

**GOVERNMENT OF THE DISTRICT OF COLUMBIA  
OFFICE OF THE INSPECTOR GENERAL**

**DISTRICT OF COLUMBIA  
UNEMPLOYMENT COMPENSATION FUND**

**Financial Statements and  
Management's Discussion and Analysis  
(with Independent Auditors' Report Thereon)  
Years Ended September 30, 2007, and 2006**



**CHARLES J. WILLOUGHBY  
INSPECTOR GENERAL**

**GOVERNMENT OF THE DISTRICT OF COLUMBIA**  
**Office of the Inspector General**

Inspector General



May 14, 2008

The Honorable Adrian M. Fenty  
Mayor of the District of Columbia  
Mayor's Correspondence Unit, Suite 221  
John A. Wilson Building  
1350 Pennsylvania Avenue, N.W.  
Washington, D.C. 20004

The Honorable Vincent C. Gray  
Chairman  
Council of the District of Columbia  
John A. Wilson Building, Suite 504  
1350 Pennsylvania Avenue, N.W.  
Washington, D.C. 20004

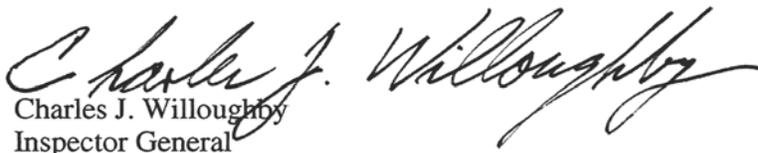
Dear Mayor Fenty and Chairman Gray:

As part of our contract for the audit of the District of Columbia's general purpose financial statements for fiscal year (FY) 2007, Thompson, Cobb, Bazilio & Associates, PC (TCBA) submitted the enclosed final report on the District of Columbia Unemployment Compensation Fund (Fund).

TCBA opined that the financial statements present fairly, in all material respects, the financial position of the Fund, for the year ended September 30, 2007, and 2006, in conformity with accounting principles generally accepted in the United States of America. In accordance with *Government Accounting Standards*, TCBA has issued its report on consideration of the Fund's internal control over financial reporting and on TCBA's tests of the Fund's compliance with certain provisions of laws, regulations, contracts, grant agreements, and other matters.

If you have questions or need additional information, please contact William J. DiVello, Assistant Inspector General for Audits, at (202) 727-2540.

Sincerely,

  
Charles J. Willoughby  
Inspector General

Enclosure

CJW/ws

cc: See Distribution List

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Mayor Fenty and Chairman Gray  
FY 2007 and 2006 Unemployment Compensation  
Fund Financial Statements, Management's  
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Auditor's Report Thereon)  
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May 14, 2008  
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**GOVERNMENT OF THE  
DISTRICT OF COLUMBIA  
UNEMPLOYMENT COMPENSATION FUND**

**FINANCIAL STATEMENTS AND MANAGEMENT'S  
DISCUSSION AND ANALYSIS  
(WITH INDEPENDENT AUDITOR'S REPORT THEREON)  
YEARS ENDED SEPTEMBER 30, 2007 AND 2006**

**THOMPSON, COBB, BAZILIO & ASSOCIATES, P.C.**  
*Certified Public Accountants and Management, Systems and Financial Consultants*

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**GOVERNMENT OF THE  
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UNEMPLOYMENT COMPENSATION FUND  
FINANCIAL STATEMENTS AND MANAGEMENT'S  
DISCUSSION AND ANALYSIS  
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YEARS ENDED SEPTEMBER 30, 2007 AND 2006**

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**THOMPSON, COBB, BAZILIO & ASSOCIATES, PC**  
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### Independent Auditor's Report

To the Mayor, Members of the Council and the  
Inspector General of the Government of the District of Columbia

We have audited the accompanying statements of net assets of the District of Columbia Unemployment Compensation Fund (the Fund) as of September 30, 2007 and 2006 and the related statements of revenues, expenses, and change in net assets and cash flows for the years then ended. These financial statements are the responsibility of the Fund's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits 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 of America. 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 audits provide a reasonable basis for our opinion.

As discussed in Note 1, these financial statements present only the financial activity of the Fund and are not intended to present the financial position and results of operations of the Government of the District of Columbia taken as a whole.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Fund, as of September 30, 2007 and 2006, and the results of its operations and its cash flows for the years 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 February 27, 2008 on our consideration of the Fund's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and 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 should be considered in assessing the results of our audit.

The management's discussion and analysis on pages 3 through 7 is not a required part of the basic financial statements, but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

Washington, DC  
February 27, 2008

*Thompson, Cofl, Bazilio & Associates, P.C.*

**GOVERNMENT OF THE DISTRICT OF COLUMBIA  
UNEMPLOYMENT COMPENSATION FUND  
MANAGEMENT'S DISCUSSION AND ANALYSIS  
September 30, 2007**

This section of the annual financial report of the District of Columbia Unemployment Compensation Fund (“the Fund”) presents our discussion and analysis of the financial performance of the Fund during the fiscal year ended September 30, 2007. This discussion has been prepared by management and should be read in conjunction with the financial statements and note disclosures. The financial statements, disclosures and discussion and analysis are the responsibility of management.

**Financial Highlights**

At September 30, 2007, the Fund’s net assets were \$375.1 million, an increase of \$27.2 million from September 30, 2006. See *Table 1: Overall Financial Position for the Years Ended September 30, 2007 and 2006*. This 7.8% increase was primarily the result of an increase in cash. The cash balance in the Fund is restricted for future payments.

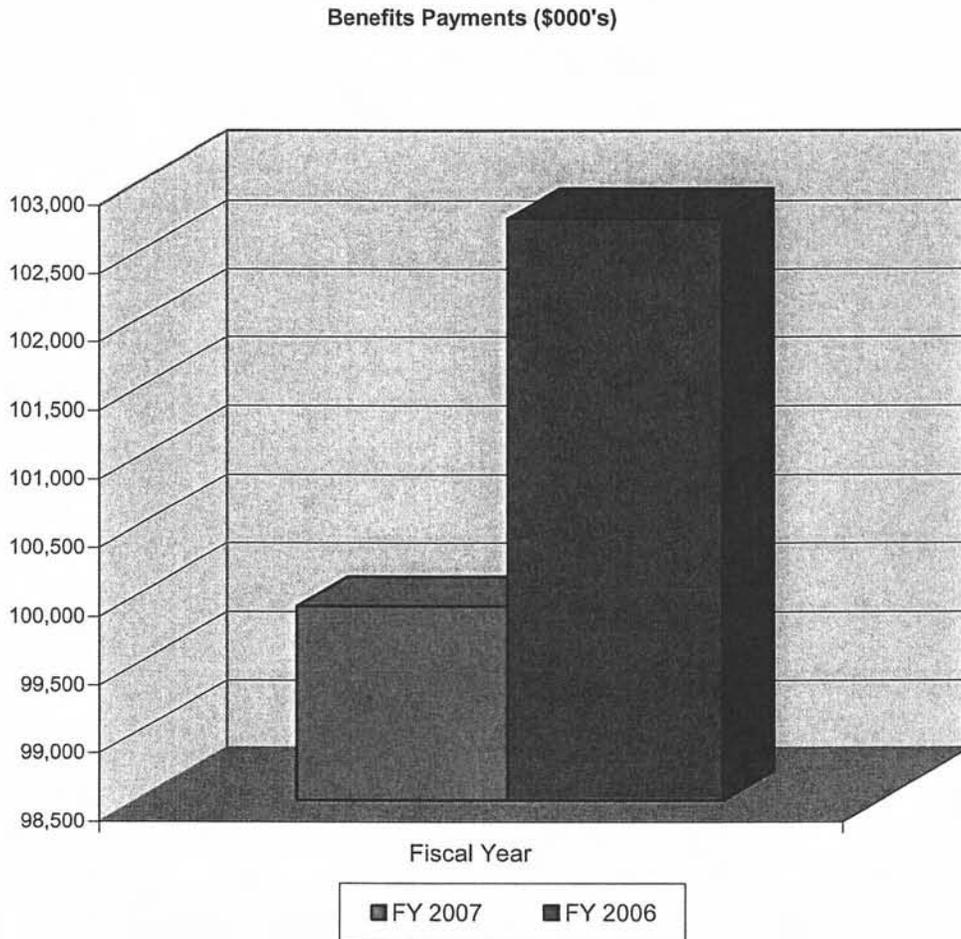
In fiscal year 2007, the Funds operating expenses decreased by \$2.8 million to \$99.9 million. See *Figure 1: Total Operating Expenses for the Years Ended September 30, 2007 and 2006*.

**Table 1: Overall Financial Position for the Years Ended September 30, 2007 and 2006**

Overall Financial Position		
(in millions)		
	2007	2006
Total Assets	\$ 412.0	\$ 389.0
Total Liabilities	37.7	41.1
Net Assets	\$ 375.1	\$ 347.9

**GOVERNMENT OF THE DISTRICT OF COLUMBIA  
UNEMPLOYMENT COMPENSATION FUND  
MANAGEMENT'S DISCUSSION AND ANALYSIS  
September 30, 2007**

**Figure 1: Total Operating Expenses for the Years Ended September 30, 2007 and 2006**



**Using This Annual Financial Report**

This annual financial report consists of a series of financial statements, prepared in accordance with Governmental Accounting Standards Board Statement No. 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments*. One of the most important questions asked about the Fund's finances is whether or not the Fund has improved as a result of the year's activities. The key to understanding this core question is the Statement of Net Assets; the Statement of Revenues, Expenses and Change in Net Assets; and the Statement of Cash Flows. These statements present financial information in a form that is similar to that used by corporations.

**GOVERNMENT OF THE DISTRICT OF COLUMBIA**  
**UNEMPLOYMENT COMPENSATION FUND**  
**MANAGEMENT'S DISCUSSION AND ANALYSIS**  
**September 30, 2007**

The Fund's net assets (the difference between assets and liabilities) are one indicator of the improvement or erosion of the Fund's financial health. The Statement of Net Assets includes all assets and liabilities. It is prepared under the accrual basis of accounting, whereby assets are recognized when the employer taxes and contributions are due, and liabilities are recognized when the liability to provide benefits to claimants has occurred.

The Statement of Revenues, Expenses and Change in Net Assets presents the revenues earned and the expenses incurred during the year. Activities are reported as either operating or non-operating.

Another important factor to consider when evaluating financial viability is the Fund's ability to meet financial obligations as they mature. The Statement of Cash Flows presents information related to cash inflows and outflows summarized by operating, non-capital financing and investing activities.

### **Reporting Entity**

The financial statements report information about the Fund as a whole using accounting methods similar to those used by private-sector companies. The Fund was established by the District to account for its unemployment compensation program. The Fund is administered by the Director of the District's Department of Employment Services. Substantially all administrative costs of the program are paid by a federal grant which is recorded in the District's General Fund. The Fund is included as a proprietary fund in the District's financial statements. These financial statements present only the revenues, benefits expense, and related assets, liabilities and net assets of the Fund.

### **Financial Analysis of the Fund**

At September 30, 2007, total Fund assets were approximately \$412.8 million. The Fund's largest asset is cash. Restricted cash totaling approximately \$405.2 million accounted for 98% of total assets. Restricted cash increased by \$25 million or 6.1 %. The other asset held by the Fund is accounts receivable, which totaled \$7.5 million as of September 30, 2007, as compared to \$8.8 million at the close of fiscal year 2006. These receivables are comprised of payments due from employers in the District of Columbia and from other states.

The Fund's liabilities totaled \$37.7 million as of September 30, 2007, which consisted primarily of \$26.0 million for benefit payments due to unemployed residents of the District of Columbia, and \$11.6 million due to the District of Columbia.

The Fund's current assets of \$412.8 million were sufficient to cover current liabilities of \$37.7 million, a ratio of 11 dollars in assets for every dollar in liabilities.

The Fund's sole operating expense is for unemployment compensation benefits to individuals separated from employment through no fault of their own. In fiscal year 2007, operating expenses were \$99.9 million compared to \$102.7 million in fiscal year 2006.

**GOVERNMENT OF THE DISTRICT OF COLUMBIA  
UNEMPLOYMENT COMPENSATION FUND  
MANAGEMENT'S DISCUSSION AND ANALYSIS  
September 30, 2007**

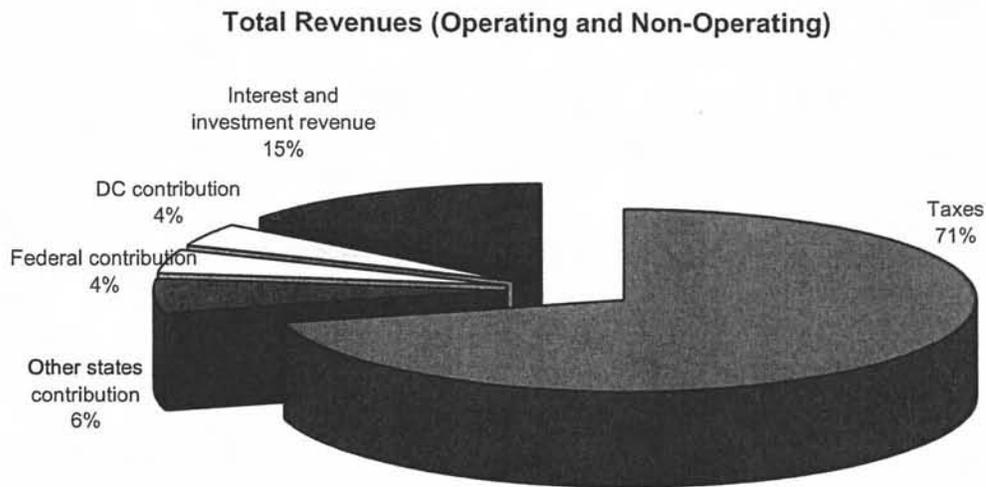
In fiscal year 2007, operating revenue totaled \$108.5 million compared to \$110.7 million in fiscal year 2006. Operating revenues decreased by 2%. Operating revenues come primarily from employer taxes. In fiscal year 2007, employer tax rates ranged from 1.3% to 6.6%.

Revenues from all sources (operating and non-operating) totaled \$127.1 million in fiscal year 2007 compared to \$127.8 million in fiscal year 2006. The sources of operating revenue for the Fund in fiscal year 2007 include:

- \$90.1 million from taxes,
- \$7.6 million from other states' contributions,
- \$5.5 million from the Federal government (contribution), and
- \$5.2 million reimbursed from the District government. The District government reimburses the Fund for unemployment compensation payments made to former District of Columbia Government employees.

The Fund's only source of non-operating revenue is interest income. Total non-operating income for fiscal year 2007 was \$18.6 million compared to \$17.1 million in fiscal year 2006. This is a slight increase from fiscal year 2006.

*Figure 4: Total Revenues (Operating and Non-Operating) for the year ended September 30, 2007*



**GOVERNMENT OF THE DISTRICT OF COLUMBIA**  
**UNEMPLOYMENT COMPENSATION FUND**  
**MANAGEMENT'S DISCUSSION AND ANALYSIS**  
**September 30, 2007**

**Statement of Cash Flows**

Another way to assess the financial health of an institution is to review the Statement of Cash Flows. Its primary purpose is to provide relevant information about the cash receipts and cash payments of an entity during a period. The Statement of Cash Flows is also used to assess:

- An organization's ability to generate future net cash flows,
- Its ability to meet its obligations as they become due, and
- The entity's needs for external financing.

**Contact Information**

This financial report is designed to provide a general overview of the Fund's finances. Questions concerning any information provided in this report, or requests for additional financial information, should be addressed to the Office of the Chief Financial Officer, Government of the District of Columbia, 1350 Pennsylvania Avenue, NW, Washington, DC 20004.

**GOVERNMENT OF THE DISTRICT OF COLUMBIA**  
**UNEMPLOYMENT COMPENSATION FUND**  
**STATEMENTS OF NET ASSETS**  
**SEPTEMBER 30, 2007 and 2006**  
**(Dollar Amounts in Thousands)**

	<u>2007</u>	<u>2006</u>
<b>ASSETS</b>		
Current assets:		
Restricted cash	\$ 405,244	\$ 380,248
Accounts receivable, net	<u>7,549</u>	<u>8,765</u>
Total assets	<u>412,793</u>	<u>389,013</u>
<b>LIABILITIES</b>		
Current liabilities:		
Benefit payments due	26,028	28,213
Due to District of Columbia	<u>11,618</u>	<u>12,862</u>
Total liabilities	<u>37,646</u>	<u>41,075</u>
<b>NET ASSETS</b>		
Restricted for unemployment compensation benefits	<u>\$ 375,147</u>	<u>\$ 347,938</u>

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

**GOVERNMENT OF THE DISTRICT OF COLUMBIA**  
**UNEMPLOYMENT COMPENSATION FUND**  
**STATEMENTS OF REVENUES, EXPENSES, AND CHANGE IN NET ASSETS**  
**FOR THE YEARS ENDED SEPTEMBER 30, 2007 and 2006**  
(Dollar Amounts in Thousands)

	<u>2007</u>	<u>2006</u>
<b>Operating revenues</b>		
Taxes	\$ 90,117	\$ 95,888
Other states' contributions	7,629	4,285
Federal contribution	5,478	5,484
District contribution	<u>5,250</u>	<u>5,056</u>
Total operating revenues	<u>108,474</u>	<u>110,713</u>
 <b>Operating expenses</b>		
Unemployment benefits	<u>99,920</u>	<u>102,749</u>
 <b>Operating income</b>	8,554	7,964
 <b>Non-operating revenues</b>		
Investment income	<u>18,655</u>	<u>17,081</u>
 Change in net assets	27,209	25,045
 Total net assets - beginning	<u>347,938</u>	<u>322,893</u>
Total net assets - ending	<u>\$ 375,147</u>	<u>\$ 347,938</u>

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

**GOVERNMENT OF THE DISTRICT OF COLUMBIA  
UNEMPLOYMENT COMPENSATION FUND  
STATEMENTS OF CASH FLOWS  
FOR THE YEARS ENDED SEPTEMBER 30, 2007 and 2006  
(Dollar Amounts in Thousands)**

	<u>2007</u>	<u>2006</u>
<b>OPERATING ACTIVITIES</b>		
Cash receipts from customers/contributions	\$ 109,690	\$ 111,569
Cash payments to employees/claimants	<u>(103,349)</u>	<u>(108,259)</u>
Net cash provided	6,341	3,310
<b>INVESTING ACTIVITIES</b>		
Interest and dividends received	<u>18,655</u>	<u>17,081</u>
Net increase in cash	24,996	20,392
Restricted cash, beginning	<u>380,248</u>	<u>359,856</u>
Restricted cash, ending	<u>\$ 405,244</u>	<u>\$ 380,248</u>
<b>Reconciliation of operating income to net cash provided by operating activities:</b>		
Operating income	\$ 8,554	\$ 7,964
Decrease (increase) in assets:		
Receivables	1,216	856
Increase (decrease) in liabilities:		
Payables	(3,429)	(5,504)
Other current liabilities	<u>-</u>	<u>(6)</u>
Net cash provided by operating activities	<u>\$ 6,341</u>	<u>\$ 3,310</u>

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

**GOVERNMENT OF THE DISTRICT OF COLUMBIA**  
**UNEMPLOYMENT COMPENSATION FUND**  
**NOTES TO FINANCIAL STATEMENTS**  
**SEPTEMBER 30, 2007 AND 2006**

**NOTE 1: ORGANIZATION AND PURPOSE**

Pursuant to federal law, the Government of the District of Columbia (the District) maintains an unemployment compensation program that is accounted for in the Government of the District of Columbia Unemployment Compensation Fund (the Fund). The Fund pays up to 26 weeks of statutory benefits to eligible unemployed former employees of the District or federal government, and private employers of the District.

The Fund is administered by the Director of the District's Department of Employment Services. Substantially all administrative costs of the program are paid by a federal grant which is recorded in the District's General Fund. The Fund is included as a proprietary fund in the District's financial statements. These financial statements present only the revenues, benefits expense, and related assets, liabilities and net assets of the Fund, and are not intended to present the financial position and results of operations of the Government of the District of Columbia taken as a whole.

**NOTE 2: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

*(a) Measurement Focus and Basis of Accounting*

The Fund uses the economic resources measurement focus and the accrual basis of accounting, whereby revenues and assets are recognized when taxes and contributions are due, and expenses and liabilities are recognized when an obligation to provide benefits has occurred, regardless of when cash is exchanged.

The Fund has elected, as allowed in paragraph 7 of Governmental Accounting Standards Board (GASB) *Statement No. 20, Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*, not to follow Financial Accounting Standard Board (FASB) pronouncements issued subsequent to November 30, 1989. Therefore, the Fund follows all GASB pronouncements and FASB pronouncements issued on or before November 30, 1989, unless those pronouncements conflict or contradict GASB pronouncements.

**GOVERNMENT OF THE DISTRICT OF COLUMBIA**  
**UNEMPLOYMENT COMPENSATION FUND**  
**NOTES TO FINANCIAL STATEMENTS**  
**SEPTEMBER 30, 2007 AND 2006**

**NOTE 2: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

*(b) Restricted Cash*

The cash balance is restricted for future benefit payments. The funds are held at the U.S. Department of Treasury in a trust fund in the District's name. Pursuant to the Social Security Act, the funds held at the U.S. Department of Treasury earn interest quarterly based on the interest rates of U.S. Department of Treasury's Certificates of Indebtedness. The quarterly interest rates ranged from 4.64% to 4.82% for the year ended September 30, 2007. The quarterly interest rates ranged from 4.63% to 4.75% for the year ended September 30, 2006.

*(c) Accounts Receivable*

Accounts receivable represents amounts due from private employers for unremitted payroll taxes and from Federal and District governments for unemployment benefits paid. Receivables are stated net of estimated allowances for uncollectible amounts, which are based upon past collection experience and current economic conditions.

*(d) Operating Revenues*

Private employers are required to make quarterly contributions to the Fund, calculated as a percentage of payroll costs. This contribution percentage is adjusted for each private employer based on claims experience. However, the District and Federal governments reimburse the Fund only for actual benefits paid to their respective former employees. Nonprofit private employers also have the option of reimbursing the fund instead of making quarterly contributions. All other revenues are considered non-operating revenues.

*(e) Operating Expenses*

Operating expenses represent benefits paid and an estimate of amounts to be paid (based on average length of unemployment) to eligible unemployed former employees of the District or Federal government, other jurisdictions, and private employers of the District.

**GOVERNMENT OF THE DISTRICT OF COLUMBIA**  
**UNEMPLOYMENT COMPENSATION FUND**  
**NOTES TO FINANCIAL STATEMENTS**  
**SEPTEMBER 30, 2007 AND 2006**

**NOTE 2: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

*(f) Accounts Payable*

Accounts Payable represent three types of payables: (1) amounts due to other jurisdictions for claims paid to individuals by other states under the combined wage agreement among the states and U.S. territories. Individuals who earn wages in the District and another state or U.S. territory are eligible to file for, and receive unemployment benefits in either the District or other states or U.S. territories. When an individual chooses to file outside of the District, the District, through the Fund, reimburses the other state or U.S. territory for its pro rata share of the claim amount; (2) amounts due to the employers of the District who overpaid their tax contributions; and (3) amounts due to claimants for the remaining periods of eligibility on claims incurred prior to year-end, but not due and payable until the following fiscal year.

*(g) Use of Estimates*

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

**GOVERNMENT OF THE DISTRICT OF COLUMBIA  
UNEMPLOYMENT COMPENSATION FUND  
NOTES TO FINANCIAL STATEMENTS  
SEPTEMBER 30, 2007 AND 2006**

**NOTE 3: ACCOUNTS RECEIVABLE**

The accounts receivable and applicable allowance for uncollectible accounts receivable at September 30, are as follows:

	<u>2007</u>	<u>2006</u>
Accounts receivable	\$ 20,395	\$ 16,560
Less: Allowance for uncollectible accounts	<u>(12,846)</u>	<u>(7,795)</u>
Accounts receivable, net	<u>\$ 7,549</u>	<u>\$ 8,765</u>

**NOTE 4: DUE TO DISTRICT OF COLUMBIA**

This amount represents the following:

	<u>2007</u>	<u>2006</u>
Refund of employer taxes paid by the District	\$ 2,228	\$ 1,283
Systems modernization and enhancements	10,211	12,345
Less: Benefits paid to former District employees	<u>(821)</u>	<u>(766)</u>
Due to District of Columbia, net	<u>\$ 11,618</u>	<u>\$ 12,862</u>

**THOMPSON, COBB, BAZILIO & ASSOCIATES, PC**  
*Certified Public Accountants and Management, Systems, and Financial Consultants*

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**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***

To the Mayor, Members of the Council and  
Inspector General of the Government of the District of Columbia

We have audited the financial statements of the District of Columbia Unemployment Compensation Fund (the Fund) as of and for the year ended September 30, 2007, and have issued our report thereon dated February 27, 2008. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

*Internal Control over Financial Reporting*

In planning and performing our audit, we considered the Fund's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Fund's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Fund's internal control over financial reporting.

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

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the Fund's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the Fund's financial statements that is more than inconsequential will not be prevented or detected by the Fund's internal control. We consider the deficiencies described in Appendix to be significant deficiencies in internal control over financial reporting (items 2007.2, 2007.3, 2007.4 and 2007.5).

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

Our consideration of 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. However, of the significant deficiencies described in Appendix A, we consider item 2007.5 to be a material weakness.

### *Compliance and Other Matters*

As part of obtaining reasonable assurance about whether the Fund's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed one instance of noncompliance that is required to be reported under *Government Auditing Standards*, which is described in Appendix A as item 2007.1.

Management's response to the findings identified in our audit is described in Appendix A. We did not audit management's response and accordingly, we express no opinion on it.

This report is intended solely for the information and use of management, the Mayor, Members of the Council and the Inspector General of the Government of the District of Columbia, and others within the District of Columbia Department of Employment Services, and is not intended to be and should not be used by anyone other than these specified parties.

Washington, DC  
February 27, 2008

*Thompson, Cobb, Baziles & Associates, P.C.*

**SIGNIFICANT DEFICIENCIES IN INTERNAL CONTROL  
OVER FINANCIAL REPORTING AND COMPLIANCE**

**2007.1 Required Employer Payroll Audits Not Performed**

The Tax Division within the Unemployment Compensation Program is responsible for collecting tax receipts from District employers for their respective payment of unemployment taxes. Private employers doing business within the District of Columbia must file the Employers' Quarterly Contribution and Wage Reports (Form UC-30) for payment of the taxes generally within 30 days after the end of the quarter. The information reported on the Form UC-30 must match the information maintained by the employer's payroll records and the information reported for federal tax purposes.

Department of Labor (DOL) Unemployment Insurance Program Letter No. 18-93 requires the Department of Employment Services (DOES) to perform audits annually of 2% of its active contributor employer accounts. DOES did not perform the required number of audits of total active contributor employer accounts in 2007. Approximately 206 audits were performed compared to approximately 580 audits required to meet the 2% requirement. Although the program has made substantial improvement of the 30 audits performed in 2006, it still has not met the 2% requirement. We recommend that DOES ensure that the required number of payroll audits is performed annually.

Management's Response

Management concurs with this finding. The UI Tax Division will increase the current number of auditors from six full time equivalents (FTEs) to eight by the end of the 3<sup>rd</sup> quarter of 2008. It is anticipated that an increase of 2 FTEs will increase field audit completion by 25% or approximately 80 additional audits annually. The division has worked with its contractors to design and develop an audit assignment application to eliminate the manual process currently in place. The auto-audit-assignment software will be in production by March 31, 2008.

Additionally, the Office of Information Technology (OIT) is aware of the problem and is researching software for laptop access to enable auditors to process an audit and upload the information to a server from the field. This process will improve efficiency, accuracy and timeliness.

**SIGNIFICANT DEFICIENCIES IN INTERNAL CONTROL  
OVER FINANCIAL REPORTING AND COMPLIANCE**

**2007.2 Reconciliation between DUTAS and SOAR Not Properly Approved**

DUTAS, the District's Unemployment Tax Assessment System, records all activity related to the amount of taxes, interests and penalties due and the amount paid by employers. This system, however, is not the District's system of record. On a periodic basis, information from DUTAS is recorded into SOAR, the District's financial reporting system, to produce financial reports and maintain current financial data.

During 2007, monthly reconciliations were performed; however, there was no evidence that the reconciliations were approved by supervisory personnel. Where multiple systems are used to operate and manage a program, periodic reconciliations should be performed, reviewed and approved to ensure the systems agree and the reporting of information regarding the program is consistent. Without properly approved reconciliations, there is the risk of improper reporting of assets. We recommend supervisory personnel sign the reconciliations to document proper supervisory review and approval.

Management's Response

Management does not concur with this finding. The reconciliation between DUTAS and SOAR was done in fiscal year 2007. Shared Service Center Financial Reporting Manager reviewed the reconciliation and emailed it to DOES Tax Division and did a follow-up with an email. The Tax Division reconciled all known variances and discrepancies and the UI Tax Officer reviewed, approved and forwarded the request back to the Shared Service's Financial Reporting Manager.

While there was no signatory page affixed to the reconciliation document that would authenticate the review and approval, one has since been created and will accompany all reconciliation activities between the UI Tax Division and the Shared Services Center in the future.

**SIGNIFICANT DEFICIENCIES IN INTERNAL CONTROL  
OVER FINANCIAL REPORTING AND COMPLIANCE**

**2007.3 Inadequate Procedures for Processing Employer Refunds**

DUTAS, the District's Unemployment Tax Assessment System, records all activity related to the amount of taxes, interests and penalties due and the amount paid by employers. When an employer overpays its share of taxes, DUTAS creates a credit for the employer indicating the employer is due a refund. Tax examiners review the employer's account and prepare requests for refunds on behalf of the employer. The requests are forwarded to the Shared Service Center for disbursement.

While there is a process in place, the process is not adequate to ensure the employer refunds are properly paid, posted and reported in the correct period. In addition, for two of the 40 employer refunds tested, the Shared Service Center could not provide the documentation to support the refund request was paid. The payments are processed in SOAR and are never reconciled to DUTAS to ensure all amounts requested were paid. A review of DUTAS will indicate the refunds were processed (with the assumption that the amounts were paid) but without reconciling the payments processed in SOAR. Further, there is no cut-off period for processing the requests to ensure the amounts are recorded in the correct fiscal year. DOES should reconcile the employer refund account with the Shared Service Center on a periodic basis to ensure amounts requested to be paid are paid. An effective date should be included on the request to ensure amounts are posted to the correct period. In addition, the Shared Service Center should ensure documentation is maintained for all transactions and is available for review.

Management's Response

Management concurs with this finding. DOES and the Shared Services Center have designed an application, DAFRN, that automates the refund process. The application, in conjunction with the Internal Tax Refund Web Site (DOES Intranet site) will automate the approval process and the release of the refund request to SOAR. Once SOAR processes the refund and a check is issued, feedback in the form of a FTP file will be forwarded to DUTAS alerting DOES of the issuance. An auto alert will be sent to DUTAS from SOAR notifying DOES of the check clearance. The application development is in the final stages and is anticipated to be launched April 30, 2008.

**SIGNIFICANT DEFICIENCIES IN INTERNAL CONTROL  
OVER FINANCIAL REPORTING AND COMPLIANCE**

**2007.4 Inadequate Controls over Web Enabled Benefit System**

WEBS, the Web Enabled Benefit System, is the Department of Employment Services' (DOES) online application system for the Unemployment Compensation Program. This site permits individuals to file initial claims for Unemployment Compensation benefits against the District of Columbia via the internet. The eligibility requirements remain the same for claimants filing via the internet, and it is the responsibility of the DOES to ensure the requirements are met prior to approval of a claim and payment of unemployment benefits.

During fiscal year 2007, WEBS did not have adequate access controls to prevent or detect ineligible, unauthorized or fraudulent claims from being submitted. For example, a user can select an arbitrary social security number and request WEBS to generate the weekly benefit amount. If WEBS calculates the maximum weekly benefit amount (\$359) for the selected social security number, the claimant can alter the name and address on the account to receive benefits. Additionally, we observed that multiple claims for unemployment were filed using the same mailing address, multiple claims were filed using the same Internet Protocol (IP) address, and the same named claimant was used with different social security numbers.

This issue has been referred to the Office of the Inspector General and is currently under investigation. To date, the total number of claims identified is 16 for a total of about \$90,580. Best practices require that the logical access to and use of IT computing resources should be restricted by the implementation of adequate identification, authentication and authorization mechanisms, and linking users and resources with the access rules. Adequate controls were not in place to properly identify, authenticate and authorize users. Improper unemployment compensation benefits were paid to ineligible claimants. Management should improve the current security architecture of WEBS by ensuring proper identification, authentication and authorization mechanisms (for example, claimants should be required to validate their identity through a series of security questions and/or appearing in person).

Management's Response

Management does not concur with this finding. Management upon detection through the BARTS (Benefits Auditing and Recovery Tracking Systems) and through the conscientiousness of agency employees was able to develop a suspicious claim list. The WEBS system flags a claim if the name, SSN, IP address or password is the same or appears on the list. The claimant is informed if the claim cannot be processed at the time and the claimant is referred to DOES for further instructions. Claimants are called in from the suspicious list and must bring proof of identity and SSN. While any theft is not acceptable, the amount of the accumulated theft of approximately \$90,000 for 16 claimants is not massive when consideration is given to the fact that more than \$90,000,000 in benefits were paid to more than 23,000 claimants in the last year.

**SIGNIFICANT DEFICIENCIES IN INTERNAL CONTROL  
OVER FINANCIAL REPORTING AND COMPLIANCE**

**2007.5 Reserve Methodology for Employer Receivables Not Adequate**

The Unemployment Compensation Fund (the Fund) year-end accounts receivable balance includes amounts due from claimants, other states, the District of Columbia Government, the Federal Government and District employers. The Fund establishes an allowance for claimants and employers as collections on these accounts may not always occur. The methodology for employers was to establish an allowance for 100% of the balance for employers with outstanding balances two years and older and none for all accounts with balances under two years.

The reserve methodology for establishing the allowance for uncollectible employer receivables did not consider the subsequent collection activity on those accounts under two years. Per review of the accounts, only about 17% of the outstanding balance at year end was collected through February 2008. This indicates that the current method for establishing the reserve overestimated the collectability of accounts under two years.

We recommend DOES (Tax Division) work with the Shared Service Center to develop an allowance methodology that analyzes the collection activity for all accounts for a minimum of three years. This will assist management in providing a better estimate of the allowance.

Management's Response

Management concurs with the finding. Methodology used was what was agreed between management and the auditors in the previous years. As recommended, DOES Tax Division and Shared Service Center will work together to develop a methodology whereby subsequent uncollectible employer receivables two years and younger will be included in receivables. In addition, as recommended by the auditors, Shared Service Center will include collection activity on receivables for a minimum of three years.

**GOVERNMENT OF THE DISTRICT OF COLUMBIA  
 UNEMPLOYMENT COMPENSATION FUND  
 STATUS OF PRIOR YEAR MATERIAL WEAKNESSES, SIGNIFICANT DEFICIENCY AND  
 MATERIAL NONCOMPLIANCE WITH LAWS AND REGULATIONS  
 YEAR ENDED SEPTEMBER 30, 2007**

*Appendix A*

<b>Finding Number/Nature of Comment</b>	<b>Type Of Comment in FISCAL YEAR 2006</b>	<b>Current Year Status</b>
2006.1/ Required Employer Payroll Audits Not Performed	Material Non-Compliance	Noncompliance – see finding 2007.1
2006.2/ Unemployment Compensation Claimant File Management	Material Non-Compliance	Resolved
2006.3/ Reconciliation between DUTAS and SOAR Not Performed	Reportable Condition	Significant deficiency – finding modified in 2007 to indicate reconciliations were not properly reviewed and approved – see finding 2007.2