption method and recognized as expenses/expenditures when used.

These services include maintenance contracts on data processing and office equipment, equipment rentals, professional services, software costs paid in advance, and insurance coverage.

Intergovernmental Payables – Other States

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

Contributions Payable

Contributions payable includes amounts received from employers in excess of current unemployment tax liabilities. The Commission retains the payments on account to cover future tax liabilities.

Operating and Nonoperating Revenues and Expenses

The Trust Fund distinguishes operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and delivering goods in connection with a proprietary fund's principal ongoing operations. The Trust Fund's primary operating revenues are from assessments. Operating expenses include unemployment compensation benefits paid. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

Net Assets / Fund Balances

The Commission records reservations for portions of its fund equity which are legally segregated for specific future uses or which do not represent available expendable resources and therefore, are not available for expenditures in the governmental fund balance sheet. Unreserved fund balances indicate that portion of fund equity, which is available for appropriations in future periods. If restricted and unrestricted assets are available for the same purpose, then restricted assets will be used before unrestricted assets.

South Carolina Employment Security Commission

Notes to Financial Statements

Note 2. Summary of Significant Accounting Policies (continued)

Net Assets / Fund Balances (continued)

Net assets are categorized as follows:

Invested in capital assets, net of related debt – This component of net assets consists of capital assets, net of accumulated depreciation, costs to be recovered from future revenues, and unamortized debt expense 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 – This component of net assets consists of constraints placed on net asset use 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" or "invested in capital assets, net of related debt."

At June 30, 2009, two of the Commission's reserved balances are as follows:

Reed Act – The Commission has no funds available under the Reed Act in the proprietary funds. During 2009, due to the Trust Fund becoming insolvent, all funds remaining were used to pay benefits. These funds are granted to the Trust 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, \$13,827,461 was 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 \$13,827,461 was shown as a transfer from the Trust Fund to the Special Revenue Fund upon Legislative appropriation. During fiscal year 2009, the Special Revenue Fund transferred \$2,125,900 to the Trust Fund to pay unemployment benefits and \$305,000 is shown as a reserved fund balance.

SCOICC – Pursuant to 2005 Appropriation Act Proviso 51.2, all user fees collected by the South Carolina Occupational Information Coordinating Committee through the Commission may be retained to use for operating the South Carolina Occupational Information System. All user fees not expended in the prior fiscal year were brought forward for use in the current fiscal year.

As provided by 2009 Appropriation Act Proviso 51.2, all user fees not expended in fiscal year 2009 may be carried forward to fiscal year 2009 for use in the SCOICC program. As of June 30, 2009, \$222,226 was carried forward and is reported as a reserved fund balance.

Use of Estimates

The preparation of financial statements in conformance with GAAP 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

Notes to Financial Statements

Note 3. Deposits

The amount shown as cash and cash equivalents in the statement of net assets at June 30, 2009 is composed of the following:

Cash on hand	\$ 1,500
Deposits held by State Treasurer	13,201,376
Deposits held by U.S. Treasury	27,168,948
(Bank overdraft) other deposits	(23,009,890)
Totals	<u>\$ 17,361,934</u>

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. As of June 30, 2009, all State Treasurer bank balances were fully insured or collateralized with securities held by the State or its agent in the State's name.

With respect to investments in the State's internal cash management pool, all of the State Treasurer's investments are 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 Trust Fund.

Other Deposits

Custodial credit risk for deposits is the risk that in the event of a depository financial institution's failure, the Commission's deposits may not be returned or the Commission 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 to be fully insured or collateralized. All deposits of the Commission 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 Commission's name.

The Commission does not invest in foreign securities or have transactions with foreign currency, and as a result does not have a policy for foreign currency risk.

South Carolina Employment Security Commission

Notes to Financial Statements

Note 4. Interfund Receivables/Payables

The amounts shown on the financial statements as being interfund receivables/payables represent amounts which were collected for penalties and interest and contingency assessments in tax remittances from employers and unemployment compensation modernization funds. Amounts due to the Commission as of June 30, 2009 are as follows:

Modernization funds	\$ 6,961,392
Contingency assessments	2,347,206
Penalty and interest	160,350
Total	<u>\$ 9,468,948</u>

Note 5. Receivables

The receivable balances at June 30, 2009 and the related amounts for allowances for uncollectibles are as follows:

	Receivables	Allowances for Uncollectibles	Net Receivables
Special revenue fund:			
Assessments receivable:			
Contingency	\$ 1,325,305	\$ 145,573	\$ 1,179,732
Penalty and interest	2,509,649	2,021,288	488,361
Totals	<u>\$ 3,834,954</u>	<u>\$ 2,166,861</u>	<u>\$ 1,668,093</u>
Intergovernmental receivables:			
Federal	\$ 172,710	\$ —	\$ 172,710
State agencies	2,202,245	—	2,202,245
Proprietary fund:			
Assessment receivable	49,582,635	7,828,598	41,754,037
Due from reimbursable employers	1,866,372	41,483	1,824,889
Intergovernmental receivables			
Local governments	3,746,766	37,381	3,709,385
Other states	4,463,377	—	4,463,377
State agencies	2,710,676	—	2,710,676
Federal	13,733,429	—	13,733,429
Benefit overpayments receivable:			
Basic unemployment compensation	11,284,470	4,401,681	6,882,789
Federal employees	34,464	4,396	30,068
Ex-servicemen	83,746	24,046	59,700
Trade readjustment compensation	175,704	46,934	128,770
Emergency Unemployment Compensation (EUC)	2,213,258	1,674,295	538,963
Totals	<u>\$ 13,791,642</u>	<u>\$ 6,151,352</u>	<u>\$ 7,640,290</u>

South Carolina Employment Security Commission

Notes to Financial Statements

Note 6. Capital Assets

A summary of capital assets activity for the year ended June 30, 2009 is as follows:

	Balances June 30, 2008	Increases	Decreases	Balances June 30, 2009
Capital assets not being depreciated:				
Land and land improvements	\$ 3,419,379	\$ —	\$ —	\$ 3,419,379
Construction in progress	506,349	301,939	(248,665)	559,623
Total capital assets not being depreciated	3,925,728	301,939	(248,665)	3,979,002
Other capital assets:				
Buildings and improvements	29,802,966	253,635	—	30,056,601
Equipment and furniture	7,953,957	689,521	(256,333)	8,387,145
Vehicles	331,351	52,867	(12,544)	371,674
Total other capital assets	38,088,274	996,023	(268,877)	38,815,420
Less accumulated depreciation for				
Buildings and improvements	12,857,456	743,903	—	13,601,359
Equipment and furniture	5,409,924	2,627,930	(249,470)	7,788,384
Vehicles	309,986	18,472	(12,544)	315,914
Total accumulated depreciation	18,577,366	3,390,305	(262,014)	21,705,657
Other capital assets, net	19,510,908	(2,394,282)	(6,863)	17,109,763
Total capital assets, net	\$ 23,436,636	\$ (2,092,343)	\$ (255,528)	\$ 21,088,765

The total estimated costs on buildings and improvements and other capitalized projects is approximately \$560,000 with approximately \$500 worth of costs to complete. Total outstanding commitments on projects that will not be capitalized were approximately \$34,000.

Note 7. Long-Term Liabilities

A summary of changes in long-term liabilities for the year ended June 30, 2009 is as follows:

	Balance, July 1, 2008	Additions	Reductions	Balance, June 30, 2009	Due within one year
Capital lease payable	\$ 426,899	\$ —	\$ (97,922)	\$ 328,977	\$ 102,094
Accrued compensated absences and related benefits	4,804,700	2,742,161	(2,821,135)	4,725,726	3,453,435
	\$ 5,231,599	\$ 2,742,161	\$ (2,919,057)	\$ 5,054,703	\$ 3,555,529

South Carolina Employment Security Commission

Notes to Financial Statements

Note 8. Capital Projects/Capital Improvement Bond Notes Payable

In prior years, the State authorized funds for improvements and expansion of facilities using the proceeds from State capital improvement bond notes. As capital projects are authorized by the State Budget and Control Board, the bond proceeds are allocated to the projects. Revenues from State capital improvement bonds are recorded when the expenditures are incurred. These authorized funds are requested as needed once State authorities have given approval to begin specific projects. The Commission is not obligated to repay these funds to the State until they have been drawn down. A summary of the balance of the bonds receivable from this authorization as of June 30, 2009 follows:

<u>Act</u>	<u>Total Authorized</u>	<u>Balance Authorized and Not Drawn June 30, 2009</u>
538 of 1987	<u>\$ 9,607,000</u>	<u>\$ 239,455</u>

Note 9. Leases

During 2009 the Commission paid monthly payments of \$14,066 including principal and interest at 4.18% maturing in fiscal year 2013 for two capital leases for printers. Monthly executory costs of \$4,574 are included in the \$14,066 but do not reduce the principal balance. The carrying amount of the printers totaled approximately \$359,000 as of June 30, 2009. The current year's amortization expense of approximately \$103,000 on the capitalized lease assets is included in depreciation expense. Total payments on the capital leases for the year ended June 30, 2009 were \$113,904 consisting of principal of \$97,922 and interest of \$15,982.

The Commission has entered into operating leases for office space and office equipment. All of the leases are non-cancelable leases with no purchase options and their terms are greater than one year. Payments are due on a monthly basis. Ending payment dates range from fiscal years from 2009 through 2012. Certain operating leases provide for renewal options for periods from one to five years at their fair rental value at the time of renewal. In the normal course of business, operating leases are generally renewed or replaced by other leases. The Commission is responsible for maintenance on most leased property. Rental expenditures for office space and equipment were approximately \$1,043,000 for the year ended June 30, 2009.

South Carolina Employment Security Commission

Notes to Financial Statements

Note 9. Leases (continued)

The following is a schedule by years of future minimum rental payments required under the capital lease and the noncancellable operating lease agreements with remaining terms at June 30, 2009 in excess of one year. The future minimum rental payments for the capital leases exclude the monthly executory costs.

	Year Ended June 30,	Capital Leases	Operating Leases
	2010	\$ 113,904	\$ 110,848
	2011	113,904	62,568
	2012	113,904	3,464
	2013	9,492	—
Total minimum lease payments		351,204	\$ 176,880
Less: interest		(22,227)	
Present value of minimum lease payments		\$ 328,977	

Note 10. Pension Plans

The majority of employees of the Commission are covered by a retirement plan through the South Carolina Retirements System (“SCRS”), a cost-sharing multiple-employer defined benefit pension plan administered by the Retirement Division of the State Budget and Control Board, a public employee retirement system. Generally all State employees are required to participate in and contribute to the SCRS as a condition of employment unless exempted by law as provided in section 9-1-480 of the South Carolina Code of Laws. This plan provides retirement annuity benefits as well as disability, cost of living adjustments, death, and group-life insurance benefits to eligible employees and retirees.

The Retirement Division maintains four independent defined benefit plans and issues its own publicly available Comprehensive Annual Financial Report (“CAFR”) which includes financial statements and required supplementary information. A copy of the separately issued CAFR may be obtained by writing to the Retirement Division, 202 Arbor Lake Drive, Columbia, South Carolina 29223. Furthermore, the Division and the four pension plans are included in the CAFR of the State of South Carolina.

Under the SCRS, employees are eligible for a full service retirement annuity upon reaching age 65 or completion of 28 years credited service regardless of age. The benefit formula for full benefits effective since July 1, 1989 for the SCRS is 1.82 percent of an employee’s average final compensation multiplied by the number of years of credited service. Early retirement options with reduced benefits are available as early as age 55. Employees are vested for a deferred annuity after five years service and qualify for a survivor’s benefit upon completion of 15 years credited service (five years effective January 1, 2002).

Disability annuity benefits are payable to employees totally and permanently disabled provided they have a minimum of five years credited service (this requirement does not apply if the disability is a result of a job related injury). A group-life insurance benefit equal to an employee’s annual rate of compensation is payable upon the death of an active employee with a minimum of one year of credited service.

South Carolina Employment Security Commission

Notes to Financial Statements

Note 10. Pension Plans (continued)

Effective January 1, 2001, Section 9-1-2210 of the South Carolina Code of Laws allows employees eligible for service retirement to participate in the Teacher and Employee Retention Incentive (“TERI”) Program. TERI participants may retire and begin accumulating retirement benefits on a deferred basis without terminating employment for up to five years.

Upon termination of employment or at the end of the TERI period, whichever is earlier, participants will begin receiving monthly service retirement benefits which will include any cost of living adjustments granted during the TERI period. Because participants are considered retired during the TERI period, they do not make SCRS contributions, do not earn service credit, and are ineligible to receive group life insurance benefits or disability retirement benefits. Beginning July 1, 2005, TERI participants are required to make SCRS contributions.

Effective July 1, 2006, employees participating in the SCRS were required to contribute 6.50% of all compensation. Effective July 1, 2008, the employer contribution rate became 12.74%, which included a 3.50% surcharge to fund retiree health and dental insurance coverage. The Commission’s actual contributions to the SCRS for the years ended June 30, 2009, 2008, and 2007 were approximately \$3,532,000, \$3,364,000, and \$2,886,000, respectively, and equaled the required contributions of 9.24% (excluding the surcharge) for each year. Also, the Commission paid employer group life insurance contributions of approximately \$57,000, \$56,000, and \$54,000 at the rate of .15% of compensation for the current fiscal years ended June 30, 2009, 2008, and 2007 respectively.

The South Carolina Police Officers Retirement System (“PORS”) is a cost-sharing multiple employer defined benefit public employee retirement system. Generally, all full-time employees whose principal duties are the preservation of public order or the protection or prevention and control of property destruction by fire are required to participate in and contribute to PORS as a condition of employment. This plan provides annuity benefits as well as disability and group-life insurance benefits to eligible employees and retirees. In addition, participating employers in the PORS contribute to the accidental death fund which provides annuity benefits to beneficiaries of police officers and firemen killed in the actual performance of their duties. These benefits are independent of any other retirement benefits available to the beneficiary.

Since July 1, 1988, employees participating in the PORS have been required to contribute 6.50% of all compensation. Effective July 1, 2008, the employer contribution rate became 14.15% which, as for the SCRS, included the 3.50% surcharge. The Commission’s actual contributions to the PORS for the years ended June 30, 2009, 2008 and 2007, were approximately \$12,000, \$11,000, and \$11,900, respectively, and equaled the required contributions of 10.65% (excluding the surcharge) for each year. Also, the Commission paid employer group-life insurance contributions of approximately \$220 and accidental death insurance contributions of approximately \$220 in the current fiscal year for PORS participants. The rate for each of these insurance benefits is .20% of compensation.

South Carolina Employment Security Commission

Notes to Financial Statements

Note 10. Pension Plans (continued)

Certain State employees may elect to participate in the Optional Retirement Program ("ORP"), a defined contribution plan. The ORP was established in 1987 under Title 9, Chapter 17, of the South Carolina Code of Laws. The ORP provides retirement and death benefits through the purchase of individual fixed or variable annuity contracts that are issued to and become the property of the participants. The State assumes no liability for this plan other than for payment of contributions to designated insurance companies. To elect participation in the ORP, eligible employees must irrevocably waive SCRS membership within their first 90 days of employment. Under State law, contributions to the ORP are required at the same rates as for the SCRS, 9.24% plus the retiree surcharge of 3.50% from the employer in fiscal year 2009.

For the fiscal year, total contributions requirements to the ORP were approximately \$25,000 (excluding the surcharge) from the Commission as employer and approximately \$28,000 from its employees as plan members. Employer contributions in the amount of 7.74% were remitted to the Retirement Division of the State Budget and Control Board. Also, the Commission paid employer group life insurance contributions of approximately \$650 in the current fiscal year at the rate of .15% of compensation. The balance was remitted directly to the respective annuity policy providers. The obligation for payment of benefits resides with the insurance companies.

The amounts paid by the Commission for pension, group-life benefits and accidental death benefits are reported as employer contribution expenditures within the applicable functional expenditure categories to which the related salaries are charged.

Article X, Section 16, of the South Carolina Constitution requires that all State-operated retirement systems be funded on a sound actuarial basis. Title 9 of the South Carolina Code of Laws of 1976, as amended, prescribes requirements relating to membership, benefit, and employee/employer contributions for each retirement system. Employee and employer contribution rates to SCRS (and PORS) are actuarially determined.

The surcharges to fund retiree health and dental insurance are not part of the actuarially established rates. Annual benefits, payable monthly for life, are based on length of service and on average final compensation (an annualized average of the employee's highest 12 consecutive quarters of compensation).

The SCRS do not make separate measurements of assets and pension benefit obligations for individual employers. Under Title 9 of the South Carolina Code of Laws, the Commission's liability under the plans is limited to the amount of contributions (stated as a percentage of covered payroll) established by the State Budget and Control Board. Therefore, the Commission's liability under the pension plans is limited to the amounts appropriated therefore in the South Carolina Appropriation Act and amounts from other applicable revenue sources. Accordingly, the Commission recognizes no contingent liability for unfunded costs associated with participation in the plans.

At retirement, employees participating in the SCRS or PORS may receive additional service credit for up to 90 days for accumulated unused sick leave.

South Carolina Employment Security Commission

Notes to Financial Statements

Note 11. Post-Employment Benefits Other than Pensions

a. Plan Description

In accordance with the South Carolina Code of Laws and the annual Appropriations Act, the State provides post-employment health and dental and long-term disability benefits to retired State and school district employees and their covered dependents. The Commission contributes to the Retiree Medical Plan (RMP) and the Long-term Disability Plan (LTDP), cost-sharing multiple-employer defined benefit postemployment healthcare, and long-term disability plans administered by the Employee Insurance Program (EIP), a part of the State Budget and Control Board (SBCB).

Generally, retirees are eligible for the health and dental benefits if they have established at least ten years of retirement service credit. For new hires May 2, 2008 and after, retirees are eligible for benefits if they have established twenty-five years of service for 100% employer funding and fifteen through twenty-four years of service for 50% employer funding. Benefits become effective when the former employee retires under a State retirement system. Basic long-term disability (BLTD) benefits are provided to active state, public school district and participating local government employees approved for disability.

b. Funding Policies

Section 1-11-710 of the South Carolina Code of Laws of 1976, as amended, requires these postemployment and long-term disability benefits be funded through annual appropriations by the General Assembly for active employees to the EIP and participating retirees to the SBCB, except for the portion funded through the pension surcharge and provided from the other applicable sources of the EIP, for its active employees who are not funded by State General Fund appropriations. Employers participating in the RMP are mandated by State statute to contribute at a rate assessed each year by the Office of the State Budget, 3.50% and 3.42% of annual covered payroll for 2009 and 2008, respectively. The EIP sets the employer contribution rate based on a pay-as-you-go basis. The Commission paid approximately \$1,467,000 and \$1,366,000 applicable to the surcharge included with the employer contribution for retirement benefits for the fiscal years ended June 30, 2009 and 2008, respectively. BLTD benefits are funded through a person's premium charged to State agencies, public school districts, and other participating local governments. The monthly premium per active employee paid to EIP was \$3.23 for the fiscal years ended June 30, 2009 and 2008. The Commission recorded employer contributions expenses applicable to these insurance benefits for active employees in the amount of approximately \$3,856,000 and \$3,955,000 for the years ended June 30, 2009 and 2008, respectively.

Effective May 1, 2008 the State established two trust funds through Act 195 for the purpose of funding and accounting for the employer costs of retiree health and dental insurance benefits and long-term disability insurance benefits. The South Carolina Retiree Health Insurance Trust Fund is primarily funded through the payroll surcharge. Other sources of funding include additional State appropriated dollars, accumulated EIP reserves, and income generated from investments. The Long Term Disability Insurance Trust Fund is primarily funded through investment income and employer contributions.

One may obtain complete financial statements for the benefit plans and the trust funds from Employee Insurance Program, 1201 Main Street, Suite 360, Columbia, SC 29201.

South Carolina Employment Security Commission

Notes to Financial Statements

Note 12. Deferred Compensation Plans

Several optional deferred compensation plans are available to State employees and employers of its political subdivisions. Certain employees of the Commission have elected to participate. The multiple-employer plans, created under Internal Revenue Code Section 457, 401(k), and 403(b) are administered by third parties and are not included in the Comprehensive Annual Financial Report of the State of South Carolina. Compensation deferred under the plans is placed in trust for the contributing employee. The State has no liability for losses under these plans. Employees may withdraw the current value of their contributions when they terminate State employment. Employees may also withdraw contributions prior to termination if they meet requirements specified by the applicable plan.

Note 13. Risk Management

The Commission is exposed to various risks of loss and maintains State or commercial insurance coverage for each of those risks except for automobile collision and losses on building contents.

Management believes such coverage is sufficient to preclude any significant uninsured losses for the covered risks. There were no significant reductions in insurance coverage from coverage that was in force in the prior year. Settled claims have not exceeded any of its coverage's in any of the prior three years. The Commission pays insurance premiums to certain other State agencies and commercial insurers to cover risks that may occur in normal operations. The insurers promise to pay to or on behalf of the insured for covered economic losses sustained during the policy period in accord with insurance policy and benefit program limits except for deductibles.

State management believes it is more economical to manage certain risks internally and to set aside assets for claim settlement. Several State funds accumulate assets and the State itself assumes substantially all risks for the following:

1. Claims of State employees for unemployment compensation benefits (Employment Security Commission);
2. Claims of covered employees for workers' compensation benefits for job-related illnesses or injuries (State Accident Fund);
3. Claims of covered public employees for health and dental insurance benefits (Office of Insurance Services); and
4. Claims of covered public employees for long-term disability and group-life insurance benefits (Office of Insurance Services).

Employees elect health coverage through either a health maintenance organization or through the State's self-insured plan. All of the other coverages listed above are through the applicable State self-insured plan except dependent and optional life premiums are remitted to commercial carriers.

The Commission and other entities pay premiums to the State's Insurance Reserve Fund ("IRF") which issues policies, accumulates assets to cover the risks of loss, and pays claims incurred for covered losses related to the following assets, activities, and/or events:

1. Theft of, damage to, or destruction of assets;
2. Real property;
3. Motor vehicles liability; and,
4. Torts.

South Carolina Employment Security Commission

Notes to Financial Statements

Note 13. Risk Management (continued)

The IRF is a self-insurer and purchases reinsurance to obtain certain services and specialized coverage and to limit losses in the areas of certain property and equipment and auto liability. The IRF's rates are determined actuarially.

State agencies and other entities are the primary participants in the State's Health and Disability Insurance Fund and in IRF.

The Commission obtains coverage through a commercial insurer for employee fidelity bond insurance for all employees for losses arising from theft or misappropriation, up to a maximum of \$100,000 per employee. Management believes such coverage is sufficient to preclude any significant uninsured losses for the covered risks.

The Commission has recorded insurance premium expenditures in the applicable program expenditure categories of the special revenue fund.

In management's opinion, claims losses in excess of insurance coverage for insured risks are unlikely, and if incurred, would be insignificant to the Commission's financial position. Furthermore, there is no evidence of asset impairment or other information to indicate that a loss expenditure and liability should be recorded at year-end for such risks. Therefore, no loss accrual has been recorded.

Note 14. Transactions with State Agencies

The Commission has significant transactions with the State of South Carolina and various State agencies.

The Commission was required to remit \$216,754 of indirect cost recoveries to the General Fund of the State.

Services received at no cost from State agencies include maintenance of certain accounting records and payroll and disbursement processing from the Comptroller General; check preparation and banking from the State Treasurer; legal services from the Attorney General; and records storage from the Commission of Archives and History.

Other services received at no cost from the various divisions of the State Budget and Control Board include retirement plan administration, insurance plan administration, procurement services, audit services, grant services, personnel management, assistance in the preparation of the State Budget, and approval of certain budget amendments and other centralized functions.

The Commission had financial transactions with various State agencies during the fiscal year. Significant payments were made to divisions of the State Budget and Control Board for retirement and insurance plan contributions, unemployment insurance, insurance coverage, office supplies, telephone and interagency mail. Payments were also made during the year to the State Accident Fund for worker's compensation insurance. The amounts of expenditures applicable to these related party transactions are not readily available. The Commission received \$650,443 from State appropriations during the year for expenditures of the SCOICC. The Commission recorded revenues of approximately \$7,269,078 for reimbursements of benefits paid to State employees and was due approximately \$2,710,000 for these benefits at year-end.

South Carolina Employment Security Commission

Notes to Financial Statements

Note 15. Advances from Federal Government

On December 26, 2008, the Fund began to obtain advances from the Federal government in order to pay unemployment benefits due to the exhaustion of all other funds to pay benefits. These advances were obtained due to the significant increase in unemployment benefits resulting from a significant increase in the unemployment rate in the State of South Carolina and the extension of the period by the Federal government that benefits are paid to claimants. Section 1201 of Title XII of the Social Security Act provides that an advance from the Federal Unemployment Fund to the account of a state's unemployment trust fund is allowed if the governor of a state applies for payment for any 3-month period. Only amounts actually drawn down for benefit payments must be repaid. At June 30, 2009, the outstanding balance of these advances was approximately \$345 million. Principal payments are required to begin on September 30, 2011 with interest accruing at the interest rate of 4.6375% beginning on January 1, 2011. The loan is considered noncurrent since the first principal payment is due one or more years after June 30, 2009. At this time, the means of repayment of the loan has not been determined. However, under Section 1201 of Title XII of the Social Security Act, if a balance of advances to a state is outstanding on January 1, in two consecutive years and not fully repaid prior to November 10 of the second year, employers subject to contributions under such state's unemployment compensation law will be subject to additional federal unemployment taxes determined by a formula of reductions in credit against the tax. Such credit reduction will apply beginning with the second consecutive January 1 as of the beginning of which there is a balance of such advances. The credit reductions, pursuant to Section 3302(c) (2) of FUTA, increase employers' federal tax liability each year. The amount equal to the reduced credits, excluding penalty and interest, will be applied to reduce the state's balance of advances.

Note 16. Contingencies

Federal Grants – The various programs administered by the Commission for fiscal years June 30, 2009 and years prior to that are subject to audit by the Federal grantor agencies. At the present time, amounts, if any, which may be due Federal grantors have not been determined, but the Commission believes that any such amounts in the aggregate would not have a material adverse effect on the financial position of the Commission.

Litigation – The Commission is a party to various legal proceedings arising principally in the normal course of operations. The outcome of any litigation has an element of uncertainty. Because, in the opinions of management and legal counsels, the risk of loss in excess of insurance coverage for any litigation is remote, the outcome of any litigation and claims is not expected to have a material adverse effect on the financial position of the Commission. Therefore, an estimated liability has not been recorded.

Tax Withholdings – During fiscal year 2009 the Trust Fund remitted late certain Federal and State of South Carolina tax withholdings and did not remit certain withholding taxes until after June 30, 2009. The amounts paid after June 30, 2009 are included in tax withholdings payable in the accompanying statement of net assets. The amount of penalties and interest payable to the State of South Carolina are considered immaterial and are not reflected in these financial statements. The amount of penalties and interest due to the IRS for Federal tax withholdings is unknown and management is unable to estimate this amount with any accuracy. However it is management's opinion that this amount would be immaterial to these financial statements.

South Carolina Employment Security Commission

Notes to Financial Statements

Note 17. Subsequent Events

At March 31, 2010, the balance of Advances from Federal Government is \$851,214,868.

Subsequent to year end, the extended benefits program increased the weeks of eligible unemployment compensation to ninety-nine weeks. This increase will be funded by the Federal government.

On March 30, 2010, the Governor of South Carolina signed into law Act 159 restructuring the Commission into a State cabinet agency under the Governor. The Commission merged with the Workforce Investment Act division of the South Carolina Department of Commerce to become the South Carolina Department of Employment and Workforce. The three member Board of Commissioners was replaced by an appellate board and the Governor will appoint a new Executive Director. The changes that could result from this restructuring are not fully known at this time.

**South Carolina Employment Security Commission
Schedule of Expenditures of Federal Awards**

Year Ended June 30, 2009

<u>Federal Grantor/Program Title</u>	<u>Federal CFDA Number</u>	<u>Total Federal Expenditures</u>
Direct Programs:		
U.S. Department of Labor		
Labor Force Statistics	17.002	\$ 1,074,398
Employment Service	17.207	10,950,435
Employment Service – ARRA	17.207	549,385
Unemployment Insurance	17.225	382,571,299
Unemployment Insurance - ARRA	17.225	257,421,570
Federal Unemployment Account Advance	17.225	344,881,505
Work Incentives Grant	17.266	484,590
Work Opportunity Tax Credit	17.271	160,284
Labor Certification for Alien Workers	17.272	43,486
Disabled Veterans Outreach Program (DVOP)	17.801	1,227,086
Local Veterans Employment Representative (LVER)	17.804	1,412,582
Homeless Veterans Reintegration Program	17.805	195,778
Technical Assistance/Training	17.999	208,158
		<hr/>
Totals		<u><u>\$ 1,001,180,556</u></u>

**South Carolina Employment Security Commission
Note to Schedule of Expenditures of Federal Awards**

Year Ended June 30, 2009

NOTE 1 – BASIS OF PRESENTATION

The information in the Schedule of Expenditures of Federal Awards is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations* (as amended).

Loan Program

The amount reported in the accompanying Schedule of Expenditures of Federal Awards for the loan program listed below represents federal advances during the year ended June 30, 2009 for unemployment benefits.

Federal Unemployment Account Advance (CFDA 17.225)

This loan is funded by the Federal government through the Federal Unemployment Trust Fund and is used by the Commission to pay unemployment benefits. Loans made during fiscal year 2009 were \$344,881,005 and the loan balance at June 30, 2009 was \$344,881,505.

NOTE 2 – BASIS OF ACCOUNTING

The financial information shown in the Schedule of Expenditures of Federal Awards reflects amounts recorded by the Commission during its fiscal year July 1, 2008 through June 30, 2009. This information is presented on the accrual basis of accounting.

NOTE 3 – REED ACT EXPENDITURES

During fiscal year 2009 the Commission spent \$99,558,008 of Reed Act funds which are shown in the Schedule of Expenditures of Federal Awards as part of the direct program Unemployment Insurance (CFDA 17.225).

**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 Management
South Carolina Employment Security Commission
Columbia, South Carolina

We have audited the financial statements of the governmental activities, the business-type activities, and each major fund of the South Carolina Employment Security Commission (the "Commission") as of and for the year ended June 30, 2009, which collectively comprise the Commission's basic financial statements and have issued our report thereon dated March 31, 2010. 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 Commission'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 Commission's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Commission'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 deficiencies in internal control over financial reporting that we consider to be significant deficiencies and material weaknesses.

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 Commission's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the Commission's financial statements that is more than inconsequential will not be prevented or detected by the Commission's internal control. We consider the deficiencies described as items 2009-1 to 2009-12 in the accompanying schedule of findings and responses to be significant deficiencies 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 Commission'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 deficiencies 2009-1 to 2009-6 and 2009-10 to 2009-12 described in the accompanying schedule of findings and questioned costs to be material weaknesses.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Commission'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 several instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

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

This report is intended solely for the information of the State Auditor, the Governor of the State of South Carolina, management of the Commission, and federal awarding agencies and pass-through entities 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
March 31, 2010

**Report on Compliance with Requirements
Applicable to Each Major Program and on Internal Control
Over Compliance in Accordance with OMB Circular A-133**

The Office of the State Auditor and Management
South Carolina Employment Security Commission
Columbia, South Carolina

Compliance

We have audited the compliance of South Carolina Employment Security Commission (the "Commission") with the types of compliance requirements described in the U.S. Office of Management and Budget ("OMB") Circular A-133 *Compliance Supplement* that are applicable to each of its major federal programs for the year ended June 30, 2009. The Commission's major federal programs are identified in the summary of auditors' results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs is the responsibility of the Commission's management. Our responsibility is to express an opinion on the Commission's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the Commission's compliance with those requirements and performing such other procedures as we consider necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on the Commission's compliance with those requirements.

In our opinion, the Commission complied, in all material respects, with the requirements referred to above that are applicable to its major federal programs for the year ended June 30, 2009. However, the results of our auditing procedures disclosed certain instances of noncompliance with those requirements, which are required to be reported in accordance with OMB Circular A-133 and which are described in the accompanying schedule of findings and questioned costs as items 2009-10 to 2009-12.

Internal Control Over Compliance

The management of the Commission is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered the Commission's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on

compliance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the Commission's internal control over compliance.

A *control deficiency* in the Commission's internal control over compliance 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 noncompliance with a type of compliance requirement of a federal program on a timely basis. A *significant deficiency* is a control deficiency, or combination of control deficiencies, that adversely affects the Commission's ability to administer a federal program such that there is more than a remote likelihood that noncompliance with a type of compliance requirement of a federal program that is more than inconsequential will not be prevented or detected by the Commission's internal control. We consider the deficiencies in internal control over compliance described in the accompanying schedule of findings and questioned costs as items 2009-10 to 2009-12 to be significant deficiencies.

A *material weakness* is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that material noncompliance with a type of compliance requirement of a federal program will not be prevented or detected by the entity's internal control. Our consideration of the internal control over compliance 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. However, we consider the significant deficiencies described in the accompanying schedule of findings and questioned costs as items 2009-10 to 2009-12 to be material weaknesses.

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

This report is intended solely for the information of the State Auditor, the Governor of the State of South Carolina, management of the Commission, and federal awarding agencies and pass-through entities 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
March 31, 2010

**South Carolina Employment Security Commission
Schedule of Findings and Questioned Costs**

Year Ended June 30, 2009

Section I—Summary of Auditors' Results

Financial Statements:

We have issued an unqualified opinion dated March 31, 2010 on the basic financial statements of the South Carolina Employment Security Commission.

Internal control over financial reporting:

- | | |
|--|-----|
| • Material weaknesses identified? | YES |
| • Significant deficiencies identified that are not considered to be material weaknesses? | YES |
| • Noncompliance material to financial statements noted? | NO |

Federal Awards:

We have issued an unqualified opinion dated March 31, 2010 on the South Carolina Employment Security Commission's compliance for major programs.

Internal control over major programs:

- | | |
|--|-----|
| • Material weaknesses identified? | YES |
| • Significant deficiencies identified that are not considered to be material weaknesses? | YES |
| • Any audit findings disclosed that are required to be reported in accordance with section 510(a) of Circular A-133? | YES |

Identification of Major Programs:

<u>CFDA Number</u>	<u>Name of Federal Program</u>
17.207 *	Employment Service
17.207 *	Employment Service – ARRA
17.225	Unemployment Insurance
17.225	Unemployment Insurance - ARRA
17.225	Federal Unemployment Account Advance
17.801 *	Disabled Veterans Outreach Program (DVOP)
17.804 *	Local Veterans Employment Representative (LVER)

* - part of federal awards cluster

Dollar threshold used to be distinguished between Type A and Type B Programs: \$3,000,000

Auditee qualified as low-risk auditee? NO

**South Carolina Employment Security Commission
Schedule of Findings and Questioned Costs**

Year Ended June 30, 2009

Section II- Financial Statement Findings

Significant Deficiencies Considered to be Material Weaknesses:

2009-1: Maintenance of Accounting Records in Accordance with Generally Accepted Accounting Principles

Condition:

Our audit identified certain matters attributable to the maintenance of accounting records in accordance with Generally Accepted Accounting Principles ("GAAP"). These matters include the following:

1. The Commission did not record all adjusting journal entries for its Unemployment Trust Fund (the "Trust Fund") made by the auditors in its accounting system, and therefore beginning fund balances provided to the auditors did not agree with the financial statements issued for the year ended June 30, 2008.
2. The Commission did not maintain complete trial balances for the Trust Fund or perform periodic analyses of the trial balances in order to ensure they were accurately maintained in the accounting system.
3. The Commission keeps its accounting system on a cash basis of accounting for the Trust Fund.

Cause:

The Commission's accounting staff as of June 30, 2009 did not have the skills and training necessary to perform the above functions and duties.

Effect:

The Commission's accounting records are not maintained in accordance with GAAP for the Trust Fund. The Commission must make numerous journal entries to its accounting records at year-end to adjust the Trust Fund's records to the accrual basis of accounting. Some of the required journal entries were not made by management and adjustments were proposed by the independent auditors and agreed to by management to be made. In addition, audit adjustments found by the independent auditors in prior years were not made by management which in turn caused the beginning fund balances to be incorrect in the next audit year.

Criteria:

In accordance with GAAP, the Commission's year-end financial statements for the Trust Fund should be prepared using the accrual basis of accounting.

Recommendation:

The Commission's accounting system must be converted to the accrual basis of accounting at year-end for financial reporting purposes. This conversion should be supervised by management so that no significant audit adjustments result from the year-end audit. If the independent auditors make audit adjustments, management must understand and agree with these adjustments before they are booked and financial statements issued. Staff who maintains the accounting system of the Trust Fund should make efforts to record the audit adjustments made by the auditors and reconcile the trial balance to the issued financial statements. Governmental Auditing Standards require that management take responsibility for the financial statements. Subsequent to June 30, 2009, the Commission hired a new accounting manager for the Trust Fund who has GAAP accounting skills and knowledge, which should improve the accounting processes during the year and at year-end and assist with this recommendation as well as those discussed below.

2009-2: Filing Deadline of Audited Financial Statements as Required by State of South Carolina Office of the Comptroller General

Condition:

The Commission was unable to meet the draft and final deadlines for completion of its annual financial statements of September 15 and September 30, 2009, respectively, for the Trust Fund as required by the State of South Carolina's Offices of Comptroller General and State Auditor.

Cause:

Due to an increased workload caused by significant increases in benefits paid, increased Federal funds and retirement of key personnel, the Commission's accounting staff had not been able to perform many of its monthly accounting duties on a timely basis for the Trust Fund. In many cases, cash accounts had not been reconciled for the Trust Fund since June 2008. In addition, several months of transactions had not been posted to the general ledger and balance sheet reconciliations for non-cash accounts had not been maintained during the year.

Effect:

The Commission was unable to provide the auditors with an up-to-date and adjusted trial balance to audit in a timely manner for the Trust Fund. The Commission had to hire an accounting firm and a retired accounting department employee of the Commission to assist its current accounting staff to perform the yearly close of the books, reconcile cash accounts, and post several months of transactions to the trial balance via manual journal entries. The ultimate effect of this was to cause the Trust Fund's financial statements to be issued significantly late, and as a result, the Comptroller General missed its deadline for completing the State's Comprehensive Annual Financial Report ("CAFR").

Criteria:

The State of South Carolina's Offices of Comptroller General and State Auditor dictate the deadlines for all South Carolina state agency audited financials so that they can be included in the State of South Carolina's CAFR. The draft financial statements should be issued by September 15 and the final report should be issued by September 30.

Recommendation:

The Commission must implement procedures to meet these deadlines so that the Comptroller General can issue the State's CAFR on a timely basis. Such a process must include significant planning, preparation of a timeline, and controls to make sure that the timeline is met.

*2009-3: Timeliness and Difficulty in Reconciling Cash Accounts***Condition:**

The Commission's accounting staff did not reconcile cash accounts on a timely basis during the year for the Trust Fund. As a result, these reconciliations had to be caught up at year-end, which was a very difficult and time consuming process. These reconciliations have now been performed for fiscal year 2009. However, the Commission is behind in performing the reconciliations for fiscal year 2010.

Cause:

Due to the increased workload due to a significant increase of benefits paid, increased Federal funding, and retirement of key personnel, the Commission was unable to complete reconciliations of cash accounts in a timely manner for the Trust Fund. The use of multiple personnel to reconcile individual cash accounts caused confusion and inefficiency.

Effect:

The amount of time necessary to reconcile the cash balances was significantly greater than in prior years and a large number of audit entries were necessary. The ultimate effect was the Commission could not produce the information necessary to issue the Trust Fund's financial statements on time.

Criteria:

Timely, monthly reconciliations of cash accounts are required by State Law and are a best practice of all government and non-government entities. It is a best practice for only one person to reconcile an individual cash account and each reconciliation to be reviewed by management.

Recommendation:

All cash accounts must be reconciled monthly and as soon as possible after month-end. If possible no more than one person should reconcile an individual cash account. Choosing one person to reconcile all cash accounts should reduce confusion and inefficiency. These reconciliations should also be reviewed on a timely basis by a member of management.

*2009-4: Reconciliation of Federal Debt and Other Balance Sheet Accounts to the General Ledger***Condition:**

We confirmed the balance of the Commission's debt with the Federal Government's Office of Public Debt and found that the confirmation did not agree with the Commission's accounting records. In addition, certain other balance sheet account balances per the general ledger had not been reconciled to the Trust Fund's detailed records.

Cause:

The lack of monthly reconciliations of the Federal debt account and other balance sheet accounts resulted in errors in the Commission's accounting records for the Trust Fund.

Effect:

Material adjustments were required to correct the Trust Fund's trial balance.

Criteria:

Monthly reconciliations of certain accounts are required by the STARS Policies and Procedures Manual and reconciliation of all balance sheet accounts are a best practice of all government and non-government entities. Such practice will alleviate discrepancies between actual balances and internal accounting records.

Recommendation:

All significant balance sheet accounts such as the Federal debt account should be reconciled monthly and as soon as possible after month-end. All GAAP balance sheet accounts should be reconciled at least at year-end.

2009-5: Federal and State Tax Withholdings Not Remitted Timely

Condition:

Management discovered that Federal and State tax withholdings on benefits paid were not remitted for several months during 2009 when a representative from the South Carolina Department of Revenue called to inquire why payments were not being remitted.

Cause:

A member of the Commission's accounting staff decided not to draw down the funds necessary to pay Federal and State tax withholdings on benefits paid when certain data processing reports appeared to be in error.

Effect:

The Commission was delinquent in meeting both Federal and State deadlines and therefore incurred approximately \$900,000 of penalties and \$50,000 of interest from the State of South Carolina. All penalties were forgiven by the State and approximately \$25,000 of interest has not been forgiven. The IRS has yet to determine the amount of penalties and interest due it.

Criteria:

The IRS and the State of South Carolina Department of Revenue have established deadlines for the remittance of withholdings.

Recommendation:

Management must develop procedures to prevent the untimely remittance of tax withholdings in the future. A process of management review must be put in place to ensure that no one person can delay or prevent payments in the future.

2009-6: Reconciliations of Accounting Records to Statewide Accounting and Reporting System ("STARS")

Condition:

The Commission did not perform reconciliations of certain of its accounting records for the Trust Fund to STARS, the accounting system of the State of South Carolina's Office of the Comptroller General, for several months, during fiscal year 2009, for cash, revenues, and expenditures. These reconciliations have now been prepared for fiscal year 2009, but the Commission is behind in performing these reconciliations for fiscal year 2010.

Cause:

Due to the increased workload caused by a significant increase in benefits paid, increased Federal funding, and retirement of key personnel, the Commission's accounting staff did not perform monthly reconciliations to STARS.

Effect:

The Commission was unaware of differences between its accounting system of the Trust Fund and STARS for certain of its accounts which could affect management decisions as well as financial statement balances.

Criteria:

STARS Policies and Procedures Manual requires that monthly reconciliations of certain of the Commission's cash, revenue, and expenditures accounts to STARS be performed on a timely basis after each month end.

Recommendation:

Cash, revenue, and expenditure reconciliations of the Commission's accounting records of the Trust Fund to STARS must be performed monthly on a timely basis and reviewed and approved by management.

Significant Deficiencies Not Considered to be Material Weaknesses:

2009-7: Business Contingency Plan

Condition:

The Commission has not adopted a business contingency plan for the whole organization.

Cause:

The Commission has not had the resources available to focus on preparing a business contingency plan.

Effect:

The Commission's business could be significantly interrupted or destroyed without a business contingency plan in place in case of emergency or disaster.

Criteria:

Proper business practices and internal controls indicate that all entities develop an entity-wide business contingency plan to deal with unusual circumstances.

Recommendation:

The Commission should adopt a full business contingency plan for the entire agency for emergency and disaster situations. The plan should be tested yearly to ensure the organization recovers its business functions timely under unusual conditions. Business contingency planning and testing should be an ongoing objective in the Commission's risk assessment process and should be appropriately documented. This plan could be part of the Commission's overall risk assessment program.

2009-8: Disaster Recovery Plan

Condition:

The Commission has not adopted a disaster recovery plan for the Information Technology ("IT") department.

Cause:

The Commission has not had the resources available to adopt a disaster recovery plan for the IT department.

Effect:

The IT department's operations could be interrupted or destroyed without a recovery plan in place in case of emergency or disaster.

Criteria:

Proper business practices and internal controls indicate that IT departments develop a department-wide disaster recovery plan and perform periodic testing of the plan

Recommendation:

The Commission should adopt a disaster recovery plan for the IT department. The plan should be tested at least on a yearly basis to ensure the IT department recovers servers, databases, and applications timely to preserve data integrity under unusual circumstances. The testing plan, testing result, and remediation plan should be documented and approved by the director of the IT department.

2009-9: Access to Program and Data (Physical Security and Logical Security)

Condition:

The computer room located on the second floor of the Commission's building is secured by a card reader security system. However, there is no process in place to ensure that computer room access is reviewed for appropriateness on a periodic basis. In addition, although certain application data owners perform a periodic review of user access rights for certain applications, other application data owners have not yet established a plan of periodic review of user access rights for all in-scope applications to ensure all users (including terminated employees and transfers) have appropriate access rights.

Cause:

The IT Department does not have a periodic recertification process for computer room access. In addition, the IT department does not have an adequate review process for all in-scope applications regarding user access rights.

Effect:

Unauthorized users may have access to computer room and applications to disclose, modify, and damage data. All access rights may be inappropriately restricted without periodical recertification.

Criteria:

General computer controls indicate that a formal recertification process that reviews user access listing to the computer room and all in-scope applications.

Recommendation:

The IT department management should perform periodic review of the user access listing to ensure all current users are authorized to access the computer room and other sensitive data storage locations. The IT department also needs to work with various application owners to ensure that application owners or their representative performs periodic review of user access rights for all in-scope applications, in order to be certain that all users (including terminated employees and transfers) have appropriate access rights. This joint effort and objectives should be a part of entity's strategic planning and risk assessment process.

**South Carolina Employment Security Commission
Schedule of Findings and Questioned Costs**

Year Ended June 30, 2009

Section III—Federal Award Findings and Questioned Costs

Significant Deficiencies Considered to be Material Weaknesses:

2009-10: Federal Unemployment Account (“FUA”) Loan Funding Used to Pay Extended Benefit (“EB”) Program Payroll Taxes

*Department of Labor Federal Unemployment Account Advance
CFDA No.:17.225*

Condition:

FUA loan funds were drawn down to pay the payroll taxes owed on EB payments provided to claimants. Payroll taxes on EB payments are not allowable costs under the provisions of the FUA loan and are fully reimbursable under the EB provisions of the UI program.

Cause:

Information Technology reports did not provide the accounting department with a sufficient level of detail to allow for EB withholdings to be separated from UI withholdings for purposes of drawing down the daily amounts from the Trust Fund. In addition, management did not establish and maintain internal controls sufficient to ensure that staff responsible for draw downs used the appropriate funding source for EB payroll tax payments.

Effect:

The Commission expended FUA loan proceeds on unallowable costs. The known questioned costs are \$1,790,532.

Criteria:

The provisions of the FUA loan states that loan funds may only be transferred to the Commission on an as needed basis for the payment of State unemployment compensation benefits.

Recommendation:

Management should establish and maintain controls and review the nature of all disbursements involving Federal funds to ensure that the appropriate funding for each disbursement types was obtained. Staff should also be explicitly trained as to the required funding source for every disbursement type initiated by the Commission. Management should also ensure that the proper accounting personnel are included in all discussions related to programming for Federal/State extensions prior to the implementation of such programs to ensure that required information will be readily available to properly account for the new funds.

2009-11: ETA 2112 Reports Filed with U.S. Department of Labor (“DOL”) Were Not Accurately Completed

*Department of Labor Unemployment Insurance and Unemployment Insurance - ARRA
CFDA No.:17.225*

Condition:

ETA 2112 reports completed from January 2009 through May 2009 contained inaccurate information and were amended subsequent to fiscal year-end.

Cause:

Commission staff did not contain the requisite training or ability to properly convert financial information into the format necessary for completion of the ETA 2112 reports.

Effect:

The Commission filed inaccurate financial reports with U.S. DOL and violated the reporting requirements of OMB Circular A-133.

Criteria:

OMB Circular A-133 requires that the financial reports filed by the Commission represent the actual financial operations of the entity.

Recommendation:

We recommend that management take necessary steps to ensure that all reports filed with the U.S. DOL are accurate. Staff involved who committed the original error is no longer employed with the Commission. Management has taken action to ensure that the ETA 2112 reports are accurately prepared.

2009-12: American Recovery and Reinvestment Act (“ARRA”) Funds Not Tracked Separately As Required

*Department of Labor Unemployment Insurance - ARRA
CFDA No.: 17.225*

Condition:

A portion of ARRA funds were not tracked separately from non-ARRA funds in the Commission’s accounting records during the fiscal year. ARRA funding for the extension of Extended Unemployment Compensation (“EUC”) availability and the ARRA portion of EB payments were not originally accounted for as ARRA funding throughout the fiscal year.

Cause:

The Commission’s management was not aware that the two excluded provisions noted above required separate maintenance within its accounting records. As a result, programming required to distinguish these amounts from regular EB and EUC benefits was not properly implemented.

Effect:

The Commission is not in compliance with the separate maintenance provisions of the American Recovery and Reinvestment Act (“ARRA”).

Criteria:

ARRA requires that all stimulus funds be separately tracked and accounted for separately from other Federal funds.

Recommendation:

Management must ensure that separate accounts are set up in the general ledger to track and account for each individual source of Federal funds. Management should take steps to disseminate relevant information regarding new programming and accounting requirements for new Federal program funding to the proper Commission personnel prior to the implementation of such programs.

Summary Schedule of Prior Audit Findings:

During the current year audit, we reviewed the status of corrective action taken on the findings as reported in our prior year’s reports on internal control and compliance of the Commission dated March 31, 2009, resulting from the audit of the financial statements and OMB Circular A-133 audit reports for the year ended June 30, 2008. We found that adequate corrective action was taken for all of the management letter comments, findings, and questioned costs except for item 2008-1 which is repeated above as comment 2009-1.

Appendix A

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

INTERIM EXECUTIVE DIRECTOR
Samuel R. Foster
803-737-2617



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

March 31, 2010

South Carolina Employment Security Commission
Corrective Action Plan

The South Carolina Employment Security Commission respectfully submits the following Corrective Action Plan for the audit of the year ended June 30, 2009.

Name and address of the independent public accounting firm: Scott McElveen, LLP

Audit Period: July 1, 2008 through June 30, 2009

Financial Statement Findings

2009-1: Maintenance of Accounting Records in Accordance with Generally Accepted Accounting Principles

Recommendation:

The Commission's accounting system must be converted to the accrual basis of accounting at year-end for financial reporting purposes. This conversion should be supervised by management so that no significant audit adjustments result from the year-end audit. If the independent auditors make audit adjustments, management must understand and agree with these adjustments before they are booked and financial statements issued. Staff who maintains the accounting system of the Trust Fund should make efforts to record the audit adjustments made by the auditors and reconcile the trial balance to the issued financial statements. Governmental Auditing Standards require that management take responsibility for the financial statements. Subsequent to June 30, 2009, the Commission hired a new accounting manager for the Trust Fund who has GAAP accounting skills and knowledge, which should improve the accounting processes during the year and at year-end and assist with this recommendation as well as those discussed below.

Response:

The Trust Fund's management will review, approve and post entries proposed by the independent auditors, subject to certain technical limitations. Restrictions inherent in the Trust Fund's current general ledger system currently preclude the posting of certain types of journal entries after year-end closing. The Commission's IT department has begun working on a new, all-inclusive accounting and reporting system that will address this issue. Management will book all necessary year-end journal entries, including accrual entries, required in order for the financial statement to be presented in accordance with GAAP.

When finalized, tested and implemented, the new accounting system being developed by the Commission's IT department will include the necessary functionality to generate customized reports, including a trial balance, at a given date. The accuracy of these reports will be tested by management to ensure that a usable trial balance will be available for the annual audit.

The Trust Fund is required to report its activities and balances on a cash basis for Federal reporting purposes. Therefore, the Trust Fund's internal records must be kept using the cash basis of accounting. The State of South Carolina has begun implementing a new statewide accounting system that will allow for real-time reporting of activities and balances using the accrual method of accounting; however, the Fund has not yet implemented this system due to problems encountered during the initial roll-out of the program.

The Trust Fund's management and staff will make every effort to post the proper year-end journal entries necessary to convert the Fund's books from the cash basis to the accrual basis as required by GAAP.

2009-2: Filing Deadline of Audited Financial Statements as Required by State of South Carolina Office of the Comptroller General

Recommendation:

The Commission must implement procedures to meet these deadlines so that the Comptroller General can issue the State's CAFR on a timely basis. Such a process must include significant planning, preparation of a timeline, and controls to make sure that the timeline is met.

Response:

Management is making every effort to implement procedures to ensure all required information is accurate and provided in a timely manner for audit procedures to be completed and financial statements drafted and issued within the allowable period prior to the State's deadline. The new accounting manager for the Trust Fund is currently undertaking efforts to update and automate several key processes, currently performed manually, that will assist in bringing all internal accounting and reporting processes up to date. It is management's goal to show marked improvement in the timeliness and accuracy of financial information by the end of the current fiscal year.

2009-3 Timeliness and Difficulty in Reconciling Cash Accounts

Recommendation:

All cash accounts must be reconciled monthly and as soon as possible after month-end. If possible no more than one person should reconcile an individual cash account. Choosing one person to reconcile all cash accounts should reduce confusion and inefficiency. These reconciliations should also be reviewed on a timely basis by a member of management.

Response:

As mentioned in the response to issue 2009-2, the improved accuracy and timeliness of the Trust Fund's financial information has assumed top-priority under the accounting unit's new management. Although the Trust Fund is still dealing with a significant backlog of work, including the reconciliations of cash accounts, management is making every effort to perform the reconciliations immediately following the recording of each month's transactions.

As soon as the current backlog of work has been brought up to date and the required personnel put into place, new procedures will immediately take effect requiring that one individual be responsible for reconciling every bank account to the Trust Fund's general ledger for each month, by the midpoint of the following month, to be reviewed by management. Management will ensure that the individual responsible for performing bank reconciliations has the required knowledge and resources to perform these procedures, on time, without exception. The same individual will also be required to represent an understanding of the legal requirements and best-practices related to this process, as well as the ramifications for any deviation from policy resulting from negligence on his or her part.

2009-4: Reconciliation of Federal Debt and Other Balance Sheet Accounts to the General Ledger

Recommendation:

All significant balance sheet accounts such as the Federal debt account should be reconciled monthly and as soon as possible after month-end. All GAAP balance sheet accounts should be reconciled at least at year-end.

Response:

As mentioned before, new systems, policies, and procedures are currently being developed by the Trust Fund's management to enable the accurate and timely performance of general accounting duties during the normal course of business. As soon as the Trust Fund's employees have brought all reconciliations up to date, these policies will take immediate effect. Staff with requisite accounting knowledge will be individually assigned to perform timely reconciliations of the Federal debt and all other balance sheet accounts. The level of knowledge required and responsibility assumed will be considered individually for each account, and staff members will be assigned accordingly based on their level of experience and their history of performance within the organization.

Again, the importance of the accurate, timely performance of these duties will be emphasized as they are assigned, along with the ramifications for any unreasonable exceptions to the unit's policies and procedures.

2009-5: Federal and State Tax Withholdings Not Remitted Timely

Recommendation:

Management must develop procedures to prevent the untimely remittance of tax withholdings in the future. A process of management review must be put in place to ensure that no one person can delay or prevent payments in the future.

Response:

As emphasized by our auditors in their report, the criteria for the remittance of Federal and State withholdings to the taxing authority is clearly defined by the IRS and SC Department of Revenue. The Trust Fund's management will not tolerate any unreasonable delay or failure in drawing-down and remitting these funds within the specified time periods.

Problems obtaining accurate withholding figures due to data processing issues should be addressed immediately by accounting personnel and should assume top priority in all cases. Management continues to notify the Commission's data processing department of all known issues that caused (or could cause) delays in determining proper remittance amounts. Accounting staff assigned to calculate, draw-down and remit withholdings will be assigned such duties in accordance with their history of performance, understanding of specific procedures, and knowledge of the legal requirements and ramifications for non-compliance.

2009-6: Reconciliations of Accounting Records to Statewide Accounting and Reporting System ("STARS")

Recommendation:

Cash, revenue, and expenditure reconciliations of the Commission's accounting records of the Trust Fund to STARS must be performed monthly on a timely basis and reviewed and approved by management.

Response:

Policies and procedures for monthly reconciliation of the Trust Fund's general ledger to STARS will be clearly outlined by management to prevent any delays in performance. Employees of the Trust Fund's accounting unit will be specifically assigned to reconcile cash, revenues and expenditures to STARS based on their level of experience and responsibility.

2009-7: Business Contingency Plan

Recommendation:

The Commission should adopt a full business contingency plan for the entire agency for emergency and disaster situations. The plan should be tested yearly to ensure the organization recovers its business functions timely under unusual conditions. Business contingency planning and testing should be an ongoing objective in the Commission's risk assessment process and should be appropriately documented. This plan could be part of the Commission's overall risk assessment program.

Response:

The Commission's IT department has received a Supplemental Budget Request (SBR) to develop a UI IT Contingency Plan which will address this deficiency.

2009-8: Disaster Recovery Plan

Recommendation:

The Commission should adopt a disaster recovery plan for the IT department. The plan should be tested at least on a yearly basis to ensure the IT department recovers servers, databases, and applications timely to preserve data integrity under unusual circumstances. The testing plan, testing result, and remediation plan should be documented and approved by the director of the IT department.

Response:

The Commission's IT department has received a Supplemental Budget Request (SBR) to develop a UI IT Contingency Plan which will address the disaster recovery deficiency.

2009-9: Access to Program and Data (Physical Security and Logical Security)

Recommendation:

The IT department management should perform periodic review of the user access listing to ensure all current users are authorized to access the computer room and other sensitive data storage locations. The IT department also needs to work with various application owners to ensure that application owners or their representative performs periodic review of user access rights for all in-scope applications, in order to be certain that all users (including terminated employees and transfers) have appropriate access rights. This joint effort and objectives should be a part of entity's strategic planning and risk assessment process.

Response:

The IT department management will develop and implement a plan for periodically reviewing computer room access and management will work with application owners to develop and implement a process for periodic review of user access rights. This will be addressed in the Commission's IT annual planning.

2009-10: Federal Unemployment Account ("FUA") Loan Funding Used to Pay Extended Benefit ("EB") Program Payroll Taxes; CFDA #17.225

Recommendation:

Management should establish and maintain controls and review the nature of all disbursements involving Federal funds to ensure that the appropriate funding for each disbursement types was obtained. Staff should also be explicitly trained as to the required funding source for every disbursement type initiated by the Commission. Management should also ensure that the proper accounting personnel are included in all discussions related to programming for Federal/State extensions prior to the implementation of such programs to ensure that required information will be readily available to properly account for the new funds.

Response:

Management for the Trust Fund identified this error in January 2010. As of the date of this response, an IT report that previously omitted details required to properly fund and account for the EB withholdings has been fixed. Management is currently working to make the proper adjustments to the Trust Fund's EB account and the FUA loan per specific guidance provided by the U.S Department of Labor.

The Control Accounts manager is now being included in UI staff meetings in an effort to ensure that programming for new programs and Federal extensions will meet the requirements for accurate and proper accounting and reporting.

2009-11: ETA 2112 Reports Filed with US. Department of Labor ("DOL") Were Not Accurately Completed; CFDA #17.225

Recommendation:

We recommend that management take necessary steps to ensure that all reports filed with the U.S. DOL are accurate. Staff involved who committed the original error is no longer employed with the Commission. Management has taken action to ensure that the ETA 2112 reports are accurately prepared.

Response:

New management for the Trust Fund continues its efforts to automate processes needed to generate the ETA-2112 data. These processes were previously performed manually which led to errors that were discovered and amended subsequent to year-end.

2009-12: American Recovery and Reinvestment Act ("ARRA") Funds Not Tracked Separately As Required; CFDA #17.225

Recommendation:

Management must ensure that separate accounts are set up in the general ledger to track and account for each individual source of Federal funds. Management should take steps to disseminate relevant information regarding new programming and accounting requirements for new Federal program funding to the proper Commission personnel prior to the implementation of such programs.

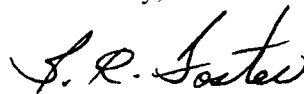
Response:

Management for the Trust Fund properly accounted for Federal Additional Unemployment Compensation (FAUC) in separate fund ledgers during the year under audit. Since receiving guidance on the additional ARRA classifications of EUC and EB, the accounting unit has properly established separate fund ledgers, both on the State level and internally, for these portions of benefits payments.

As noted in the response to issue *2009-11*, the Control Accounts manager is now being included in UI staff meetings. In addition, management will continue to work closely with the U.S. Department of Labor in supporting the Commission's efforts to properly account for all sources of funding in accordance with prescribed regulations.

If you have any questions, or if additional information is needed, please contact Charles D. Reeves, Director of Finance, at (803) 737-2584.

Sincerely,

A handwritten signature in black ink, appearing to read "S. R. Foster".

Samuel R. Foster
Interim Executive Director

SRF/vnb

REF: AS-4