

South Carolina  
Department of Employment and Workforce  
Columbia, South Carolina  
Financial Statements  
and Independent Auditors' Reports  
Year Ended June 30, 2011

# State of South Carolina



## Office of the State Auditor

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May 2, 2012

The Honorable Nikki R. Haley, Governor  
and  
Mr. Abraham Turner, Director  
South Carolina Department of Employment and Workforce  
Columbia, South Carolina

This report on the audit of the basic financial statements of the South Carolina Department of Employment and Workforce and the accompanying schedule of expenditures of federal awards as required by the U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments and Non-Profit Organizations*, the fiscal year ended June 30, 2011, was issued by Scott and Company, L.L.P., Certified Public Accountants, under contract with the South Carolina Office of the State Auditor.

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

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Richard H. Gilbert, Jr.", written in a cursive style.

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

RHGjr/trb

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## Independent Auditors' Report

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The Office of the State Auditor and Management  
South Carolina Department of Employment and Workforce  
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 Department of Employment and Workforce (the "Agency") as of and for the year ended June 30, 2011, which collectively comprise the Agency's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Agency'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 consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Agency's internal control over financial reporting. Accordingly, we express no such opinion. 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 Agency are intended to present the financial position, the changes in financial position and, where applicable, cash flows of only that portion of governmental activities, the business-type activities, and each major fund of only that portion of the funds of the State of South Carolina (the "State") financial reporting entity that is attributable to the transactions of the Agency. They do not purport to and do not present fairly the financial position of the State as of June 30, 2011, the changes in its financial position, or, where applicable, its cash flows 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 Agency as of June 30, 2011, 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 April 30, 2012 on our consideration of the Agency'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 should be considered in assessing the results of our audit.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages three through nine be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise the Agency's basic financial statements as a whole. 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 Agency. Such information 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 and Company LLP*

Columbia, South Carolina  
April 30, 2012

## MANAGEMENT'S DISCUSSION AND ANALYSIS

Management of the South Carolina Department of Employment and Workforce (the "Agency") offers readers this narrative overview and analysis of the financial activities for the year ended June 30, 2011. Please read this information in conjunction with the Agency's financial statements and accompanying notes.

### Financial Highlights

- The overall financial condition of the Agency improved during the fiscal year ended June 30, 2011. The Agency's liabilities exceeded its assets at fiscal year ending June 30, 2011 by \$547,728,093 (shown as "total net deficit"), which represents a net reduction of the deficit of \$181,134,430 from the prior year.
- Total Unemployment Compensation benefits paid were \$2,171,063,209 and \$2,027,711,376 during the years ended June 30, 2011 and 2010, respectively.

### Overview/Discussion of the Annual Financial Report

The discussion and analysis provides an introduction to the Agency'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 Agency'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 Agency'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 Agency's financial health (financial position) is strengthening or weakening. But in order to assess the Agency'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 entity's overall net assets changed during the year. The statement of activities can help to show how much it costs the Agency 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.

## **Entity-wide Financial Statements (continued)**

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

### **Governmental Activities:**

The Agency's internal administrative activities are reported as governmental activities including general administration, employment and training services, and unemployment insurance administrative costs. 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 activities of the South Carolina Department of Employment and Workforce Unemployment Compensation Fund (the "Trust Fund") are considered business-type activities. This fund collects money through federal grant revenues, unemployment taxes paid by businesses, and federal loans, when needed.

## **Fund Financial Statements**

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

### **Governmental Funds:**

The Agency 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 Agency'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 Agency 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 Agency's proprietary funds is from assessments to employers and reimbursement from the federal government for the payment of unemployment benefits. The Agency's proprietary fund is used to account for the State's Unemployment 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.

## **Fund Financial Statements (continued)**

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 Agency, liabilities exceeded assets by \$547,728,093 at the year-ended June 30, 2011. In the prior year, liabilities exceeded assets by \$728,862,523.

The Agency's net deficit can be attributed to the Trust Fund due to the effect of increasing unemployment during the recent national recession, coupled with an outdated unemployment insurance tax structure. In response to the net deficit, the Agency has taken advances from the federal government to continue providing unemployment benefits to the citizens of South Carolina. In addition, recent legislation was enacted by the State to restructure the unemployment insurance tax rate system to bring the Trust Fund back to solvency and to establish an acceptable level of reserve funding in the future. The new rate system was also specifically designed to allow the State to repay all federal advances and the associated interest, which began accruing on January 1, 2011. The Agency expects all federal advances to be repaid by the end of 2015.

The improved overall condition at the Agency is largely attributable to the effectiveness of the new unemployment insurance tax rate structure, effective January 1, 2011.

At the end of the 2011 fiscal year, the Agency was able to report positive net asset balances in the governmental activities which represent capital assets, amounts restricted for debt service and unrestricted net assets.

## **Governmental Activities**

Total assets increased by \$19,500,463 (36.2%) from last year due primarily to an increase in cash from the collection of an interest surcharge, implemented as part of revised SUTA legislation effective January 1, 2011. The interest surcharge was new in fiscal year 2011 and represents the amount collected by the Agency from employers to pay for the interest on the advances from the federal government.

There was an increase in federal grant activity, increasing revenue by approximately \$55.9 million.

**South Carolina Department of Employment and Workforce**  
**Statement of Net Assets**  
**June 30, 2011 and 2010**  
**(Condensed Financial Data)**

	Governmental Activities		Business-Type Activities		Total	
	2011	2010	2011	2010	2011	2010
<b>Assets:</b>						
Current & other assets	\$ 51,181,634	\$ 32,155,381	\$ 406,059,577	\$ 157,834,655	\$457,241,211	\$189,990,036
Capital assets	22,254,713	21,780,503	—	—	22,254,713	21,780,503
Total assets	<u>\$ 73,436,347</u>	<u>\$ 53,935,884</u>	<u>\$ 406,059,577</u>	<u>\$ 157,834,655</u>	<u>479,495,924</u>	<u>\$211,770,539</u>
<b>Liabilities:</b>						
Current	\$ 32,032,231	\$ 20,500,002	\$ 210,961,526	\$ 32,320,146	\$ 242,993,757	\$52,820,148
Non-current	1,036,784	1,150,562	783,193,476	886,662,352	784,230,260	887,812,914
Total liabilities	<u>33,069,015</u>	<u>21,650,564</u>	<u>994,155,002</u>	<u>918,982,498</u>	<u>1,027,224,017</u>	<u>940,633,062</u>
<b>Net assets:</b>						
Invested in capital assets, net of related debt	22,134,274	21,553,620	—	—	22,134,274	21,553,620
Restricted for debt service	13,848,414	—	—	—	13,848,414	—
Unrestricted	4,384,644	10,731,700	(588,095,425)	(761,147,843)	(583,710,781)	(750,416,143)
Total net assets (deficit)	<u>40,367,332</u>	<u>32,285,320</u>	<u>(588,095,425)</u>	<u>(761,147,843)</u>	<u>(547,728,093)</u>	<u>(728,862,523)</u>
Total liabilities & net assets	<u>\$ 73,436,347</u>	<u>\$ 53,935,884</u>	<u>\$ 406,059,577</u>	<u>\$ 157,834,655</u>	<u>\$479,495,924</u>	<u>\$211,770,539</u>

**Statement of Activities**

	Governmental Activities		Business-Type Activities		Total	
	2011	2010	2011	2010	2011	2010
<b>Revenues:</b>						
<b>Program revenues:</b>						
Charges for services	\$ 30,551,850	\$ 7,468,825	\$ 517,502,522	\$ 302,762,139	\$ 548,054,372	\$ 310,230,964
Operating grants & contributions	156,852,702	123,964,581	1,791,424,360	1,281,068,369	1,948,277,062	1,405,032,950
<b>General revenues:</b>						
State appropriations	433,307	512,778	—	—	433,307	512,778
Total revenues	<u>187,837,859</u>	<u>131,946,184</u>	<u>2,308,926,882</u>	<u>1,583,830,508</u>	<u>2,496,764,741</u>	<u>1,715,776,692</u>
<b>Expenses:</b>						
Employment & training services	179,531,527	131,378,094	—	—	179,531,527	131,378,094
Unemployment compensation	—	—	2,171,063,209	2,027,711,376	2,171,063,209	2,027,711,376
Total expenses	<u>179,531,527</u>	<u>131,378,094</u>	<u>2,171,063,209</u>	<u>2,027,711,376</u>	<u>2,350,594,736</u>	<u>2,159,089,470</u>
Contributed capital	—	32,760	—	—	—	32,760
Loss on disposal of capital assets	(35,229)	(23,026)	—	—	(35,229)	(23,026)
Gain on forgiveness of debt	—	—	35,188,745	—	35,188,745	—
Indirect cost remitted to general fund of the State	(189,091)	(183,650)	—	—	(189,091)	(183,650)
(Decrease) increase in net assets	8,082,012	394,174	173,052,418	(443,880,868)	181,134,430	(443,486,694)
Net assets (deficit) – beginning	<u>32,285,320</u>	<u>31,891,146</u>	<u>(761,147,843)</u>	<u>(317,266,975)</u>	<u>(728,862,523)</u>	<u>(285,375,829)</u>
Net assets (deficit) – ending	<u>\$ 40,367,332</u>	<u>\$ 32,285,320</u>	<u>\$(588,095,425)</u>	<u>\$(761,147,843)</u>	<u>\$(547,728,093)</u>	<u>\$(728,862,523)</u>

## **Business-Type Activities**

### **Statements of Net Deficit:**

Total assets increased by approximately \$253 million due primarily to the increase in the cash balance, which was the result of both a decrease in State-funded unemployment benefit claims paid during the 2011 fiscal year and the increased amounts of state unemployment taxes (“SUTA”) assessed to employer accounts. Unemployment continued to increase, with claimants filing for a longer period of time, as required by the federal government. Many individuals exhausted regular State UI benefits during the year, and began receiving benefit payments fully-funded by the federal government instead of being funded by the taxes on state businesses.

Federal intergovernmental payables increased during the year, largely due to claimant refunds, cancelled payments, and other items being owed back to the federal government which, in total, offset any amounts due from the federal government. For the year ended June 30, 2011, a significant amount due from the federal government was reported. This balance was largely a result of the *Unemployment Compensation Extension Act of 2010*, passed by Congress in late July 2010. As a result of claimants continuing to file for various Emergency Unemployment Compensation (“EUC”) and Extended Benefits (“EB”) during the period between the original ending date of federal EUC and EB funding and extension passed on July 22, 2010, a large number of claims for benefit weeks ending prior to June 30, 2010 were paid subsequent to year end. The accrual of these benefit expenses required a corresponding accrual for reimbursable amounts receivable from the federal government.

Ending net deficit decreased by approximately \$173 million as compared to a \$444 million increase for the prior year, due to the increases in SUTA revenues and federal grants received.

### **Revenues, Expenses, and Changes in Net Deficit:**

SUTA assessments increased by approximately \$215 million compared to the prior fiscal year due to higher tax rates being assessed on employers as a result of the revised state unemployment law, effective January 1, 2011.

Total operating revenues increased by approximately \$725 million primarily due to an increase in federal grants relating to federally funded unemployment programs and increased amounts of tax revenues received from employers.

Unemployment compensation benefits increased by approximately \$143 million due to increased unemployment and increases in the period of time over which benefits are paid as mandated by the federal government.

Operating income for 2011 was approximately \$138 million as compared to a \$444 million operating loss for the prior year due to the increase in assessments received.

Non-operating revenues increased by approximately \$35 million for the year 2011 as a result of the federal government’s forgiveness of certain trust fund debts via the application of Federal Unemployment Tax Act (“FUTA”) credit reductions for employers subject to the provisions of the State’s unemployment application law. This resulted from the State’s failure to meet FUTA credit reduction avoidance criteria in 2010. State businesses paid 0.3% in increased FUTA tax for the 2010 calendar year. These additional federal taxes were then applied against the State’s federal loan balance.

## **Business-Type Activities**

### **Revenues, Expenses, and Changes in Net Deficit: (continued)**

Due to proper and adequate principal payments being made subsequent to the end of the 2011 fiscal year and meeting other prescribed criteria, the FUTA credit reduction has been avoided for the 2011 tax year. For the 2011 calendar year, the required loan payments and other avoidance criteria to avoid FUTA credit reduction were funded through increased tax assessments coupled with non-recurring revenues appropriated to the Fund by the State's General Assembly. The US DOL has approved the State's application for 2011 FUTA credit reduction avoidance. South Carolina is the only borrowing state to successfully apply for and be approved for FUTA credit reduction avoidance.

### **Financial Analysis of the Governments Funds**

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

### **Governmental Funds**

The focus of the Agency's governmental fund is to provide information on near-term inflows, outflows, and balances of spendable resources. Such information is useful in assessing the Agency's financing requirements. In particular, the assigned fund balance may serve as a useful measure of an agency's net resources available for spending at the end of the fiscal year. As of the end of the current fiscal year, the Agency's governmental fund reported combined ending fund balances of \$22,021,898, an increase of approximately \$7.5 million for the year.

Assigned fund balance accounts for approximately 35% or \$7.7 million of ending fund balance and is available for spending at the Agency's discretion, in accordance with federal and state regulations.

Restricted fund balance accounts for approximately 64% or \$14.1 million of ending fund balance and includes amounts that can only be spent for specific purposes stipulated by constitution, external resource providers, or through enabling legislation.

Non-spendable fund balance accounts for 1% or \$0.2 million of ending fund balance and accounts for prepaid items.

### **Proprietary Fund**

The Agency's proprietary fund provides the same type of information found in the entity-wide financial statements in more detail for the Trust Fund. Unrestricted net deficit of the Fund at the end of the year amounted to approximately \$588 million. Other information concerning this fund has been addressed in the discussion of the Agency's business-type activities.

## **Capital Assets and Debt Administration**

Primary changes in capital amounts during the year were related to incurring expenses related to development of internally generated/modified computer software currently classified as construction in progress (“CIP”). In addition, a significant amount of computer software equipment was disposed of during the year.

Long-term liabilities fell into three areas as follows:

Advances from the federal government;  
Capital leases payable; and  
Accrued compensated absences and related benefits.

More detailed information about the Agency’s capital assets is presented in Note 6 to the financial statements. More detailed information about the Agency’s debt administration is presented in Notes 7, 8 and 14 to the financial statements.

## **Economic Factors and Next Year’s Rate**

Tax rates for 2011 were set to raise sufficient revenue in 2011 to cover projected benefit costs, estimated loan repayments, interest owed on outstanding federal advances and to increase net trust fund solvency as required to avoid FUTA credit reductions for state businesses. The State anticipates being able to pay off all outstanding debt to the federal government by the year 2015 based on current economic projections and enacted legislation. The Trust Fund’s net assets are projected to slowly increase as additional loans are repaid in each year and revenues are sufficient to meet projected obligations. The maximum number of weeks of state UI trust fund unemployment compensation was reduced from 26 weeks to 20 weeks, effective June 14, 2011. This resulted in a reduction of total available weeks of state and federally funded benefits from 99 to 78 weeks.

## **Request for Information**

This management’s discussion and analysis is designed to provide a general overview of the South Carolina Department of Employment and Workforce’s finances for all those with interest in the Agency’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 Finance, 1550 Gadsden Street, Post Office Box 995, Columbia, South Carolina 29202.

South Carolina Department of Employment and Workforce  
Statement of Net Assets  
June 30, 2011

	<u>Governmental Activities</u>	<u>Business-type Activities</u>	<u>Totals</u>
<b>Assets:</b>			
Current assets:			
Cash and cash equivalents	\$ 8,296,144	\$ 260,981,907	\$ 269,278,051
Restricted cash	13,848,414	—	13,848,414
Assessments receivable, net	9,926,251	126,936,099	136,862,350
Benefit overpayments receivable, net	—	10,627,713	10,627,713
Due from reimbursable employers, net	—	1,508,560	1,508,560
Internal balances	5,087,092	(5,087,092)	—
Intergovernmental receivables, net:			
Federal	13,518,586	3,594,035	17,112,621
State agencies	344,838	2,320,509	2,665,347
Local governments	—	3,459,727	3,459,727
Other states	—	1,718,119	1,718,119
Prepaid items	160,309	—	160,309
Total current assets	<u>51,181,634</u>	<u>406,059,577</u>	<u>457,241,211</u>
Non-current assets:			
Capital assets, net of accumulated depreciation	<u>22,254,713</u>	<u>—</u>	<u>22,254,713</u>
Total assets	<u>\$ 73,436,347</u>	<u>\$ 406,059,577</u>	<u>\$ 479,495,924</u>
<b>Liabilities:</b>			
Current liabilities:			
Benefits payable	\$ —	\$ 3,778,647	\$ 3,778,647
Accounts payable	7,443,495	—	7,443,495
Tax withholdings payable	—	40,704	40,704
Contributions payable	—	8,979,575	8,979,575
Accrued salaries and related benefits	4,006,813	—	4,006,813
Intergovernmental payables:			
Federal	17,709,428	9,896,282	27,605,710
Other states	—	4,391,551	4,391,551
Current portion of capital leases payable	110,980	—	110,980
Advances from federal	—	183,874,767	183,874,767
Current portion of accrued compensated absences and related benefits	<u>2,761,515</u>	<u>—</u>	<u>2,761,515</u>
Total current liabilities	<u>32,032,231</u>	<u>210,961,526</u>	<u>242,993,757</u>
Non-current liabilities:			
Advances from federal government, net of current portion	—	783,193,476	783,193,476
Non-current portion of capital leases payable	9,459	—	9,459
Accrued compensated absences and related benefits	<u>1,027,325</u>	<u>—</u>	<u>1,027,325</u>
Total non-current liabilities	<u>1,036,784</u>	<u>783,193,476</u>	<u>784,230,260</u>
Total liabilities	<u>33,069,015</u>	<u>994,155,002</u>	<u>1,027,224,017</u>
<b>Net Assets (Deficit):</b>			
Invested in capital assets, net of related debt	22,134,274	—	22,134,274
Restricted for debt service	13,848,414	—	13,848,414
Unrestricted	4,384,644	(588,095,425)	(583,710,781)
Total net assets (deficit)	<u>40,367,332</u>	<u>(588,095,425)</u>	<u>(547,728,093)</u>
Total liabilities and net assets	<u>\$ 73,436,347</u>	<u>\$ 406,059,577</u>	<u>\$ 479,495,924</u>

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

South Carolina Department of Employment and Workforce  
Statement of Activities  
Year ended June 30, 2011

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, workforce development, and training services	\$ 179,531,527	\$ 30,551,850	\$ 156,852,702	\$ 7,873,025	\$ —
Business-type activities: Unemployment benefits	<u>2,171,063,209</u>	<u>517,502,522</u>	<u>1,791,424,360</u>	<u>—</u>	<u>137,863,673</u>
Totals	<u>\$ 2,350,594,736</u>	<u>\$ 548,054,372</u>	<u>\$1,948,277,062</u>	<u>7,873,025</u>	<u>137,863,673</u>
		General revenues:			
				433,307	—
				(35,229)	—
				—	35,188,745
				(189,091)	—
			Total general revenue (expenses) and transfers	<u>208,987</u>	<u>35,188,745</u>
			Increase in net assets	8,082,012	173,052,418
			Net assets (deficit) – beginning	<u>32,285,320</u>	<u>(761,147,843)</u>
			Net assets (deficit) – ending	<u>\$ 40,367,332</u>	<u>\$ (588,095,425)</u>

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

South Carolina Department of Employment and Workforce  
Balance Sheet  
Governmental Fund – Special Revenue  
June 30, 2011

<b>Assets:</b>	
Cash and cash equivalents	\$ 8,296,144
Restricted cash	13,848,414
Assessments receivable, net	9,926,251
Intergovernmental receivables:	
Federal	13,518,586
State agencies	344,838
Interfund receivable – unemployment compensation fund	5,087,092
Prepaid items	<u>160,309</u>
 Total assets	 <u>\$ 51,181,634</u>
 <b>Liabilities and Fund Balances:</b>	
Liabilities:	
Accounts payable	\$ 7,443,495
Intergovernmental payables:	
Federal	17,709,428
Accrued salaries and related benefits	<u>4,006,813</u>
 Total liabilities	 <u>29,159,736</u>
 Fund balances:	
Non-spendable:	
Prepaid items	160,309
Restricted:	
Debt service	13,848,414
Reed Act expenditures	47,779
South Carolina Occupational Information Coordinating Committee	213,740
Assigned fund balance	<u>7,751,656</u>
 Total fund balances	 <u>22,021,898</u>
 Total liabilities and fund balances	 <u>\$ 51,181,634</u>

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

South Carolina Department of Employment and Workforce  
 Balance Sheet  
 Governmental Fund – Special Revenue (Continued)  
 June 30, 2011

**Reconciliation to the Statements of Net Assets:**

Fund balances – governmental funds		\$ 22,021,898
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	(120,439)	
Accrued compensated absences	<u>(3,788,840)</u>	(3,909,279)
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>22,254,713</u>
Net assets – governmental activities		<u>\$ 40,367,332</u>

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

South Carolina Department of Employment and Workforce  
Statement of Revenues, Expenditures, and Changes in Fund Balances  
Governmental Fund – Special Revenue  
Year ended June 30, 2011

**Revenues:**

Employer tax contingency assessments	\$ 8,206,459
Employer tax penalties and interest	988,861
Interest surcharge	21,291,426
User fees	5,465
Intergovernmental:	
Federal	146,441,049
State of South Carolina	433,307
Local	9,978,346
Other	59,639
Total Revenues	187,404,552

**Expenditures:**

Employment and training administration	56,543,075
Contingency assessments	5,627,842
Penalties and interest	1,016,450
Workforce Investment Act	67,196,604
Trade Adjustment Assistance	15,119,107
Other federal programs	3,930,409
Other non-federal programs	9,929,897
Parking	44,742
Occupational Information Coordinating Committee	448,285
Capital outlay	2,047,355
Debt service:	
Principal	106,444
Interest	17,716,888
Total Expenditures	179,727,098

Excess of Revenues Over Expenditures	7,677,454
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Other Financing Uses:

Indirect costs remitted to General Fund of the State	189,091
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Total Other Financing Uses	189,091
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Net Change in Fund Balance	7,488,363
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Beginning Fund Balance	14,533,535
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Ending Fund Balance	\$ 22,021,898
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*The accompanying notes are an integral part of these financial statements.*

South Carolina Department of Employment and Workforce  
Statement of Revenues, Expenditures, and Changes in Fund Balances  
Governmental Fund – Special Revenue (Continued)  
Year ended June 30, 2011

**Reconciliation to the Statement of Activities:**

Expenditures and other financing uses over revenues and other financing sources for the governmental fund	\$ 7,488,363
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	2,047,355
Depreciation of capital assets is reported as an expense in the statement of activities	(1,537,916)
The carrying values of capital assets disposed of are reported as expenses in the statement of activities	(35,229)
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	106,444
Net decrease in accrued compensated absences is reported as an increase of expenses in the statement of activities	<u>12,995</u>
Increase in net assets	<u>\$ 8,082,012</u>

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

South Carolina Department of Employment and Workforce  
Statement of Net Assets  
Proprietary Fund  
June 30, 2011

**Assets:**

Current assets:

Cash and cash equivalents	\$ 260,981,907
Assessments receivable, net	126,936,099
Benefit overpayments receivable, net	10,627,713
Due from reimbursable employers, net	1,508,560
Intergovernmental receivables, net:	
Federal	3,594,035
State agencies	2,320,509
Local governments	3,459,727
Other states	1,718,119
Total assets	\$ 411,146,669

**Liabilities:**

Current liabilities:

Benefits payable	\$ 3,778,647
Tax withholdings payable	40,704
Contributions payable	8,979,575
Intergovernmental payables:	
Federal	9,896,282
Other states	4,391,551
Interfund payable – Department	5,087,092
Advances from federal government	183,374,767
Total current liabilities	215,548,618

Advances from federal government, net of current portion	783,693,476
Total liabilities	999,242,094

**Net Deficit Assets:**

Unrestricted	(588,095,425)
Total liabilities and net assets	\$ 411,146,669

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

South Carolina Department of Employment and Workforce  
Statement of Revenues, Expenses, and Changes in Fund Net Assets  
Proprietary Fund  
Year ended June 30, 2011

<b>Operating Revenues:</b>	
Assessments	\$ 502,622,038
Reimbursement of unemployment compensation benefits from employers	5,946,656
Benefit overpayment recoveries	8,933,828
Intergovernmental:	
Federal	1,753,813,746
State agencies	10,042,141
Other states	8,548,524
Local governments	19,019,949
Total operating revenues	<u>2,308,926,882</u>
 <b>Operating Expenses:</b>	
Unemployment compensation benefits	<u>2,171,063,209</u>
Total operating expenses	<u>2,171,063,209</u>
Operating income	<u>137,863,673</u>
 <b>Non-operating revenue:</b>	
Gain on forgiveness of debt	<u>35,188,745</u>
Total non-operating revenues	<u>35,188,745</u>
Changes in net assets	173,052,418
<b>Total net deficit – beginning</b>	<u>(761,147,843)</u>
<b>Total net deficit – ending</b>	<u>\$ (588,095,425)</u>

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

South Carolina Department of Employment and Workforce  
Statement of Cash Flows  
Proprietary Fund  
Year ended June 30, 2011

<b>Cash flows provided by operating activities:</b>	
Cash received from assessments	\$ 424,942,221
Cash received from employers	6,014,734
Cash received from benefit overpayment recoveries	4,970,992
Cash received from federal, state and local agencies	1,821,405,854
Benefits paid	(2,180,196,869)
Refund overpayment of assessments	(2,981,905)
Net cash provided by operating activities	74,155,027
 <b>Cash flows provided by non-capital financing activities:</b>	
Proceeds from advances from federal government	115,594,636
Net cash provided by non-capital financing activities	115,594,636
Net increase in cash	189,749,663
<b>Cash and cash equivalents – beginning</b>	71,232,244
<b>Cash and cash equivalents – ending</b>	\$ 260,981,907
 Reconciliation of operating income to net cash provided by operating activities:	
Operating income	\$ 137,863,673
Net changes in assets and liabilities:	
Assessments receivable	(77,526,374)
Benefit overpayments receivable	(3,962,836)
Due from reimbursable employers	68,078
Intergovernmental receivables:	
Local governments	482,350
State agencies	1,950,206
Other states	686,969
Federal	26,861,969
Benefits payable	(16,905,933)
Tax withholdings payable	(43,009)
Contributions payable	2,171,441
Interfund payable – Department	(3,135,348)
Intergovernmental payable:	
Federal	5,996,009
Other states	(352,168)
Net cash provided by operating activities	\$ 74,155,027

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

# South Carolina Department of Employment and Workforce

## Notes to Financial Statements

### **Note 1. Liquidity**

Over the last decade, the Trust Fund generated substantial operating losses and was required to use all of its cash resources to fund the continued payment of unemployment insurance benefits. Revised tax legislation, effective January 1, 2011, significantly increased tax assessment revenues for the Trust Fund. Cash balances at June 30, 2011 consist primarily of funds received from employers and held in the State of South Carolina's ("State") account in the Federal Unemployment Compensation Fund for purposes of paying state unemployment insurance benefits and repaying principle on advances from the federal unemployment account. Due to the increasing unemployment rate and the resulting increased amount of unemployment benefits paid, and the increased length of time over which the benefits are paid, the Fund was required to obtain advances from the Federal Unemployment Account ("FUA") of \$115,594,636 and \$541,780,847 during the years ended June 30, 2011 and 2010, respectively.

Increased tax collections, coupled with decreases in the number of individuals eligible for and claiming State unemployment insurance benefits, have enabled the Trust Fund to operate without obtaining additional advances from the federal government since April of 2011. The federal government has not established a maximum amount that the Fund can borrow.

In addition, Note 16 discusses State supplemental funding provided via SC FY 11-12 Proviso 90.18, subsequent to year-end. These amounts offset cash collected from business via SUTA revenues with supplemental funding from various State sources.

Legislative reforms to the State's unemployment insurance tax structure, effective on tax assessments for the first quarter of the 2011 calendar year, were specifically designed to assist in putting the Trust Fund back on the path to solvency, including providing for timely repayment of federal unemployment account balances. These changes are addressed in Note 14.

### **Note 2. Summary of Significant Accounting Policies**

#### ***Reporting Entity***

The accounting policies of the Agency 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 Agency'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 Agency has determined it has no component units. The primary government is the State of South Carolina. The State has determined that the Agency 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.

South Carolina Department of Employment and Workforce

Notes to Financial Statements

**Note 2. Summary of Significant Accounting Policies (continued)**

***Reporting Entity (continued)***

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.

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 Agency 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. On March 30, 2010, the Governor of South Carolina signed into law Act 159 restructuring the Agency into a State cabinet agency under the Governor. The Commission merged with the Workforce Development division of the South Carolina Department of Commerce to become the South Carolina Department of Employment and Workforce. Act 159 designated the Department of Employment and Workforce as the entity responsible for the administration of Workforce Investment Act ("WIA") and Trade Adjustment Assistance ("TAA") activities and for carrying out all functions necessary to comply with WIA and the Trade Act of 1974, as amended by the Trade and Globalization Adjustment Assistance Act of 2009. The administrative costs of the Agency are paid from grants primarily from the United States Department of Labor ("US DOL").

The Unemployment Insurance Program collects taxes from employers covered by the law, and pays out unemployment benefits to eligible unemployed citizens under both state and federal law.

# South Carolina Department of Employment and Workforce

## Notes to Financial Statements

### **Note 2. Summary of Significant Accounting Policies (continued)**

#### ***Reporting Entity (continued)***

The Employment Services Program operates as a free labor exchange where workers and jobs are brought together in local “SC Works” centers 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 (“UI”) claimants. In addition, the Agency maintains a comprehensive Labor Market Information Program, which collects and disseminates employee statistics, job forecasts, wage information, demographics, and other information in cooperation with the US DOL’s Bureau of Labor Statistics.

The Agency 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 Agency. The Appropriations Act authorizes expenditures from the General Fund of the State and authorizes expenditures of total funds.

#### ***Governmental 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 Agency reporting entity defined above.

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 Agency’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 Agency 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:

*Employment and Training Administration* (“ETA Administrative”) – The division of the US DOL which administers Employment Services and Unemployment Insurance includes administrative funds in the UI, Employment Service (“ES”), and ES Reimbursable Programs.

*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 State unemployment taxes fund unemployment compensation benefits in the proprietary fund.

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

## South Carolina Department of Employment and Workforce

### Notes to Financial Statements

#### **Note 2. Summary of Significant Accounting Policies (continued)**

##### ***Governmental Funds (continued)***

*Unemployment Compensation Modernization Incentive Payments (“Modernization”)* – This is a special transfer of funds from the US DOL to the Agency’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”)* – The SCOICC was established in 1977 as a consortium of agencies mandated by the Carl D. Perkins Vocational Education Act. 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 education programs and the employment and training programs at national, state, and local levels. These functions have primarily been delivered by the on-line Career Information System referred to as the South Carolina Occupational Information System (“SCOIS”). SCOIS also develops printed career development products for schools grade K-12. The SCOICC is charged with giving special attention to the career and educational needs of individuals involved in career decision making. The SCOIS system delivers up-to-date occupational, educational, employment and career guidance information to career decision makers and job seekers. The SCOICC is funded by an appropriation from the State of South Carolina to support its operations. All school districts in South Carolina have free access to the SCOIS Career System.

*Workforce Investment Act (“WIA”)* – WIA is a federal program administered in South Carolina through the Workforce Division of the Department of Employment and Workforce and through 12 Workforce Investment areas throughout the State. A statewide board appointed by the Governor and comprised of business owners, state government officials, educators and private citizens guides policy for all WIA-funded programs. WIA programs help businesses meet their need for skilled workers and provide individuals with access to training that helps them prepare for work.

*Trade Adjustment Assistance (“TAA”)* - TAA is a federal program of the US DOL that provides reemployment services to workers who have been adversely impacted by increased imports or by a shift in production or services to another country. The goal of the TAA program is to help workers become reemployed in a suitable job as quickly as possible.

##### ***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 Agency’s proprietary fund is from assessments to employers and reimbursement from the federal government for the payment of unemployment benefits. The Agency’s proprietary fund is used to account for the Trust Fund.

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.

South Carolina Department of Employment and Workforce

Notes to Financial Statements

**Note 2. Summary of Significant Accounting Policies (continued)**

***Proprietary Funds (continued)***

The Trust Fund includes the following accounts:

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

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

*Unemployment Compensation for Ex-Servicemen (“UCX”)* – This fund accounts for unemployment compensation paid to ex-servicemen and is funded by the federal government.

*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.

*Alternative Trade Adjustment Assistance Program (“ATAA”)* - This fund 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.

*Reemployment Trade Adjustment Assistance (“RTAA”)* – This program was implemented in fiscal year 2009 as a wage option available to older workers under the TAA program to eventually replace ATAA. Consists of monies paid to individuals age 50+ who had lost their jobs due to imports but are now working again at a lower salary. They are paid 50% of the difference in their old and new salary. It is funded by the federal government.

*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 predetermined level. The minimum time period for these benefits is a thirteen week period. All benefits which are not reimbursable by other states are funded by the federal government and partially funded with ARRA funds. See subsequent event disclosure related to changes in this program passed by Congress subsequent to year-end.

*Emergency Unemployment Compensation Tier I (“EUC 08”)* - The Emergency Unemployment Compensation (“EUC”) program, created in June 2008 and expanded in November 2008, provides up to 20 weeks of benefits to eligible jobless workers in all states and up to 13 additional weeks of benefits in states with high unemployment. It was set to expire on March 31, 2009. The ARRA extended the date for new EUC claims to December 31, 2009, with payments on those claims ending on May 31, 2010. The Unemployment Compensation Extension Act of 2010 extended the date for new EUC claims to November 30, 2010, with payments on those claims ending April 30, 2011. The date was extended again for new claims to be filed by December 24, 2011 with the last week payable of June 9, 2012. It is funded by the federal government and partially funded with ARRA funds. See subsequent event disclosure related to changes in this program passed by Congress subsequent to year-end.

South Carolina Department of Employment and Workforce

Notes to Financial Statements

**Note 2. Summary of Significant Accounting Policies (continued)**

***Proprietary Funds (continued)***

*Emergency Unemployment Compensation Tier II (“EUC 2”)* – 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, 2011, with payments on those claims ending on June 9, 2012. It is funded by the federal government. See subsequent event disclosure related to changes in this program passed by Congress subsequent to year-end.

*Emergency Unemployment Compensation Tier II, wk 14 (“EUC 2 wk 14”)* - This is the 14<sup>th</sup> week of EUC2 which was granted subsequent to EUC3 and EUC4 and allows an extra week of EUC2 claims to be paid to eligible claimants. It is funded by the federal government. See subsequent event disclosure related to changes in this program passed by Congress subsequent to year-end.

*Emergency Unemployment Compensation Tier III (“EUC 3”)* - This is an additional 13 week expansion of the EUC 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, 2011 with payments on those claims ending on June 9, 2012. It is funded by the federal government. See subsequent event disclosure related to changes in this program passed by Congress subsequent to year-end.

*Emergency Unemployment Compensation Tier IV (“EUC 4”)* - This is an additional 6 week expansion of the EUC 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, 2010 with payments on those claims ending on June 9, 2011. It is funded by the federal government. See subsequent event disclosure related to changes in this program passed by Congress subsequent to year-end.

*Federal Additional Compensation (“FAC”)* – This provides a \$25 weekly supplement to the unemployment compensation of eligible claimants. It is funded by the federal government through stimulus funds under ARRA. The June 2, 2010 end date for new FAC claims was not extended under the Unemployment Compensation Extension Act of 2010.

***Government-wide and Fund Financial Statements***

The financial statements of the Agency 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.

Notes to Financial Statements

**Note 2. Summary of Significant Accounting Policies (continued)**

***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 Agency 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 Agency 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 Agency 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 Agency 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.

***Budget Policy***

The Agency is granted an annual appropriation for operating purposes by the General Assembly. The appropriation as enacted becomes the legal operating budget for the Agency. 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.

South Carolina Department of Employment and Workforce

Notes to Financial Statements

**Note 2. Summary of Significant Accounting Policies (continued)**

***Budget Policy (continued)***

The Agency's budget is not presented for comparison purposes because GASB 34 requires only major special revenue funds of the State to present such information. Since the Agency 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 Agency, participate in the State's internal cash management pool. Because the internal 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 internal 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 internal 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 Agency 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.

***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.

# South Carolina Department of Employment and Workforce

## Notes to Financial Statements

### **Note 2. Summary of Significant Accounting Policies (continued)**

#### ***Receivables (continued)***

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 Agency is required to notify employers of such tax delinquencies. If the delinquent amount is not paid within ten days thereafter, the Agency is directed to initiate a collection notification process consisting of follow-up notices, telephone calls, and ultimately the issuance of 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 Agency 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 Agency.

#### 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 Agency 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.

#### Allowance for Uncollectibles

The allowance for uncollectibles is computed based upon an estimate of collections with all receivables over 24 months old being allowed for as doubtful accounts.

# South Carolina Department of Employment and Workforce

## 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 Agency 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 Agency 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 full-time equivalent 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 Agency 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 Agency 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 Agency and services provided by other State agencies. During the period July 1, 2010 through June 30, 2011, the Agency recovered approximately \$11,338,642 of indirect cost from the indirect cost agreement. Of this amount, approximately \$189,091 was remitted to the State and approximately \$11,149,551 was retained by the Agency. Indirect cost recoveries are reported as federal revenues.

## South Carolina Department of Employment and Workforce

### 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 Agency'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 Agency 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 Agency 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. Unassigned 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 Department of Employment and Workforce

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."

The Agency has adopted GASB Statement No. 54, Fund Balance Reporting and Governmental Fund Type Definitions (required implementation date of June 2011). This Statement establishes criteria for classifying governmental fund balances into specifically defined classifications. Classifications are hierarchical and are based primarily on the extent to which the Agency is bound to honor constraints on the specific purposes for which amounts in the funds may be spent. Application of the Statement requires the Agency to classify and report amounts in the appropriate fund balance classifications. The Agency's accounting and finance policies are used to interpret the nature and/or requirements of the funds and their corresponding assignment of restricted, committed, assigned, or unassigned. Fund balances are classified as follows:

*Non-spendable* – Amounts that cannot be spent either because they are not in a spendable form, such as inventory or prepaid insurance, or because they are legally or contractually required to be maintained intact – such as a trust.

*Restricted* – amounts that can be spent only for specific purposes because of Agency ordinances, state or federal laws, or externally imposed conditions by grantors or creditors – such as the surcharge adopted to pay the Trust Funds debt.

*Committed* – amounts constrained to specific purposes by the Agency itself, using the highest level of decision-making authority. To be reported as committed, amounts cannot be used for any other purpose unless the Agency takes the same highest level action to remove or change the constraint.

*Assigned* – amounts the Agency intends to use for a specific purpose. Intent can be expressed by an official or body to which the Agency delegates the authority.

*Unassigned* – all amounts not included in other spendable classifications.

The Agency permits funds to be expended in the following order: committed, assigned, and unassigned.

South Carolina Department of Employment and Workforce

Notes to Financial Statements

**Note 2. Summary of Significant Accounting Policies (continued)**

*Net Assets / Fund Balances (continued)*

At June 30, 2011, three of the Agency's restricted balances are as follows:

Debt service – The Trust Fund has received advances of approximately \$967 million from the federal government as of June 30, 2011. By law, the Trust Fund is a proprietary fund and only permitted to pay unemployment benefits. Therefore debt service of the interest due on the advances must be accounted for in the governmental funds of the Agency. At June 30, 2011, approximately \$13.8 million is restricted for debt service of the interest.

Reed Act – The Agency has no funds available under the Reed Act in the proprietary funds. During 2010, 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 2011, \$162,221 was spent from the previously appropriated funds and \$47,779 is shown as a restricted 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 Agency 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 2011 Appropriation Act Proviso 67.1, all user fees not expended in fiscal year 2010 may be carried forward to fiscal year 2011 for use in the SCOICC program. As of June 30, 2011, \$213,740 was carried forward and is reported as a restricted 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.

**Note 3. Deposits**

The amount shown as cash and cash equivalents in the statement of net assets at June 30, 2011 is composed of the following:

Cash on hand	\$ 1,500
Deposits held by State Treasurer	25,247,234
Deposits held by U.S. Treasury	244,275,981
Other deposits	13,601,750
Totals	<u>\$ 283,126,465</u>

South Carolina Department of Employment and Workforce

Notes to Financial Statements

**Note 3. Deposits (continued)**

**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, 2011, 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. However, individual states are not due any interest while carrying federal unemployment account advances on their books.

**Other Deposits**

Custodial credit risk for deposits is the risk that in the event of a depository financial institution's failure, the Agency's deposits may not be returned or the Agency 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 Agency 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 Agency's name.

The Agency 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.

**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 as of June 30, 2011 are as follows:

Contingency assessments	\$ 103,441
Penalty and interest	167,099
Special administration funds	4,396,500
Interest surcharge	394,319
Reed Act	25,733
Total	<u>\$ 5,087,092</u>

South Carolina Department of Employment and Workforce

Notes to Financial Statements

**Note 5. Receivables**

The receivable balances at June 30, 2011 and the related amounts for allowances for uncollectibles are as follows:

	Receivables	Allowances for Uncollectibles	Net Receivables
Special revenue fund:			
Assessments receivable:			
Contingency	\$ 2,308,444	\$ (217,833)	\$ 2,090,611
Penalty and interest	4,494,918	(3,707,970)	786,948
Interest surcharge	7,587,523	(538,831)	7,048,692
Intergovernmental receivables:			
Federal	\$ 13,518,586	\$ —	\$ 13,518,586
State agencies	344,838	—	344,838
Totals	\$ 28,254,309	\$ (4,464,634)	\$ 23,789,675

	Receivables	Allowances for Uncollectibles	Net Receivables
Proprietary fund:			
Assessments receivable	\$ 139,401,750	\$ (12,465,651)	\$ 126,936,099
Due from reimbursable employers	1,631,050	(122,490)	1,508,560
Intergovernmental receivables			
Local governments	3,497,110	(37,383)	3,459,727
State agencies	2,320,509	—	2,320,509
Other states	1,718,119	—	1,718,119
Federal	3,594,035	—	3,594,035
Benefit overpayments receivable:			
Basic unemployment compensation (UI)	10,016,293	(3,632,023)	6,384,270
Federal employees (UCFE)	78,289	(70,212)	8,077
Ex-servicemen (UCX)	64,254	(55,720)	8,534
Trade readjustment compensation (TRA)	78,445	(37,508)	40,937
Emergency Unemployment Compensation (EUC)	9,270,228	(5,084,333)	4,185,895
Totals	\$ 171,670,082	\$ (21,505,320)	\$ 150,164,762

South Carolina Department of Employment and Workforce

Notes to Financial Statements

**Note 6. Capital Assets**

A summary of capital assets activity for the year ended June 30, 2011 is as follows:

	<u>Balances June 30, 2010</u>	<u>Increases and Reclassifications</u>	<u>Decreases and Reclassifications</u>	<u>Balances June 30, 2011</u>
Capital assets not being depreciated:				
Land and land improvements	\$ 3,419,379	\$ —	\$ —	\$ 3,419,379
Construction in progress	—	1,498,080	—	1,498,080
<b>Total capital assets not being depreciated</b>	<b>3,419,379</b>	<b>1,498,080</b>	<b>—</b>	<b>4,917,459</b>
Other capital assets:				
Buildings and improvements	30,593,198	—	—	30,593,198
Equipment and furniture	5,205,194	351,526	(1,318,279)	4,238,441
Vehicles	375,724	—	(56,802)	318,922
Intangible assets	5,073,784	813,040	—	5,886,824
<b>Total other capital assets</b>	<b>41,247,900</b>	<b>1,164,566</b>	<b>(1,375,081)</b>	<b>41,037,385</b>
Less accumulated depreciation for:				
Buildings and improvements	14,353,567	753,868	—	15,107,435
Equipment and furniture	4,270,474	427,742	(1,763,106)	2,935,110
Vehicles	331,015	20,191	(51,159)	300,047
Intangible assets	3,931,720	1,425,819	—	5,357,539
<b>Total accumulated depreciation</b>	<b>22,886,776</b>	<b>2,627,620</b>	<b>(1,814,265)</b>	<b>23,700,131</b>
<b>Other capital assets, net</b>	<b>18,361,124</b>	<b>(1,463,054)</b>	<b>439,184</b>	<b>17,337,254</b>
<b>Total capital assets, net</b>	<b>\$ 21,780,503</b>	<b>\$ 35,026</b>	<b>\$ 439,184</b>	<b>\$ 22,254,713</b>

Depreciation expense was approximately \$1,538,000. Total outstanding commitments on projects that will not be capitalized were approximately \$26,000.

**Note 7. Long-Term Liabilities**

A summary of changes in long-term liabilities for the year ended June 30, 2011 is as follows:

<b>Governmental</b>	<u>Balance, July 1, 2010</u>	<u>Additions</u>	<u>Reductions</u>	<u>Balance, June 30, 2011</u>	<u>Due within one year</u>
Capital lease payable	\$ 226,883	\$ —	\$ 106,444	\$ 120,439	\$ 110,980
Accrued compensated absences and related benefits	3,801,835	2,802,301	2,815,296	3,788,840	2,761,515
	<u>\$ 4,028,718</u>	<u>\$ 2,802,301</u>	<u>\$ 2,921,740</u>	<u>\$ 3,909,279</u>	<u>\$ 2,872,495</u>

South Carolina Department of Employment and Workforce

Notes to Financial Statements

**Note 7. Long-Term Liabilities (continued)**

Business-type	Balance, July 1, 2010	Additions	Reductions	Balance, June 30, 2011	Due within one year
Advances from federal government	\$886,662,352	\$115,594,636	\$ 35,188,745	\$967,068,243	\$183,874,767
	<u>\$886,662,352</u>	<u>\$115,594,636</u>	<u>\$ 35,188,745</u>	<u>\$967,068,243</u>	<u>\$183,874,767</u>

**Note 8. Leases**

During 2011, the Agency 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 \$154,000 as of June 30, 2011. The current year's amortization expense of approximately \$94,000 on the capitalized lease assets is included in depreciation expense. Total payments on the capital leases for the year ended June 30, 2011 were \$113,904 consisting of principal of \$106,444 and interest of \$7,460.

The Agency 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 2011 through 2015. 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 Agency is responsible for maintenance on most leased property. Rental expenditures for office space and equipment were approximately \$1,089,000 for the year ended June 30, 2011.

The following is a schedule by years of future minimum rental payments required under the capital lease and the noncancelable operating lease agreements with remaining terms at June 30, 2011 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
	2012	\$ 113,904	\$ 46,329
	2013	9,492	42,864
	2014	—	42,864
	2015	—	42,864
Total minimum lease payments		<u>123,396</u>	<u>\$ 174,921</u>
Less: interest		<u>(2,957)</u>	
Present value of minimum lease payments		<u>\$ 120,439</u>	

**Note 9. Pension Plans**

The majority of employees of the Agency are covered by a retirement plan through the South Carolina Retirement 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 full-time equivalent 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.

## South Carolina Department of Employment and Workforce

### Notes to Financial Statements

#### **Note 9. Pension Plans (continued)**

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.

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 earn service credit, and are ineligible to receive group life insurance benefits or disability retirement benefits.

Effective July 1, 2006, employees participating in the SCRS were required to contribute 6.50% of all compensation. Effective July 1, 2010, the employer contribution rate became 13.14%, which included a 3.90% surcharge to fund retiree health and dental insurance coverage. The Agency’s actual contributions to the SCRS for the years ended June 30, 2011, 2010, and 2009 were approximately \$5,149,200, \$5,351,400, and \$4,870,600, respectively, and equaled the required contributions of 9.24% (excluding the surcharge) for each year. Also, the Agency paid employer group life insurance contributions of approximately \$59,000, \$63,000, and \$57,000 at the rate of .15% of compensation for the current fiscal years ended June 30, 2011, 2010, and 2009 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.

## South Carolina Department of Employment and Workforce

### Notes to Financial Statements

#### **Note 9. Pension Plans (continued)**

Since July 1, 1988, employees participating in the PORS have been required to contribute 6.50% of all compensation. Effective July 1, 2010, the employer contribution rate became 15.03% which, as for the SCRS, included the 3.90% surcharge. The Agency's actual contributions to the PORS for the years ended June 30, 2011, 2010 and 2009, were approximately \$23,000, \$21,000, and \$16,000, respectively, and equaled the required contributions of 11.13% (excluding the surcharge) for each year. Also, the Agency paid employer group-life insurance contributions of approximately \$300 and accidental death insurance contributions of approximately \$300 in the current fiscal year for PORS participants. The rate for each of these insurance benefits is 0.20% of compensation.

New 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 benefits through contributions to a 401(a) with one of four approved vendors. The State assumes no liability for this plan other than for payment of contributions to designated companies. To elect participation in the ORP, eligible employees must elect membership within their first 30 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 3.90% from the employer in fiscal year 2011.

For the fiscal year, total contributions requirements to the ORP were approximately \$13,000 (excluding the surcharge) from the Agency as employer and approximately \$16,000 from its employees as plan members.

Employer contributions in the amount of 8.14% were remitted to the Retirement Division of the State Budget and Control Board. Also, the Agency paid employer group life insurance contributions of approximately \$380 in the current fiscal year at the rate of 0.15% 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 Agency 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 does not make separate measurements of assets and pension benefit obligations for individual employers. Under Title 9 of the South Carolina Code of Laws, the Agency'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 Agency'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 Agency recognizes no contingent liability for unfunded costs associated with participation in the plans.

## South Carolina Department of Employment and Workforce

### Notes to Financial Statements

#### **Note 9. Pension Plans (continued)**

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

#### **Note 10. Post-Employment Benefits Other than Pensions**

##### **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 Agency 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 25 years of service for 100% employer funding and 15 through 24 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.

##### **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% of annual covered payroll for 2011 and 2010. The EIP sets the employer contribution rate based on a pay-as-you-go basis. The Agency paid approximately \$1,666,000 and \$1,685,000 applicable to the surcharge included with the employer contribution for retirement benefits for the fiscal years ended June 30, 2011 and 2010, 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, 2011 and 2010. The Agency recorded employer contributions expenses applicable to these insurance benefits for active employees in the amount of approximately \$4,443,000 and \$4,843,000 for the years ended June 30, 2011 and 2010, 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.

## South Carolina Department of Employment and Workforce

### Notes to Financial Statements

#### **Note 10. Post-Employment Benefits Other than Pensions (continued)**

##### **Funding Policies (continued)**

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.

#### **Note 11. Deferred Compensation Plans**

Several optional deferred compensation plans are available to State employees and employers of its political subdivisions. Certain employees of the Agency 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 12. Risk Management**

The Agency 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 Agency 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 Agency Fund);
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.

## South Carolina Department of Employment and Workforce

### Notes to Financial Statements

#### **Note 12. Risk Management (continued)**

The Agency 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.

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 IRF.

The Agency 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 Agency 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 Agency'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 13. Transactions with State Agencies**

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

The Agency was required to remit \$189,091 of indirect cost recoveries to the General Fund of the State in payment of services received from State agencies including 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 Department of Archives and History.

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

South Carolina Department of Employment and Workforce

Notes to Financial Statements

**Note 13. Transactions with State Agencies (continued)**

The Agency had financial transactions with various State agencies during the fiscal year. Payments were made to divisions of the SBCB 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 related party transactions with State agencies in the governmental fund – special revenue are as follows for the year ended June 30, 2011:

Technical and Computer Education Board	\$2,093,624
Budget and Control Board	1,397,719
Department of Commerce	512,453
Department of Social Services	273,101
University of South Carolina	242,423
State Accident Fund	242,081
Legislative Audit Council	239,187
Francis Marion University	163,178
Comptroller General	130,711
Department of Education	53,036
Winthrop University	45,398
Clemson University	43,373
Other	91,671
	<u>\$ 5,527,955</u>

In the governmental fund - special revenue, the Agency received \$433,307 from State appropriations during the year for expenditures of the SCOICC. In the proprietary fund, the Agency recorded revenues of approximately \$10,042,000 for reimbursements of benefits paid to State employees and was due approximately \$2,321,000 for these benefits at year-end.

**Note 14. 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, 2011 and 2010, the outstanding balance of these advances was approximately \$967 million and \$887 million, respectively. Interest payments are required to begin on September 30, 2011 with interest accruing at a rate of approximately four (4) percent beginning on January 1, 2011. Of the \$967 million total loan principal, approximately \$784 million is reported as a non-current liability, and \$183 million is reported as being due within one year.

## South Carolina Department of Employment and Workforce

### Notes to Financial Statements

#### **Note 14. Advances from Federal Government (continued)**

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. For the fiscal year ended June 30, 2011, a total of \$35,188,745 was applied to reduce the balance of federal unemployment account advances to the Fund as a result of the reduced FUTA credits. This amount has been reported as non-operating revenue in the Statements of Revenues, Expenses, and Changes in Fund Net Deficit. The current tax system along with non-recurring revenues appropriated to the Agency by the general assembly was utilized to make principal payments on the federal advances in amounts sufficient to avoid the FUTA credit reduction for state employers for the 2011 tax year.

As mentioned in Note 1, comprehensive changes to the State's UI tax structure have been implemented and specifically designed to assist in putting the Fund back on the path to solvency. State unemployment tax rates for future years will be structured to raise revenues that more accurately address the demands on the Fund and the changing economic environment in which the Fund operates. While the Fund remains in federal loan status, required tax revenues will consist of estimated benefit payouts for the subsequent year, an amount required to repay the principal on all outstanding federal advances over five years, and an additional surcharge designated to pay accrued interest on outstanding advances. As the expected level of state UI benefits continues to decrease, a greater proportion of state UI tax revenues will be available to repay the advanced funds.

Increased tax collections coupled with decreases in the number of individuals eligible for and claiming state UI benefits have enabled the Fund to operate without obtaining additional advances from the federal government since April 2011. Federal regulations specify that interest on federal unemployment account advances may not be paid, either directly or indirectly, from the Fund; therefore, no accrued interest is reported in the financial statements of the Fund. The Fund has not been required to borrow from the federal government since April 2011. In addition, the State applied for and received acceptance to avoid a second 0.3% credit reduction for tax year 2011 by meeting all FUTA credit reduction avoidance criteria during 2011. For tax year 2011, the FUTA credit will be restored in full to all qualified South Carolina businesses. Management believes the current tax system should allow South Carolina to avoid requiring any further advances from the federal government, and avoid any additional FUTA credit reductions through 2015, when all advances should be paid-off.

#### **Note 15. Contingencies**

**Federal Grants** – The various programs administered by the Agency for fiscal years June 30, 2011 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 Agency believes that any such amounts in the aggregate would not have a material adverse effect on the financial position of the Agency. Also, see information on subsequent events in Note 16 regarding new legislation and loss of administrative funding.

## South Carolina Department of Employment and Workforce

### Notes to Financial Statements

#### **Note 15. Contingencies (continued)**

**Litigation** – The Agency 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 Agency. Therefore, an estimated liability has not been recorded.

#### **Note 16. Subsequent Events**

The balance of advances from federal government is \$782,283,237 at the date of the audit report, which is net of principal payments made in September and November 2011 of \$183,874,767 and FUTA credit reductions of \$910,239 applied against the balance of advances from federal government subsequent to year-end. The Fund has not taken any additional advances from the federal government since April 2011. The Agency paid accrued interest of \$26,481,178 on September 29, 2011.

Due to a budget proviso recently enacted, which provides the Fund with \$146 million earmarked for federal loan repayments (received by the agency in September 2011), the agency was required to recalculate business unemployment taxes for 2011 retroactive to January 1, 2011. The recalculation of rates resulted in overpayments from businesses for the first two calendar quarters of 2011. Any credits resulting from the lower rates were applied to future quarters automatically. If a business was interested in receiving a refund for any overpayments made in the 2<sup>nd</sup> quarter of 2011, they began to request these refunds October 1, 2011. Approximately \$29 million was available to South Carolina businesses for cash refunds on 2<sup>nd</sup> quarter assessments. As of the date of the audit report, approximately \$7 million in refunds have been issued as a result of this budget proviso. Any overpayments associated with the 1<sup>st</sup> quarter were required to be kept on the books with the agency as a credit to be applied to future tax liability, and the estimate of this amount was approximately \$67 million.

Congress passed legislation in February 2011 that will significantly impact federally-funded unemployment compensation payments under the Extended Benefits (“EB”) and Emergency Unemployment Compensation (“EUC”) programs. Significant detailed changes, tied to an individual state’s unemployment rate, will effectively phase-out federally funded benefits under the EB and EUC programs by the end of the 2012 calendar year. Benefits under the UCFE and UCX programs for former federal and military employees will not be affected by this change. However, EUC and EB payments have represented a significant portion of the increasing totals of unemployment compensation expense, and related federal revenue since the beginning of the 2008 recession.

The Agency also expects to realize a reduction in federal administrative funding under the Unemployment Insurance program as the workloads associated with the EB and EUC programs are phased out over a one-year period. The amount of reduced administrative funding is not reasonably estimable as of the issuance of this report.

**South Carolina Department of Employment and Workforce  
Schedule of Expenditures of Federal Awards**

**Year Ended June 30, 2011**

<b>Federal Grantor/Program Title</b>	<b>Federal CFDA Number</b>	<b>Total Federal Expenditures</b>	<b>Passed Through to Sub- Recipients</b>
<b>Direct Programs:</b>			
<b>U.S. Department of Labor</b>			
Labor Force Statistics	17.002	\$ 1,193,523	\$ —
Employment Service*	17.207	10,766,640	393,298
ARRA - Employment Service*	17.207	908,856	—
Unemployment Insurance	17.225	971,461,951	—
ARRA - Unemployment Insurance	17.225	731,410,980	—
Federal Unemployment Account Advance	17.225	115,594,636	—
Trade Adjustment Assistance – Workers	17.245	15,119,107	7,721,563
Workforce Investment Act – Adult **	17.258	15,069,163	14,328,047
ARRA – Workforce Investment Act – Adult**	17.258	2,520,911	2,520,911
Workforce Investment Act – Youth**	17.259	16,766,226	15,725,365
ARRA – Workforce Investment Act – Youth**	17.259	4,550,708	4,550,708
Workforce Investment Act – National Emergency Grants**	17.277	42,678	10,291
Workforce Investment Act – Dislocated Workers**	17.278	18,131,090	17,074,800
ARRA - Workforce Investment Act – Dislocated Workers**	17.278	9,642,622	9,642,622
Quick Skills SC Project Incentive Grant	17.267	295,823	295,823
Work Opportunity Tax Credit	17.271	274,650	—
Labor Certification for Alien Workers	17.272	90,457	—
Disabled Veterans Outreach Program (DVOP)*	17.801	1,167,293	—
Local Veterans Employment Representative (LVER)*	17.804	1,513,858	—
Technical Assistance/Training	17.999	55,737	—
		1,916,576,909	72,263,428
<b>Appalachian Regional Commission</b>			
SC Jobs for America’s Graduate Program	23.002	28,435	—
Totals		\$ 1,916,605,344	\$ 72,263,428

**South Carolina Department of Employment and Workforce  
Note to Schedule of Expenditures of Federal Awards**

**Year Ended June 30, 2011**

**NOTE 1 – BASIS OF PRESENTATION**

The accompanying Schedule of Federal Awards (“Schedule”) presents the activity of all federal awards programs of the Agency for the year ended June 30, 2011. The information in the Schedule is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Expenditures for federal financial assistance awarded directly from federal agencies, as well as those passed through other government agencies, are included on the Schedule.

***Loan Program***

The amount reported in the accompanying Schedule for the loan program listed below represents federal advances during the year ended June 30, 2011 and 2010 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 Agency to pay unemployment benefits. Loans made during fiscal year 2011 and 2010 were \$115,594,636 and \$541,780,847, respectively, and the loan balance at June 30, 2011 was \$967,068,243.

**NOTE 2 – BASIS OF ACCOUNTING**

The accompanying Schedule is presented using the full accrual basis of accounting, which is described in the notes to the Agency’s basic financial statements.



**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 Department of Employment and Workforce  
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 Department of Employment and Workforce (the “Agency”) as of and for the year ended June 30, 2011, which collectively comprise the Agency’s basic financial statements and have issued our report thereon dated April 30, 2012. 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 Agency’s internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Agency’s internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Agency’s internal control over financial reporting.

A *deficiency in internal control* 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 and correct misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity’s financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiency described as item 2011-1 in the accompanying schedule of findings and questioned costs to be a material weakness.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies, or material weaknesses. However, as described in the accompanying schedule of findings and questioned costs, we identified a deficiency in internal control over financial reporting that we consider to be a material weakness and other deficiencies that we consider to be significant deficiencies.

A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider the deficiencies described as items 2011-2 to 2011-4 in the accompanying schedule of findings and questioned costs to be significant deficiencies.

### Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Agency's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

The Agency'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 Agency'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 Agency, 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 and Company LLP*

Columbia, South Carolina  
April 30, 2012

**Independent Auditors' Report on Compliance with Requirements  
That Could Have a Direct and Material Effect on 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 Department of Employment and Workforce  
Columbia, South Carolina

Compliance

We have audited the compliance of South Carolina Department of Employment and Workforce (the "Agency") with the types of compliance requirements described in the *OMB Circular A-133 Compliance Supplement* that could have a direct and material effect on each of the Agency's major federal programs for the year ended June 30, 2011. The Agency's major federal programs are identified in the summary of auditor's 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 Agency's management. Our responsibility is to express an opinion on the Agency'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 Agency's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination of the Agency's compliance with those requirements.

In our opinion, the Agency complied, in all material respects, with the compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended June 30, 2011.

Internal Control Over Compliance

Management of the Agency is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered the Agency's internal control over compliance with the requirements that could have a direct and material effect on a major federal program to determine the auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133, 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 Agency's internal control over compliance.

*A deficiency in internal control over compliance* exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct noncompliance with a type of compliance requirement of a federal program on a timely basis. A *material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis.

Our consideration of internal control over compliance was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over compliance that might be deficiencies, significant deficiencies or material weaknesses. We consider the deficiency described as item 2011-1 in the accompanying schedule of findings and questioned costs to be a material weakness as defined in the preceding paragraph.

This report is intended solely for the information and use of the State Auditor, the Governor of the State of South Carolina, management of the Agency, 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 and Company LLP*

Columbia, South Carolina  
April 30, 2012

**South Carolina Department of Employment and Workforce  
Schedule of Findings and Questioned Costs**

**Year Ended June 30, 2011**

**Section I—Summary of Auditors’ Results**

**Financial Statements:**

We have issued an unqualified opinion dated April 30, 2012 on the basic financial statements of the South Carolina Department of Employment and Workforce.

**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 April 30, 2012 on the South Carolina Department of Employment and Workforce’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? NO
- Any audit findings disclosed that are required to be reported in accordance with section 510(a) of Circular A-133? NO

**Identification of Major Programs:**

<u>CFDA Number</u>	<u>Name of Federal Program</u>
17.225	Unemployment Insurance
17.225	ARRA - Unemployment Insurance
17.225	Federal Unemployment Account Advance
17.245	Trade Adjustment Act
17.258 *	Workforce Investment Act – Adult
17.258 *	ARRA - Workforce Investment Act – Adult
17.259 *	Workforce Investment Act – Youth
17.259 *	ARRA - Workforce Investment Act – Youth
17.277 *	Workforce Investment Act – National Emergency Grants
17.278 *	Workforce Investment Act – Dislocated Workers
17.278 *	ARRA - Workforce Investment Act – Dislocated Workers

\* - part of Workforce Investment Act federal awards cluster

Dollar threshold used to be distinguished between Type A and Type B Programs: \$5,403,032

Auditee qualified as low-risk auditee? NO

**South Carolina Department of Employment and Workforce  
Schedule of Findings and Questioned Costs**

**Year Ended June 30, 2011**

**Section II- Financial Statement Findings**

**Significant Deficiencies Considered to be Material Weaknesses (This Finding Also Relates to Federal Awards:**

*2011-1: Audit Adjustments to the Financial Statements*

**Condition:**

During our audit we proposed an adjustment to expenditures and accounts payable and revenues and accounts receivable that was considered to be material to the financial statements. In addition we proposed an adjustment to the allowance for doubtful accounts that was considered to be material to the financial statements. Management agreed to the adjustments and the financial statements reflect the adjustments.

**Cause:**

Accounts payable were understated due to fiscal year 2011 transactions being coded to the general ledger in fiscal year 2012. The allowance for doubtful accounts for penalties was understated based on collections received subsequent to the year-end. These issues were probably caused by the retirement of a long time accounting employee and subsequent transition of duties to a new accountant.

**Effect:**

Accounts payable and expenditures, accounts receivable and revenues and the allowance for doubtful accounts were understated for the year ended June 30, 2011. The federal expenditures on the schedule of federal awards were also understated.

**Criteria:**

As part of the annual closing of the financial statements, the cut-off of expense recognition must be kept on the basis of accounting prescribed by generally accepted accounting principles. Accounts receivable must be examined by management for collectability and the allowance for doubtful accounts adjusted accordingly.

**Recommendation:**

Procedures should be strengthened to assure that accounts payable, accounts receivable, and related accounts are adjusted at year-end for the proper cut-off of revenues and expenditures, including federal expenditures. In addition, procedures should be strengthened for management to assess the collectability of accounts receivable.

**Significant Deficiencies Not Considered to be Material Weaknesses:**

*2011-2: Information Technology (“IT”) Contingency Plan*

**Condition:**

The Agency has not adopted an IT contingency plan.

**Cause:**

The Agency has not had the resources available to focus on preparing an IT contingency plan.

**Effect:**

The Agency’s business could be significantly interrupted or destroyed without an IT contingency plan in place in case of emergency.

**Criteria:**

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

**Recommendation:**

The Agency should adopt an IT contingency plan for emergency situations. The plan should be tested yearly to ensure the organization recovers its business functions timely under unusual conditions. IT contingency planning and testing should be an ongoing objective in the Agency’s risk assessment process and should be appropriately documented. This plan could be part of the Agency’s overall risk assessment program. We understand that subsequent to year-end funds were received to implement an IT contingency plan that will be in place by 2012.

*2011-3: IT Disaster Recovery Plan*

**Condition:**

The Agency has not adopted a disaster recovery plan for the IT department.

**Cause:**

The Agency 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 Agency should develop 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. We understand that subsequent to year-end the Agency is developing a budget in order to implement a disaster recovery plan that will be in place in 2012.

*2011-4: Access to Program and Data (Physical Security and Logical Security)*

**Condition:**

The computer room located on the second floor of the Agency'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 objective should be a part of entity's strategic planning and risk assessment process.

**South Carolina Department of Employment and Workforce  
Schedule of Findings and Questioned Costs**

**Year Ended June 30, 2011**

**Section III- Federal Award Findings and Questioned Costs**

**Significant Deficiencies Considered to be Material Weaknesses:**

*See finding 2011-1*

**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 Agency dated May 23, 2011, resulting from the audit of the financial statements and OMB Circular A-133 audit reports for the year ended June 30, 2010. We found that adequate corrective action was taken for all of the management letter comments, findings, and questioned costs except for items 2010-1, 2010-2, 2010-3 and 2010-4 which are repeated above as comments 2011-1, 2011-2, 2011-3, and 2011-4, respectively.

On approximately April 1, 2010, the WIA federal program cluster was transferred from the South Carolina Department of Commerce to the Agency. The Office of the South Carolina State Auditor ("State Auditor") audited the WIA federal program cluster for the 9 month period of July 1, 2009 to March 31, 2010 while the program was still administered by the South Carolina Department of Commerce. During their audit of the WIA federal program cluster, the State Auditor reported two significant deficiencies related to a lack of adequate documentation (finding 10P32-1) and reporting (finding 10P32-2). We found that corrective action was taken for the management comments 10P32-1 and 10P32-2.

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**Nikki R. Haley**  
Governor

**Abraham J. Turner**  
Executive Director

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April 30, 2012

**South Carolina Department of Employment and Workforce  
Corrective Action Plan**

The South Carolina Department of Employment and Workforce respectfully submits the following Corrective Action Plan for the audit of the year ended June 30, 2011 performed by the independent accounting firm:

Scott and Company LLP  
1441 Main Street, Suite 800  
Columbia, South Carolina 29202

Audit period: July 1, 2010 to June 30, 2011

**Schedule of Findings and Responses**

*2011-1: Audit Adjustments to the Financial Statements*

**Condition:**

During our audit we proposed an adjustment to expenditures and accounts payable and revenues and accounts receivable that was considered to be material to the financial statements. In addition we proposed an adjustment to the allowance for doubtful accounts that was considered to be material to the financial statements. Management agreed to the adjustments and the financial statements reflect the adjustments.

**Management's Response:**

The year under audit represents the first full year that DEW has administered the WIA program since it was moved from the Department of Commerce via executive order in 2010. The understatement of accounts payable and expenditures occurred due accounting staff interpreting WIA expenditures at the local level differently than in the prior year. All accounting staff will immediately be trained to properly and consistently account for these particular transactions in accordance with GAAP and federal regulations going forward.

The methodology for estimating the allowance for doubtful accounts for penalties was established by staff that is no longer with the agency. While this methodology likely proved adequate and reasonable at the time it was established, current leadership feels that it needs to be revisited and revamped to more appropriately estimate all allowances, with more emphasis placed on actual collections. Collectability will now be assessed by accounting staff on a regular basis to assess the effectiveness of the collections process, and to ensure its proper presentation at year-end for financial reporting purposes.

**Significant Deficiencies Not Considered to be Material Weaknesses:**

*2011-2: Information Technology ("IT") Contingency Plan*

**Condition:**

The Agency has not adopted an IT contingency plan.

**Management's Response:**

IT Continuity Plan

**Phase 1** (Contingency for outages of minutes)

The Department of Information ("DoIT") within the Agency has addressed the physical infrastructure supporting the hardware in the computer room supporting Agency mission critical systems with the implementation of an UPS (Uninterruptable Power System) to furnish battery power for the computer room for up to 80 minutes in the event of a short term power outage. The electrical grid power distribution panels in the computer room were mapped to devices and documented. An electrical engineer has been contracted with to design a gas generator system within the Agency's electrical power grid to provide for emergency electrical power generation to support the Agency's network and computer room. Once completed the physical plant infrastructure will be designed to have fault tolerance for both short and long term power outages.

**Phase 2** (Contingency for outages for indefinite time periods)

Blade servers with the VMware operating system have been implemented to allow for load balancing across servers to support recovery from a failing server. A remote storage device has been located with the Agency complex to provide for real time remote shadowing copying of data to support data recovery resulting from a storage device hardware failure.

Disaster recovery planning meetings have been held with the South Carolina Budget and Control Board Division of State Information Technology on the recovery times and cost(s) of using the Board's disaster recovery contract with SunGard systems. Pre-planning communications have been held with Clemson University Division of IT to discuss utilizing the university's computer room to host Agency owned equipment that would be used as an offsite disaster recovery data repository and emergency computer operations center to recover Agency IT systems. Hardware quotes have been received from IBM for the purchase cost of equipment to be located offsite and used to recover Agency systems in the event a disaster makes the Robert E David building unusable for computer operations.

Agency procedures for the storage of Agency data at an offsite location have been reviewed to verify that the Agency can restore IT systems when a recovery center would be located.

*2010-3: IT Disaster Recovery Plan*

**Condition:**

The Agency has not adopted a disaster recovery plan for the IT department.

**Management's Response:**

Z/os mainframe full backups are run Saturday night at 8:30 pm using IBM Software

These backups are copied to tape and are taken offsite to Iron Mountain Recovery. Backups have been tested for the operating system level to the individual file level in both a testing task and actual recovery from a failing server. Note all open systems will be virtualized utilizing VM/Ware by 9/2012.

Other Platform (PCs) backups are performed each night at 7:00 PM to the backup SAN located in a separate building.

Beginning in August of 2011, discussions have been held with the State CIO's and Clemson University concerning options for disaster recovery of the DEW hardware and network. Price quotes for a both DASD and Tape storage with the point in time copy feature needed to replicate data to the offsite recovery location have been obtained. A budget required to implement Disaster Recovery is being developed.

*2010-4: Access to Program and Data (Physical Security and Logical Security)*

**Condition:**

The computer room located on the second floor of the Agency'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.

**Management's Response:**

DoIT's Office of Information security (OIS) has had communications with Human Resources to assure proper steps are taken for off boarding of employees with regard to account access. The audit trail now exists in an electronic KBox database. Furthermore, proper account purges have been automated to assure this lapse does not reoccur. These steps have already been completed. An official approval of written policy documentation is being added to our security manual.

The current IT Security System does not meet the requirements of the IRS and SSA. SCDEW has applied for and received a US Department of Labor (DOL) grant to upgrade this system and is in the process of doing so. We have been working with the State Information Technology Management Office (ITMO) on releasing a procurement to upgrade the system and anticipate it to be released this month. We should have the new System installed by the end of December of 2012.

The current system does not provide all the information necessary to do a recertification as defined by the IRS. Once the new system is installed, this process will be formalized and done. It is our intent to review 1/12 of all people each month of the year.

The access is currently controlled by badges. When someone with a badge is granted access, they are always monitored while in the computer room. When the new security System is completed, DoIT will be reviewing computer room access and it is anticipated that the number of people allowed access to the computer room will substantially decrease.

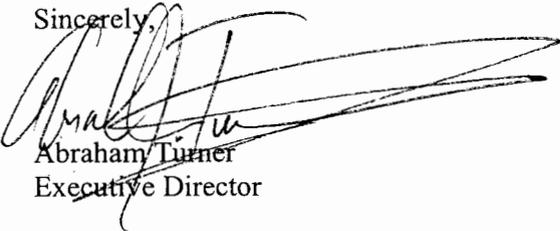
As stated in the cause section, DoIT will audit and reduce the number of personnel who can badge into the computer room. In the new system, each time someone does so, the event will be recorded by person, entry time, door and who is authorized to enter the computer room as well as have their picture recorded by the new cameras. As before, anyone who does not have a badge but needs to be in the computer room (maintenance personnel for example) is watched until they exit the computer room.

Each time a person is hired by the agency or terminated, DoIT receives a report from SCDEW's HR Department. In addition, the list of personnel working for SCDEW is controlled by DoIT by using the Email address as the controlling point for new additions to the agency. Also, DoIT revokes Email for anyone not using their email address for 90 days in case a terminated person's information is not recorded.

SCDEW's DoIT division is implementing the New IT Security System as outlined in the columns to the left. The procurement has been completed and is expected to be released in March of 2012. The plan is to have it implemented by December 31, 2012.

If there are any questions, or if additional information is needed, please contact Don Grant, CPA, Director of Finance, at (803) 737-0367.

Sincerely,

A handwritten signature in black ink, appearing to read 'Abraham Turner', is written over a horizontal line. The signature is stylized and somewhat cursive.

Abraham Turner  
Executive Director