



STATE OF WISCONSIN
Legislative Audit Bureau
NONPARTISAN • INDEPENDENT • ACCURATE

Report 21-9
May 2021

Unemployment Reserve Fund

FY 2018-19 and FY 2019-20

Department of Workforce Development



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FY 2018-19 and FY 2019-20
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May 27, 2021

Senator Robert Cowles and
Representative Samantha Kerkman, Co-chairpersons
Joint Legislative Audit Committee
State Capitol
Madison, Wisconsin 53702

Dear Senator Cowles and Representative Kerkman:

To help fulfill our audit responsibilities under s. 13.94, Wis. Stats., and at the request of the Department of Workforce Development (DWD), we have audited the financial statements of the State of Wisconsin Unemployment Reserve Fund, which accounts for Wisconsin's Unemployment Insurance program benefits paid to eligible individuals. This audit report contains our unmodified opinion on the Fund's financial statements and related notes as of and for the years ended June 30, 2020, and June 30, 2019.

In response to the public health emergency, additional federal funds were made available through the Unemployment Insurance program, including those provided under the federal Coronavirus Aid, Relief, and Economic Security (CARES) Act. The CARES Act programs provided almost \$2.4 billion in benefits paid to eligible individuals during fiscal year (FY) 2019-20. The net position of the Fund was \$1.7 billion as of June 30, 2020, which was a decrease of \$345.4 million, or 17.1 percent, from the net position as of June 30, 2019.

The Schedule of Cash Balance Related to Taxable Employers is used to determine the state unemployment tax rate paid by employers. Section 108.18 (3m), Wis. Stats., requires a certain tax rate schedule to be in effect for the calendar year based upon the Fund's cash balance as of June 30 of the preceding year. Because the cash balance continued to be above \$1.2 billion as of June 30, 2020, the lowest tax rate schedule continues to be in effect for calendar year 2021.

We identified a material weakness in internal control over financial reporting related to the reporting of benefits payable. We recommend DWD revise its procedures for calculating the benefits payable at the end of the fiscal year to ensure the effects of changes in circumstances, such as the backlog of claims that occurred in FY 2019-20, are accurately reflected in the payable. We also recommend that DWD report to the Joint Legislative Audit Committee on the status of its efforts to continue to process and pay benefits under new or continuing federal programs, to determine the relief that will be provided to employers for regular unemployment benefits provided during the public health emergency, and to complete the reviews DWD identified to assess if payments were incorrectly provided and establish an overpayment amount, as appropriate.

We appreciate the courtesy and cooperation extended to us by DWD staff during the audit. A response from DWD follows our report.

Respectfully submitted,

Joe Chrisman
State Auditor

JC/LK/ss

Introduction

The Unemployment Insurance program provides benefits to eligible individuals who become unemployed through no fault of their own.

Wisconsin's Unemployment Insurance program was enacted in 1932 and was the first such program in the United States. The program, which is authorized in ch. 108, Wis. Stats., is accounted for in the State of Wisconsin Unemployment Reserve Fund and is managed by the Department of Workforce Development (DWD). The program provides benefits temporarily to replace a portion of lost wages for eligible individuals who become unemployed through no fault of their own. Administrative costs of the program are funded primarily by federal grants, and these costs are accounted for in the State's General Fund. However, \$18.9 million in federal funding that was received in fiscal year (FY) 2019-20 under the Families First Coronavirus Response Act for administrative costs is being accounted for in the Unemployment Reserve Fund.

The Unemployment Insurance Advisory Council (UIAC) advises DWD on matters related to unemployment insurance and makes recommendations for unemployment insurance changes to the Legislature. Section 15.227 (3), Wis. Stats., provides that the UIAC consists of five employer and five employee representatives who serve six-year terms and are appointed by the Secretary of DWD. The Secretary also appoints a DWD employee to serve as the nonvoting chairperson.

In March 2020, in response to the public health emergency, the federal Coronavirus Aid, Relief, and Economic Security (CARES) Act established additional federal programs to fund benefits to unemployed individuals and to provide funding for certain regular unemployment benefits. Further, Wisconsin enacted statutory changes, including 2019 Wisconsin Act 185, and emergency administrative rule changes to increase flexibility and to accommodate federal law changes. The effect of these additional federal programs on the financial statements of the

Unemployment Reserve Fund are discussed further in the sections that follow.

Employer Taxes

Each employer has an account within the Unemployment Reserve Fund. The federal government, the State of Wisconsin, electing local governmental units, and electing nonprofit organizations reimburse the Unemployment Reserve Fund for benefits charged to their accounts, rather than contribute in advance of benefit payments and are referred to as reimbursable employers. All other employers are considered taxable employers that are subject to a basic tax and a solvency tax that together constitute their total state unemployment insurance tax.

Certain regular unemployment benefit payments related to the public health emergency will not affect an employer's account and may be charged to the solvency account or may be federally reimbursed.

The basic tax is credited to a taxable employer's account and is based on each employer's unemployment experience rating. For example, taxable employers with more employee layoffs pay more in basic taxes than those with fewer layoffs. The solvency tax is credited to the Unemployment Reserve Fund's balancing, or solvency account, and is based on each employer's unemployment experience rating, payroll size, and account balance. The solvency account, which is reported as part of the Unemployment Reserve Fund's net position, is used to pay benefits that by state law cannot be charged to an employer's account, such as unemployment benefit expenditures for unemployed workers of an employer that went out of business. Under the provisions of 2019 Wisconsin Act 185 and 2021 Wisconsin Act 4, certain regular unemployment benefits that occurred during the public health emergency will also be charged to the solvency account. Both the use of the solvency account and the expected federal reimbursement will provide relief to taxable employers as these benefit payments would not directly affect the amounts used to determine future contribution rates.

The lowest unemployment insurance tax rate schedule has been in effect since calendar year 2018.

Wisconsin Statutes designate that one of four unemployment insurance tax rate schedules, as shown in Table 1, is in effect for a calendar year based on the cash balance of the Unemployment Reserve Fund as of June 30 of the preceding year. The lowest tax rate schedule, Schedule D, has been in effect since calendar year 2018.

Table 1

Unemployment Insurance Tax Rate Schedules

Schedule ¹	Cash Balance ²	Calendar Year in Effect
Schedule A	Less than \$300.0 million	2015
Schedule B	At least \$300.0 million but less than \$900.0 million	2016
Schedule C	At least \$900.0 million but less than \$1.2 billion	2017
Schedule D	At least \$1.2 billion	2018, 2019, 2020, and 2021

¹ In order from highest tax rate to lowest.

² Cash balance of the Unemployment Reserve Fund as of June 30 of the preceding year.

Based on the tax rate schedule, unemployment insurance tax rates are applied to each employee's wages up to the taxable wage base established in Wisconsin Statutes. Wisconsin's taxable wage base has been \$14,000 since 2013.

Unemployment Insurance Benefits

The average weekly regular unemployment benefit payment was \$295 in 2020.

Unemployed individuals file their initial benefit claim applications and subsequent weekly benefit claims online. DWD verifies the information provided in order to establish the eligibility of individuals and the amount of weekly benefits to pay them. Regular unemployment benefits are funded primarily by employer-paid taxes that are deposited in the Unemployment Reserve Fund. Eligible individuals may receive 26 weeks of regular unemployment benefits. Since January 2009, the minimum weekly regular unemployment benefit payment has been \$54; and since January 2014, the maximum payment has been \$370. Benefit recipients received an average weekly regular unemployment benefit payment of \$325 in 2019 and \$295 in 2020.

Benefits provided under the new federal programs during FY 2019-20 totaled almost \$2.4 billion.

In addition to regular unemployment benefits, in March 2020 the CARES Act created several federally funded unemployment benefit programs. Benefits provided under the following programs during FY 2019-20, totaled almost \$2.4 billion:

- the Pandemic Emergency Unemployment Compensation program, which provided temporary funding of benefits for an additional 13 weeks of eligibility;
- the Pandemic Unemployment Assistance program, which provided 39 weeks of benefits to individuals ineligible for regular unemployment benefits, had a minimum payment amount of \$163 and maximum payment amount of \$370; and

- the Federal Pandemic Unemployment Compensation program, which provided an additional \$600 to the weekly benefit payment for individuals eligible for either regular or pandemic-related unemployment benefits.

In March 2020, DWD waived work-search requirements for individuals receiving unemployment benefits.

Prior to March 2020, eligible individuals were generally required to be available to work and certify that they were searching for work or were granted a waiver. Work-search requirements included at least four reasonable search actions for suitable work during a week of unemployment. A reasonable work-search action is defined by administrative rule, and may include submitting a job application to a suitable employer, registering with a placement agency, or participating in employment workshops. To meet federal requirements related to easing eligibility requirements and access to unemployment benefits, an emergency rule was promulgated that modified the requirements related to the availability for work and provided a waiver to the work-search requirements for the period of the public health emergency. This rule expired in May 2021.

The net receivable from overpayments to claimants as of June 30, 2020, was \$32.0 million, or 8.0 percent less than the June 30, 2019 balance.

Individuals are sometimes paid more unemployment benefits than they are entitled to receive. This can occur if the individual or employer intentionally or unintentionally provides incorrect information used to calculate weekly benefit amounts or if DWD makes an error in determining the amount of benefits paid. It may also occur through no fault if, for example, an individual was paid benefits based on accurate information but was later awarded back pay from his or her employer, thereby reducing the amount of benefits that should have been paid. When an overpayment is identified, a receivable is established for the amount of the overpayment. The net receivable reported by the Unemployment Reserve Fund as a result of overpayments to claimants declined from \$34.8 million as of June 30, 2019, to \$32.0 million as of June 30, 2020, or by 8.0 percent.

In addition to the new federal unemployment programs, the CARES Act also provided federal reimbursement for certain regular unemployment benefits provided during the public health emergency. For instance, the CARES Act provided federal reimbursement for regular unemployment benefits for states that did not require individuals to wait one week to receive benefits. 2019 Wisconsin Act 185 temporarily suspended the one-week waiting period, which allows federal funding to be received for the first week of benefits for weeks beginning April 19, 2020. Federal reimbursement is also expected for a portion of regular unemployment benefits provided by reimbursable employers and benefits provided under the work-share, or short-term compensation program, which is a program intended to provide prorated unemployment benefits for employees of employers who voluntarily make an agreement with the state to reduce work hours instead of laying off workers. Although the final amount of federal reimbursement has not yet been determined DWD included in the financial statements a receivable of \$140.0 million from the federal government related to these programs for FY 2019-20.

Financial Position

The U.S. Department of Labor recommends that states have sufficient reserves to sustain 12 months of benefit payments.

Programs established for unemployment benefits are intended to accumulate resources during periods of low unemployment to ensure funds are sufficient to pay benefits during periods of high unemployment. The U.S. Department of Labor (DOL) recommends that states have sufficient reserves to sustain 12 months of unemployment benefit payments estimated using specified criteria, without relying upon contribution revenue. For Wisconsin, DOL reported that the reserve balance of approximately \$1.9 billion as of January 1, 2020, was just below this recommended reserve level.

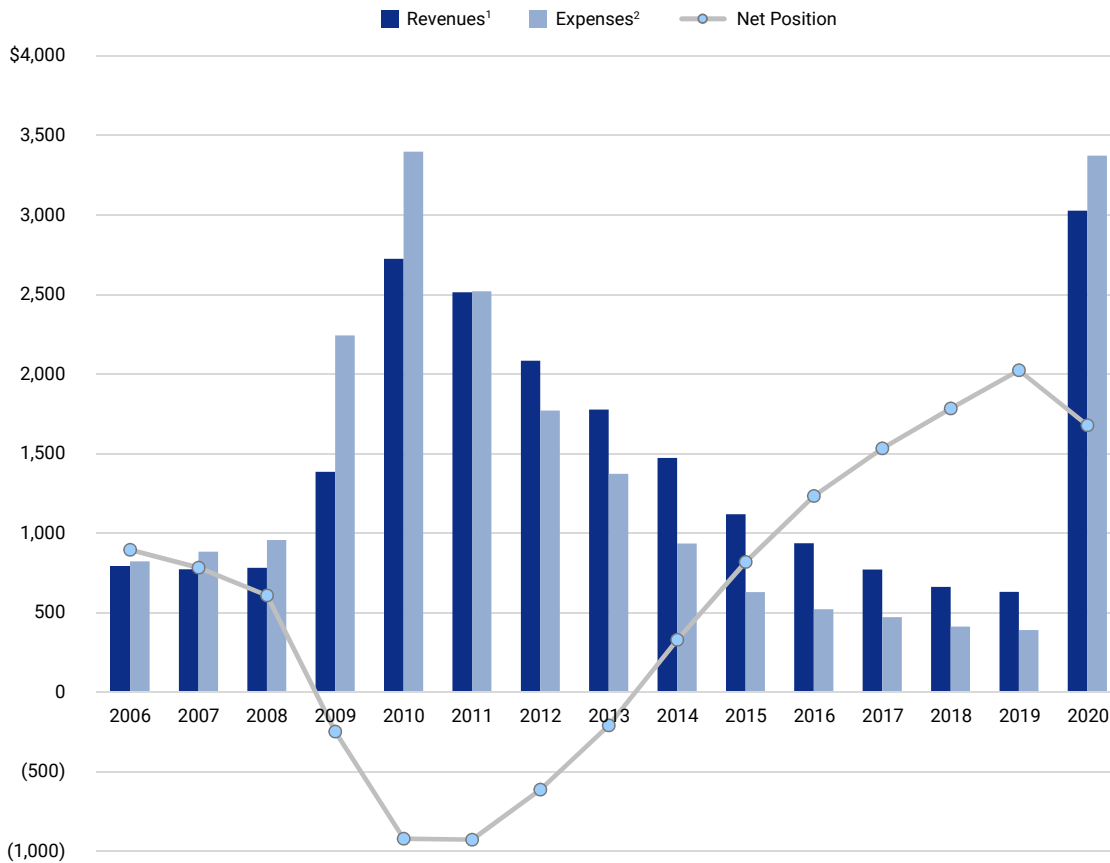
The net position of the Unemployment Reserve Fund, as reported in accordance with generally accepted accounting principles, represents the value of the plan's assets that are available to meet unemployment benefit obligations as they become due. In years when the resources provided through employer taxes and other revenue exceeds unemployment benefit payments and transfers, the net position will increase. When unemployment benefit payments and transfers exceed the resources provided, the net position will decrease. As shown in Figure 1, in FY 2018-19 employer taxes and other revenue totaled \$629.7 million, while unemployment benefit payments and transfers totaled \$390.3 million. Therefore, the net position as of June 30, 2019, increased to \$2.0 billion.

The net position of the Unemployment Reserve Fund declined to \$1.7 billion as of June 30, 2020.

Subsequently, the net position of the Unemployment Reserve Fund decreased because unemployment benefit payments and transfers totaled \$3.4 billion, which exceeded the \$3.0 billion in employer taxes and other revenues that included almost \$2.4 billion in federal reimbursement for benefits provided under the CARES Act programs. From June 30, 2019, to June 30, 2020, the Unemployment Reserve Fund's net position decreased by \$345.4 million, or by 17.1 percent. The decline in net position was not more significant because federal reimbursement was received to provide for both federal and certain regular unemployment benefit payments.

Figure 1

Unemployment Reserve Fund Revenues, Expenses, and Net Position
 For Fiscal Year Ended June 30
 (in millions)



¹ Revenues include employer contributions, Federal Unemployment Tax Act (FUTA) credit reduction, investment earnings, and federal funds received for certain benefits.

² Expenses include benefits paid to unemployed individuals and transfers to other funds.

Audit Results

We provided an unmodified opinion on the financial statements of the Unemployment Reserve Fund as of and for the years ended June 30, 2020, and June 30, 2019.

We performed an audit of the Unemployment Reserve Fund financial statements, which are prepared by DWD using generally accepted accounting principles prescribed by the Governmental Accounting Standards Board. To complete our audit of the financial statements, we reviewed DWD’s internal controls over financial reporting, tested financial transactions, and reviewed the financial statements, notes, and supplementary information that were prepared by DWD management. We provided an unmodified opinion on the financial statements and related notes as of and for the years ended June 30, 2020,

and June 30, 2019. Our opinion begins on page 15 and the related financial statements begin on page 30.

We report a material weakness in internal control over financial reporting.

Our Independent Auditor's Report on Internal Control over Financial Reporting and on Compliance and Other Matters begins on page 47. As discussed in this report, our consideration of internal control was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. However, as discussed, we identified an internal control deficiency that we consider to be a material weakness, which is a deficiency that creates a reasonable possibility that a material misstatement will not be prevented, or will not be detected and corrected, on a timely basis. We found DWD did not properly consider the significant backlog of claims that resulted from the public health emergency when assessing the potential unemployment benefits that were payable as of June 30, 2020. DWD prepared adjustments to correct the errors we identified. We recommend DWD revise its procedures for calculating the benefits payable at the end of the fiscal year to ensure the effects of changes in circumstances, such as the backlog of claims that occurred in FY 2019-20, are accurately reflected in the payable. Because the Unemployment Reserve Fund's financial statements are also included in the State of Wisconsin's Comprehensive Annual Financial Report for the fiscal year ended June 30, 2020, this material weakness was also included in the Independent Auditor's Report on Internal Control over Financial Reporting and on Compliance and Other Matters related to our audit of the State of Wisconsin's financial statements (report 20-30) as Finding 2020-004.

Other Audits of Unemployment Insurance

Under the provisions of 2019 Wisconsin Act 185, we performed three evaluations of DWD's administration of the Unemployment Insurance program and recommended improvements to DWD. In report 20-5, we evaluated reported overpayments of certain unemployment insurance benefits that occurred in April 2020; in report 20-13, we completed a review of DWD's management of unemployment insurance call centers; and in report 20-28, we evaluated the processing and resolution of certain Unemployment Insurance benefit claims. DWD has provided follow-up reports to the Joint Legislative Audit Committee on the status of its efforts to implement the recommendations included in these reports.

Our single audit report identified concerns with IT security controls for systems that are used to administer the Unemployment Insurance program.

As part of our audit of federal funds expended by the State of Wisconsin, we audited the Unemployment Insurance program and identified a significant deficiency related to information technology (IT) security controls over systems that are used to administer the Unemployment Insurance program. Failure to properly maintain IT controls could result in the issuance of erroneous or fraudulent payments, ineligible program participants, or inappropriate viewing of confidential data. We recommend that DWD improve its IT controls

(report 21-6), and we will follow up on the status of DWD's efforts to address our recommendations as a part of our FY 2020-21 single audit.

Ongoing Issues

As the public health emergency continued into FY 2020-21, the high volume of unemployment insurance claims has put additional pressures on the Unemployment Reserve Fund. As of January 1, 2021, DOL reported that Wisconsin's reserve balance of approximately \$1.1 billion was one half of the recommended reserve level. Further, the Unemployment Insurance program continues to be affected by matters that continued after the end of FY 2019-20 or that arose after the end of the fiscal year. These include the need to continue to process and pay benefits under new or continuing federal unemployment benefit programs, the determination of relief that will be provided to employers for regular unemployment benefits provided during the public health emergency, and the need to complete reviews DWD identified to assess if payments were incorrectly provided and establish an overpayment amount, as appropriate.

DWD has reported that it continues to process and pay benefits under new and continuing federal programs.

Federal benefits provided under the unemployment benefit programs established through the CARES Act continued in FY 2020-21 and an additional benefit program was established through the Lost Wage Assistance program, which provided funding for additional benefits for a six-week period in August and September 2020. Federal benefit payments for the CARES Act programs were further extended by the federal Continued Assistance Act, on December 27, 2020, and the American Rescue Plan Act, on March 11, 2021. As a result, the benefit period was extended to a possible 79 weeks with supplemental weekly benefits of \$300 available for most weeks. In addition, the Mixed Earners Unemployment Compensation program was created to provide an additional \$100 in weekly benefits to self-employed individuals receiving regular unemployment benefits. Federal pandemic unemployment benefits are currently set to expire on September 4, 2021. We will review the benefits provided under these federal programs as part of our FY 2020-21 financial audit of the State of Wisconsin.

DWD has not yet determined the extent of federal reimbursement for regular unemployment benefits or the amounts that will be charged to the solvency account or the interest and penalty account.

As noted, the CARES Act also established programs intended to provide relief to employers through federal reimbursement of certain regular unemployment benefits, including the first week of benefit payments as well as amounts to provide relief to reimbursable employer and for work-share benefits. In addition, 2019 Wisconsin Act 185 and 2021 Wisconsin Act 4 provided additional employer relief through the use of the solvency account for regular unemployment benefits provided to employees of taxable employers and for the use of funds in the interest and penalty account, which is maintained in the State's General Fund, for regular unemployment benefits provided to employees of reimbursable employers. DWD has reported that it must perform a manual process to review regular unemployment benefit payments made during the public health emergency to determine whether these

payments relate to the public health emergency, could be reimbursed by the federal government, could be charged to the solvency account, or could be charged to the interest and penalty account. Until DWD completes its determination, the relief that will be provided to employers through the receipt of federal reimbursement and the use of the solvency account or the interest and penalty account cannot be known.

Fraud and overpayments related to the unemployment insurance program have been identified as a concern by DOL's Office of the Inspector General (OIG). In an alert memorandum, dated February 22, 2021, the OIG reported that potential fraud existed and that DOL needed to take action to ensure states had appropriate controls to mitigate fraud in high-risk areas. DWD is statutorily required to report annually to the UIAC on its activities related to detecting and prosecuting program fraud in the previous calendar year. DWD's 2020 report, which was submitted on March 15, 2021, indicated a total of \$4.5 million in overpayments as a result of fraud, a decrease of 4.0 percent from 2019. As benefit payments increase, it would generally be expected that overpayments, which may or may not be the result of fraud, would also increase. DWD uses multiple methods, such as by comparing or cross-matching information provided by individuals with employment, immigration, and incarceration records, to detect and prevent programmatic overpayments including those that may be indicative of fraud. Although we were informed by DWD staff that these methods continued to be used, the increase in claim activity created an increase in the number of cross-matches that were identified for further reviews. It will be important for DWD to complete the reviews it has identified through these methods to assess if payments were incorrectly provided, either by error or fraud, and to establish an overpayment amount, as appropriate.

☑ Recommendation

We recommend the Department of Workforce Development report to the Joint Legislative Audit Committee, by September 16, 2021, on the status of its efforts to:

- *continue to process and pay benefits under the federal programs included in the Continued Assistance Act and the American Rescue Plan Act;*
- *determine the relief that will be provided to employers for regular unemployment benefits during the public health emergency, including amounts that will be reimbursed by the federal government, amounts that will be charged to the solvency account, and amounts that will be charged to the interest and penalty account; and*
- *complete the reviews DWD identified to assess if payments were incorrectly provided and establish an overpayment amount, as appropriate.*

Audit Opinion



STATE OF WISCONSIN
Legislative Audit Bureau

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State Auditor

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Independent Auditor's Report on the Financial Statements and Other Reporting Required by *Government Auditing Standards*

Senator Robert Cowles and
Representative Samantha Kerkman, Co-chairpersons
Joint Legislative Audit Committee

Amy Pechacek, Secretary
Department of Workforce Development

Report on the Financial Statements

We have audited the accompanying financial statements and the related notes of the State of Wisconsin Unemployment Reserve Fund as of and for the years ended June 30, 2020, and June 30, 2019, as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management of the Unemployment Reserve Fund is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America. This includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, which is 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 from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of the accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion on these financial statements.

Opinion

In our opinion, the financial statements referred to in the first paragraph present fairly, in all material respects, the financial position of the Unemployment Reserve Fund as of June 30, 2020, and June 30, 2019, and the respective changes in its financial position and its cash flows thereof for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Emphases of Matters

As discussed in Note 1 to the financial statements, the financial statements referred to in the first paragraph present only the Unemployment Reserve Fund and do not purport to, and do not, present fairly the financial position of the State of Wisconsin as of June 30, 2020, and June 30, 2019, the changes in its financial position, or where applicable, its cash flows for the years then ended, in accordance with accounting principles generally accepted in the United States of America.

As discussed in Note 5 to the financial statements, the presentation of the Unemployment Reserve Fund net position in the Statement of Net Position was updated to report net position as restricted for benefit payments.

As discussed in Note 6 to the financial statements, an estimate was not developed for payments related to the remaining backlog of weekly unemployment claims that related to FY 2019-20, as of November 30, 2020, and therefore, a liability for these claims has not been reported.

Our opinion is not modified with respect to these matters.

Other Matters

Required Supplementary Information—Accounting principles generally accepted in the United States of America require that the Management Discussion and Analysis on pages 19 through 27 be presented to supplement the financial statements. Such information, although not a part of the financial statements, is required by the Governmental Accounting Standards Board, which considers it to be essential for placing the financial statements in an appropriate operational, economic, or historical context. In accordance with auditing standards generally accepted in the United States of America, we applied certain limited procedures to the required supplementary information that included inquiries of management about the methods of preparing the information. We further compared the information for consistency with management's responses to our inquiries, the financial statements, and other knowledge we obtained during our audits of the 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.

Accompanying Information—Our audits were conducted for the purpose of forming an opinion on the financial statements of the Unemployment Reserve Fund. The Schedule of Cash Balance Related to Taxable Employers on page 41 and the related note on pages 43 through 44 are presented for purposes of additional analysis and are not a required part of the financial statements. This cash balance is used to determine the unemployment tax rate schedule to be used during the following calendar year. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audits of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in

the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued a report dated May 25, 2021, that begins on page 47 on our consideration of the Unemployment Reserve Fund's internal control over financial reporting; our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements; and other matters. The purpose of that report is solely 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 effectiveness of the Unemployment Reserve Fund's 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 used when considering the Unemployment Reserve Fund's internal control over financial reporting and compliance.

LEGISLATIVE AUDIT BUREAU



Joe Chrisman
State Auditor

May 25, 2021

Management's Discussion and Analysis

Prepared by Management of the Unemployment Reserve Fund

Management's Discussion and Analysis provides users of the State of Wisconsin Unemployment Reserve Fund's financial statements with an overview of the statements and an analysis of the Fund's financial performance during the fiscal years ended June 30, 2020, and June 30, 2019. The financial statements, notes, and this discussion are the responsibility of management of the Fund.

Financial Summary (Highlights)

The assets of the Unemployment Reserve Fund exceeded liabilities at the close of fiscal year (FY) 2019-20 by approximately \$1.7 billion. Except for \$20.4 million in certain federal allocations, the Fund's net position, if positive, can be used only to pay unemployment benefits to eligible unemployed persons.

The Fund's net position decreased by \$106.0 million during the two-year period from July 1, 2018, through June 30, 2020. Unemployment taxes paid by employers decreased each fiscal year compared to the previous year. Benefits paid to unemployed workers decreased between FY 2017-18 and FY 2018-19, but substantially increased between FY 2018-19 and FY 2019-20.

Overview of the Fund

The Wisconsin Unemployment Reserve Fund was established under ch. 108, Wis. Stats., to account for unemployment tax contributions received from employers and benefits paid to unemployed workers. The Fund is administered by the State of Wisconsin Department of Workforce Development (DWD). The Unemployment Insurance Advisory Council, consisting of labor and management representatives,

advises DWD on the administration of unemployment insurance law and submits its recommended changes in the law to the Legislature during every biennial legislative session.

Generally, the principal source of revenue for the Fund is quarterly unemployment tax contributions paid by the approximately 144,000 employers subject to the taxing provisions of ch. 108, Wis. Stats. During FY 2019-20, the Fund also received a significant amount of federal funding to pay for pandemic unemployment benefits. Federal law requires the Fund to hold all reserves in the Federal Unemployment Trust Fund, which invests in obligations guaranteed by the United States, and earnings on the Trust Fund may be used only to pay benefits. With the exception of certain federal allocations, the Fund's reserves may be used only to pay unemployment benefits or to refund tax and benefit overpayments to employers or, in the event benefits were federally funded, to the federal government. Federal special administrative allocations, which are special distributions to each state, may only be used for administration of the program and are not available for the payment of unemployment benefits.

If the Fund exhausts all of its reserves, it may borrow from the Federal Unemployment Trust Fund to continue paying benefits. Except for some short-term cash flow situations, and the period from March 18, 2020, through September 6, 2021, federal borrowing normally carries interest charges. The interest charges may not be funded from the Unemployment Reserve Fund.

Administrative costs of the Unemployment Insurance program are accounted for in the State of Wisconsin's General Fund and are not reported within the Unemployment Reserve Fund's financial statements. In addition, interest on outstanding advances from the federal government is accounted for in the State of Wisconsin's Unemployment Interest Payment Fund and general purpose revenue appropriations and is not reported within these financial statements.

Financial Statements

These financial statements are intended to show the Fund's financial position as of June 30, 2020, and June 30, 2019, and results of operations and cash flows for FY 2019-20 and FY 2018-19. The Statement of Net Position reports the Fund's assets and liabilities. The Statement of Revenues, Expenses, and Changes in Fund Net Position reports all the Fund's revenues, expenses, and transfers regardless of when cash is received or paid. This statement also shows the Fund's net position and how it has changed. The Statement of Cash Flows provides information about the Fund's cash receipts and cash payments during the fiscal years and provides a reconciliation of operating income to net cash provided by operating activities.

Assets

The Fund's assets consist of cash and cash equivalents and receivables. Table A shows that total assets increased by \$240.7 million between June 30, 2018, and June 30, 2019, and by \$517.1 million between June 30, 2019, and June 30, 2020.

Table A

Assets
(in millions)

	June 30, 2018	June 30, 2019	Change	June 30, 2020	Change
Cash and Cash Equivalents	\$ 1,625.9	\$1,878.8	\$252.9	\$1,585.9	\$(292.9)
Employer Receivables	153.7	146.3	(7.4)	127.2	(19.1)
Overpayments to Claimants	40.4	34.8	(5.6)	32.0	(2.8)
Other Receivables	0.3	1.1	0.8	833.0	831.9
Total Assets	\$1,820.3	\$2,061.0	\$240.7	\$2,578.1	\$517.1

Cash received from employer contributions continued to exceed cash payments for benefits during FY 2017-18 and FY 2018-19. The unemployment rate, averaging 3.1 percent, remained low during this period. However, with the onset of the COVID-19 pandemic during FY 2019-20, cash payments for benefits significantly exceeded cash received from employer contributions. The unemployment rate reached a high of 14.9 percent in April 2020. In addition, the receivable from the federal government for federally funded benefits increased from \$0.05 million as of June 30, 2018, to \$805.4 million as of June 30, 2020.

Liabilities

Table B shows the Fund's liabilities increased by \$1.3 million between June 30, 2018, and June 30, 2019, and by \$862.5 million between June 30, 2019, and June 30, 2020.

Table B

Liabilities
(in millions)

	June 30, 2018	June 30, 2019	Change	June 30, 2020	Change
Benefit Overpayments					
Due Others	\$16.7	\$13.9	\$(2.8)	\$ 13.6	\$ (0.3)
Benefits Payable	7.1	5.6	(1.5)	761.6	756.0
Due to State of Wisconsin	2.1	2.0	(0.1)	69.0	67.0
Overdrafts	0.0	2.1	2.1	20.1	18.0
Other Liabilities	10.5	14.1	3.6	35.9	21.8
Total Liabilities	\$36.4	\$37.7	\$1.3	\$900.2	\$862.5

The Fund accrues a liability for benefits that relate to claims of unemployment for weeks on or before June 30 but have not yet been paid as of June 30. During FY 2019-20, DWD experienced a backlog of unemployment claims that contributed to the \$756.0 million increase of the Benefits Payable liability from \$5.6 million as of June 30, 2019, to \$761.6 million as of June 30, 2020.

Claimants may choose to have federal and/or state income taxes withheld from their unemployment payments. The Fund remits tax withholdings to the Internal Revenue Service and the Wisconsin Department of Revenue. While federal tax withholding is required to be transferred several times a week, state tax withholding is only required to be transferred every three months and, therefore, results in a payable due to the State of Wisconsin. The Fund held \$68.3 million in state tax withholding as of June 30, 2020, an increase of \$66.6 million from the \$1.7 million held as of June 30, 2019. This is attributed to the increase in benefit payments made and, therefore, the increase in tax withholding, during FY 2019-20 due to the onset of the COVID-19 pandemic.

Net Position

Table C shows the Fund's net position increased by \$239.4 million between June 30, 2018, and June 30, 2019, and decreased by \$345.4 million between June 30, 2019, and June 30, 2020.

Table C

Net Position
(in millions)

	June 30, 2018	June 30, 2019	Change	June 30, 2020	Change
Restricted for Benefit Payments	\$1,781.9	\$2,021.4	\$239.5	\$1,657.5	\$(363.9)
Restricted for Administration	2.0	1.9	(0.1)	20.4	18.5
Total Net Position	\$1,783.9	\$2,023.3	\$239.4	\$1,677.9	\$(345.4)

The primary factors affecting the Fund's net position are the tax rate and the unemployment rate. See below under Operating Revenue and Operating Expense for an analysis of these factors.

Operating Revenue

The two major sources of operating revenue for the Fund are employer tax contributions, including those collected through the Federal Unemployment Tax Act (FUTA) tax credit reduction, and reimbursements for benefits paid on behalf of the federal government, other governmental units, and nonprofit organizations. A smaller amount of revenue is received from penalties and other sources. Table D shows that the Fund's operating revenues decreased by \$40.2 million during FY 2018-19 and increased by \$2,372.9 million during FY 2019-20.

Table D

Operating Revenue
(in millions)

	FY 2017-18	FY 2018-19	Change	FY 2019-20	Change
Employer Contributions ¹	\$597.1	\$561.5	\$(35.6)	\$ 514.3	\$ (47.2)
Benefit Reimbursements	30.4	26.1	(4.3)	2,446.3	2,420.2
Penalties and Other Revenues	1.4	1.1	(0.3)	1.0	(0.1)
Total Operating Revenues	\$628.9	\$588.7	\$(40.2)	\$2,961.6	\$2,372.9

¹ Amount includes employer contributions and Federal Unemployment Tax Act (FUTA) credit reduction.

Employer contributions decreased by \$82.8 million, or 13.9 percent, between FY 2017-18 and FY 2019-20 because the average tax rate decreased during this period. The average tax rate decreased from 1.75 percent in calendar year 2018 to 1.62 percent in 2019 and to an estimated 1.50 percent in 2020. An employer's tax rate can change from year to year depending on its unemployment experience. In addition, the rate schedule in use during any calendar year can change depending on the overall cash balance in the fund on June 30 of the previous year. The rate schedule in effect for 2018 was the lowest schedule available because the June 30, 2017 balance was greater than the \$1.2 billion threshold specified in Wisconsin Statutes. The lowest rate schedule continued in 2019 and in 2020.

Benefit reimbursements increased by \$2,420.2 million during FY 2019-20 due to six new federal unemployment programs enacted during the fiscal year, including:

- The Pandemic Unemployment Assistance (PUA) program provides 39 weeks of unemployment benefits to individuals who had either exhausted all access to regular unemployment or who were otherwise ineligible, such as the self-employed, "gig workers," or those with limited recent work history.
- The Pandemic Emergency Unemployment Compensation (PEUC) program provides an additional 13 weeks of benefits to individuals who exhaust their regular unemployment entitlement.
- The Federal Pandemic Unemployment Compensation (FPUC) program provides \$600 per week in supplemental benefits to eligible recipients of other unemployment benefits during certain benefit weeks.
- The Emergency Unemployment Relief for State and Local Governmental Entities, Certain Nonprofit Organization, and Federally Recognized Indian Tribes program reimburses these employers fifty percent of the benefits paid on their behalf.
- The Short-Time Compensation (STC) program provides temporary one hundred percent federal financing of STC payments.
- The Temporary Full Federal Funding of the First Week of Compensable Regular Unemployment for States with No Waiting Week program provides one hundred percent federal financing of one week of benefits that otherwise would be a waiting week.

Nonoperating Revenues

Table E shows the Fund's nonoperating revenues increased by \$7.8 million during FY 2018-19, and by \$24.2 million during FY 2019-20.

Table E

Nonoperating Revenues
(in millions)

	FY 2017-18	FY 2018-19	Change	FY 2019-20	Change
Investment Earnings	\$33.2	\$41.0	\$7.8	\$46.3	\$ 5.3
Special Federal Aids	0.0	0.0	0.0	18.9	18.9
Total Nonoperating Revenue	\$33.2	\$41.0	\$7.8	\$65.2	\$24.2

The Federal Unemployment Trust Fund made two special distributions to all states during FY 2019-20 pursuant to the March 2020 Emergency Unemployment Insurance Stabilization and Access Act (EUISSA). A state's eligibility to receive the first distribution was conditioned on its policies for notifying employees of the availability of unemployment benefits and for notifying claimants when an application is received, as well as the mediums the state makes available to claimants to obtain help with the application. The second distribution was conditioned on the state's initial claims for unemployment increasing by ten percent over the same rolling quarter in the previous calendar year and on the state expressing its commitment to strengthen access and ease eligibility requirements for unemployment. The Fund met the conditions for both distributions and received \$18.9 million during FY 2019-20. Amounts provided pursuant to the EUISSA may only be used for administration of the unemployment program and are not available to be used for the payment of unemployment itself.

Expenses and Transfers

Table F shows the Fund's operating expenses decreased by \$21.5 million during FY 2018-19 and increased by \$2,981.6 million during FY 2019-20.

Table F

Expenses and Transfers Out
(in millions)

	FY 2017-18	FY 2018-19	Change	FY 2019-20	Change
Benefits Paid on Behalf of:					
Taxable Employers	\$382.1	\$365.1	\$(17.0)	\$ 926.6	\$ 561.5
Federal Government	0.7	0.1	(0.6)	2,398.0	2,397.9
Other Entities	28.9	25.0	(3.9)	47.2	22.2
Total Operating Expenses	\$411.7	\$390.2	\$(21.5)	\$3,371.8	\$2,981.6
Transfer to Pay Administrative Expenses in General Fund and Other Nonoperating Expenses	\$0.0	\$0.1	\$0.1	\$0.4	\$0.3

Benefits paid on behalf of taxable employers increased by \$561.5 million between FY 2018-19 and FY 2019-20, because the average unemployment rate increased from 3.1 percent in FY 2018-19 to 5.3 in FY 2019-20. Benefits paid on behalf of the federal government increased by \$2,397.9 million between FY 2018-19 and FY 2019-20 due to the six new federal unemployment programs enacted during the fiscal year and discussed under Operating Revenue.

Currently Known Facts, Decisions, and Conditions

The Continued Assistance Act, signed on December 27, 2020, and the American Rescue Plan, signed on March 11, 2021, extended the federal pandemic unemployment programs that began under the Coronavirus Aid, Relief, and Economic Security Act, signed on March 27, 2020. The benefit period was extended to a possible 79 weeks with supplementary benefits available for most weeks. Federal pandemic unemployment programs are currently set to expire on September 4, 2021.

With the rapid creation of several new significant benefits, Unemployment Insurance programs in every state, including Wisconsin, became targets for large scale identity theft activity. The total amount of fraudulent benefits issued by the Fund as a result of these activities will not be known until all suspected cases have been manually investigated. These efforts are currently ongoing. Losses attributable to federally funded programs would have no effect on the net position of the Fund.

Contacting the Unemployment Reserve Fund's Management

This financial report is designed to provide an overview of the financial results of the Fund's activities and to show the Fund's financial position. If you have questions on this report or need additional information, contact:

Wisconsin Unemployment Reserve Fund
Department of Workforce Development
Division of Unemployment Insurance
201 East Washington Avenue
Madison, Wisconsin 53703

General information relating to the Fund can be found on DWD's website,
<https://dwd.wisconsin.gov/ui/>.

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Financial Statements

Statement of Net Position
June 30, 2020, and June 30, 2019

	June 30, 2020	June 30, 2019
ASSETS		
Current Assets:		
Cash and Cash Equivalents (Note 3):		
Federal Unemployment Trust Fund	\$ 1,565,137,052	\$ 1,875,857,194
Cash in Bank	0	1,027,965
Current Cash and Cash Equivalents	<u>1,565,137,052</u>	<u>1,876,885,159</u>
Employer Accounts Receivable:		
Taxable Employers (Net of Allowances of \$16,915,337 and \$16,451,492, respectively)	112,695,181	136,132,352
Governmental Units and Nonprofit Organizations (Net of Allowances of \$0 and \$100,000, respectively)	370,154	1,817,396
Combined Wage Claim Receivables	7,078,334	1,006,648
Net Current Employer Accounts Receivable	<u>120,143,669</u>	<u>138,956,396</u>
Other Receivables:		
Overpayments to Claimants (Net of Allowances of \$30,058,609 and \$32,713,315, respectively)	9,575,575	10,794,220
Concealment Penalty due from Claimants (Net of Allowances of \$347,750 and \$355,001, respectively)	223,363	299,541
Federally Funded Unemployment Benefit Programs	805,356,321	24,260
Due from State of Wisconsin (Note 4)	26,885,704	236,079
Net Current Other Receivables	<u>842,040,963</u>	<u>11,354,100</u>
Total Current Assets	<u>2,527,321,684</u>	<u>2,027,195,655</u>
Noncurrent Assets:		
Restricted Cash for Administration	20,806,685	1,891,913
Taxable Employer Accounts Receivable	7,008,015	7,320,117
Overpayments to Claimants	22,442,058	24,004,633
Concealment penalty due from claimants	546,236	574,703
Total Noncurrent Assets	<u>50,802,994</u>	<u>33,791,366</u>
TOTAL ASSETS	<u>\$ 2,578,124,678</u>	<u>\$ 2,060,987,021</u>
LIABILITIES AND NET POSITION		
Current Liabilities:		
Benefits Payable	761,561,281	5,566,724
Overdrafts	20,079,230	2,103,180
Employer Overpayments	9,737,630	10,036,252
Benefit Overpayments Due Employers, Other States, and Federal Government	4,913,647	4,732,074
Combined Wage Claim Plan Liabilities	5,958,152	3,617,519
Due to Federal Government	170,035	225,282
Due to Government Units and Nonprofit Organizations	13,363,287	0
Due to State of Wisconsin (Note 4)	68,982,031	1,987,847
Other	6,732,219	227,105
Total Current Liabilities	<u>891,497,512</u>	<u>28,495,983</u>
Noncurrent Liabilities:		
Benefit Overpayments Due Employers, Other States, and Federal Government	8,713,297	9,225,490
Total Liabilities	<u>900,210,809</u>	<u>37,721,473</u>
Net Position (Note 1 and Note 5):		
Restricted for Benefit Payments	1,657,487,031	2,021,373,635
Restricted for Administration	20,426,838	1,891,913
Total Net Position	<u>1,677,913,869</u>	<u>2,023,265,548</u>
TOTAL LIABILITIES AND NET POSITION	<u>\$ 2,578,124,678</u>	<u>\$ 2,060,987,021</u>

The accompanying notes are an integral part of this statement.

Statement of Revenues, Expenses, and Changes in Fund Net Position for the Years Ended June 30, 2020, and June 30, 2019

	For the Year Ended June 30, 2020	For the Year Ended June 30, 2019
OPERATING REVENUES		
Employer Contributions	\$ 514,293,574	\$ 561,456,717
Federal Unemployment Tax Act Credit Reduction	7,575	37,015
Benefits reimbursed by:		
Federal Government for Benefit Programs	2,397,885,095	1,592,321
Federal Government for Former Employees	2,735,510	1,768,064
State of Wisconsin, Electing Local Governments, and Electing Nonprofit Organizations	36,514,716	18,993,997
Other States	9,167,065	3,696,370
Penalties and Other Revenues	978,483	1,125,835
Total Operating Revenues	2,961,582,018	588,670,319
OPERATING EXPENSES		
Benefits Paid or Provided on Behalf of:		
Taxable Employers	926,597,511	365,064,661
Federal Government for Benefit Programs	2,395,215,563	(1,616,501)
Federal Government for Former Employees	2,735,510	1,768,064
State of Wisconsin, Electing Local Governments, and Electing Nonprofit Organizations	36,418,125	19,001,771
Other States	9,167,066	3,696,370
Adjustment for Allowance—Claimants	(1,043,114)	(919,334)
Other	2,669,532	3,208,822
Total Operating Expenses	3,371,760,193	390,203,853
OPERATING INCOME (LOSS)	(410,178,175)	198,466,466
NONOPERATING REVENUES		
Special Federal Aids	18,914,772	0
Investment Earnings	46,291,571	41,004,261
Total Nonoperating Revenues	65,206,343	41,004,261
INCOME (LOSS) BEFORE TRANSFERS	(344,971,832)	239,470,727
TRANSFERS		
Transfer to State of Wisconsin General Fund	(379,847)	(114,152)
CHANGE IN NET POSITION	(345,351,679)	239,356,575
Net position at the Beginning of the Year	2,023,265,548	1,783,908,973
Net position at the End of the Year (Note 1)	\$ 1,677,913,869	\$ 2,023,265,548

Statement of Cash Flows for the Years Ended June 30, 2020, and June 30, 2019

	For the Year Ended June 30, 2020	For the Year Ended June 30, 2019
CASH FLOWS FROM OPERATING ACTIVITIES		
Cash Received from:		
Employer Contributions	\$ 537,766,412	\$ 571,646,972
Federal Unemployment Tax Act Credit Reduction	7,575	37,015
Benefit Reimbursements	1,649,040,554	26,150,562
Benefit Overpayment Recoveries	18,041,132	18,142,460
Other Operating Revenues	1,304,052	1,427,825
Cash Payments for:		
Benefits	(2,579,454,041)	(404,262,721)
Other Operating Expenses	(2,721,412)	(3,271,633)
Net Cash Provided (Used) by Operating Activities	(376,015,728)	209,870,480
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES		
Cash Overdraft implicitly Financed	17,976,050	2,103,180
Special Federal Aid	18,914,772	0
Transfers to State of Wisconsin General Fund	0	(123,023)
Net Cash Provided by Noncapital Financing Activities	36,890,822	1,980,157
CASH FLOWS FROM INVESTING ACTIVITIES		
Investment Earnings	46,291,571	41,004,261
Net Cash Provided by Investing Activities	46,291,571	41,004,261
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(292,833,335)	252,854,898
Cash and Cash Equivalents at the Beginning of the Year	1,878,777,072	1,625,922,174
Cash and Cash Equivalents at the End of the Year	<u>\$ 1,585,943,737</u>	<u>\$ 1,878,777,072</u>
RECONCILIATION OF OPERATING INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES		
Operating Income (Loss)	\$ (410,178,175)	\$ 198,466,466
Adjustments to Reconcile Operating Income to Net Cash Provided by Operating Activities:		
Provision for Uncollectible Accounts	(2,298,112)	(6,158,442)
Changes to Assets and Liabilities:		
Decrease in Employer Accounts Receivables	18,760,983	10,857,398
Decrease (Increase) in Other Receivables	(826,433,863)	7,450,822
Increase (Decrease) in Liabilities	844,133,439	(745,764)
Total Adjustments	34,162,447	11,404,014
Net Cash and Cash Equivalents Provided (Used) by Operating Activities	\$ (376,015,728)	\$ 209,870,480

Notes to the Financial Statements

1. DESCRIPTION OF THE UNEMPLOYMENT RESERVE FUND

The Unemployment Insurance program is authorized in ch. 108, Wis. Stats., which includes the creation of the State of Wisconsin Unemployment Reserve Fund to account for contributions received from employers and benefits paid to unemployed workers. The Fund is administered by the State of Wisconsin Department of Workforce Development (DWD).

The Unemployment Insurance program follows the requirements of the Federal Unemployment Tax Act (FUTA), as amended. Therefore, covered employers in Wisconsin are permitted to offset their FUTA tax by a portion of the amount contributed to the Wisconsin Unemployment Reserve Fund. The net FUTA taxes paid by employers to the federal government are used, in part, to reimburse DWD for its costs to administer the Fund. These administrative costs, along with federal reimbursements, are accounted for in the State of Wisconsin's General Fund and are not reported within the State of Wisconsin Unemployment Reserve Fund's financial statements.

The Unemployment Reserve Fund, which is part of the State of Wisconsin financial reporting entity and is reported as an enterprise fund in the State's basic financial statements, accounts for employer contributions and benefits paid to unemployed workers, as well as reimbursements of benefits paid or provided on behalf of the federal government, other governmental units, and nonprofit organizations. The Fund's net position includes the following restrictions:

A. Restricted for Benefit Payments

Except as noted below, the Fund's net position, if positive, can be used only to pay unemployment benefits to eligible unemployed persons.

B. Restricted for Administration

A portion of the Fund's net position has been restricted for administration of the unemployment insurance law and employment services.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**A. Fund Accounting and Basis of Presentation**

The financial statements of the Unemployment Reserve Fund have been prepared in conformance with generally accepted accounting principles for proprietary funds. The Fund applies all applicable Governmental Accounting Standards Board (GASB) statements. The Fund is accounted for using the economic resources measurement focus. With this measurement focus, all assets and liabilities are included on the Statement of Net Position. The Fund is reported on the full accrual basis of accounting. This basis of accounting recognizes revenues and overpayment recoveries when they are measurable and due, regardless of when cash is received. Expenses are recognized in the period incurred, regardless of when cash is paid. The Statement of Revenues, Expenses, and Changes in Fund Net Position classifies revenues and expenses as either operating or nonoperating.

Transactions categorized as operating revenues and expenses are those relating to the Fund's principal operation of paying benefits to unemployed workers. Operating expenses include items such as benefits paid. Operating revenues include employer contributions and federal funding for benefit payments. Certain revenues that are not related to the Fund's principal operation, such as investment earnings, are reported as nonoperating revenue.

B. Accounting Estimates

The preparation of financial statements requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. For example, allowances for doubtful collections are established for some receivables based on historical collection information. Actual results may differ from those estimates.

C. Amounts Receivable from Taxable Employers

Under the full accrual basis of accounting, employer contributions are recognized as revenues in the accounting period in which they become due and measurable. Contributions are reported based on employer self-declared payroll reports. However, some estimates are used to report contributions for employers who fail to file the required reports. In addition, historical collection information is used to estimate and establish an allowance for doubtful collections. Amounts expected to be collected, but not within twelve months, are reported as noncurrent assets on the Statement of Net Position.

D. Amounts Receivable from Governmental Units and Nonprofit Organizations

The federal government, the State of Wisconsin, electing local governmental units, and electing nonprofit organizations are referred to as “reimbursable employers” because they reimburse the Fund for benefits charged to their accounts, rather than contribute in advance of benefit payments. The Fund recognizes a receivable from these organizations when benefits are paid to their former employees. Historical collection information is used to estimate and establish an allowance for doubtful collections. All receivables, net of the allowance, are expected to be collected within twelve months. Amounts receivable from nonprofit organizations written off as uncollectible are recovered through a statutory assessment against active nonprofit employers who have elected reimbursement financing.

E. Amounts Receivable from Claimants

In some instances, benefits are paid to claimants who ultimately are proven to be ineligible to receive all or a portion of those benefits. The Fund recognizes a receivable from these claimants when the benefit overpayment is identified. A related liability is established for the portion of the overpayments that, when collected, will be credited to reimbursable employers or the federal government. Historical collection information is used to estimate and establish an allowance for doubtful collections. Amounts expected to be collected, but not within twelve months, are reported as noncurrent assets and noncurrent liabilities on the Statement of Net Position.

F. Amounts Receivable for Federally Funded Benefit Programs

The federal government provides funding for certain unemployment benefit programs that either supplement or extend regular state-funded benefits, including those that were authorized in March 2020 under the Coronavirus Aid, Relief, and Economic Security (CARES) Act. Some programs, such as Trade Readjustment Assistance, are ongoing while other programs, such as Pandemic Emergency Unemployment Compensation and Disaster Unemployment Assistance, are temporary. The Fund recognizes a receivable from the federal government when benefits are paid under these programs.

G. Benefits Payable to Claimants

Benefits payable to claimants reflect benefits payable through June 30. The liability is based upon known subsequent claim payments and other available information.

H. Deferred Outflows of Resources and Deferred Inflows of Resources

GASB Statement Number 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*, provides guidance for deferred outflows of resources and deferred inflows of resources as required elements of the financial statements. GASB standards identify certain circumstances under which deferred outflows of resources and deferred inflows of resources must be reported. The Fund

has no deferred outflows or inflows of financial resources to be reported on the Statement of Net Position.

3. DEPOSITS

Deposits include cash and cash equivalents on deposit in banks or other financial institutions. The majority of the Fund's cash and cash equivalents consist of deposits with the Federal Unemployment Trust Fund managed by the Secretary of the Treasury pursuant to Title IX of the Social Security Act. The Federal Unemployment Trust Fund includes deposits from the unemployment insurance funds of all states. The Federal Unemployment Trust Fund is required by federal law to invest only in obligations guaranteed by the United States. The State of Wisconsin Unemployment Reserve Fund is credited quarterly with earnings only to the extent the Fund's deposit with the Federal Unemployment Trust Fund exceeds the Fund's outstanding advances, if any, from the Federal Unemployment Trust Fund, as computed on a daily basis. The deposit with the Federal Unemployment Trust Fund is not categorized in accordance with the criteria under GASB Statement Number 40, *Deposit and Investment Risk Disclosures—an Amendment of GASB Statement No. 3*, because it is neither a deposit with a financial institution nor an investment.

The remainder of the Fund's cash and cash equivalents consists of deposits in a bank. If the carrying amount of the deposit is negative, the Fund reports an overdraft on the Statement of Net Position.

For deposits held in financial institutions, custodial credit risk is the risk that in the event of a failure of a depository financial institution, deposits may not be returned. Most of the deposits that are held in financial institutions are insured up to \$250,000 by the Federal Deposit Insurance Corporation (FDIC). The State of Wisconsin Public Deposit Guarantee Fund insures up to \$400,000 above the amount of federal insurance. The Fund's management monitors the debt ratings of its bank as published by Moody's, S&P, Fitch, and DBRS. The following amounts of the Fund's bank balances of \$775,340 as of June 30, 2019, and \$823,383 as of June 30, 2020, were exposed to custodial credit risk:

	<u>June 30, 2019</u>	<u>June 30, 2020</u>
Uninsured and Uncollateralized	\$125,340	\$173,383

4. AMOUNTS DUE TO/FROM STATE OF WISCONSIN

The amount reported as Due to State of Wisconsin consists primarily of state income taxes withheld from claimant benefit payments but not yet paid to the General Fund. It also consists of interest and penalty payments collected from employers and claimants but not yet paid to the General Fund.

The amount reported as Due from State of Wisconsin consists primarily of benefits paid on behalf of the State for its former employees that the State has

not yet reimbursed the Fund. Part of the amount reported as Due from State of Wisconsin resulted from the time lag between when benefits were paid out of the Unemployment Reserve Fund and when reimbursements were received. Also, under certain circumstances, benefits paid to former employees of governmental units and nonprofit organizations are reimbursed by interest and penalty funds accounted for in a program revenue appropriation in the State of Wisconsin General Fund.

5. ACCOUNTING CHANGES

The presentation of Net Position on the Statement of Net Position changed for the periods ending June 30, 2019, and June 30, 2020 when compared to prior reporting periods. This change was to correct the reporting of the net position of the Fund as restricted for the payment of benefits and remove the reporting of the solvency account, which is not a restriction, for the Statement of Net Position. There was no change to the beginning or ending net position of the Fund.

6. CONTINGENCIES

At the end of FY 2019-20, the Fund had a backlog related to weekly claims filed. The Fund accrued a liability for benefits paid through November 30, 2020, that were related to weeks prior to June 30, 2020. However, an estimate of payments related to the remaining backlog, totaling 52,694 weekly claims as of December 7, 2020, cannot be estimated and, therefore, a liability for these claims has not been reported.

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Supplementary Information

**Schedule of Cash Balance Related to Taxable Employers
June 30, 2020, and June 30, 2019**

	<u>June 30, 2020</u>	<u>June 30, 2019</u>
CASH BALANCE		
Cash and Cash Equivalents	\$ 1,565,137,052	\$ 1,876,885,159
Overdrafts	(20,079,230)	(2,103,180)
Net Cash Balance	1,545,057,822	1,874,781,979
INCREASES		
Employer Accounts Receivable:		
Government Units and Nonprofit Organizations	37,081,363	1,423,310
Combined Wage Claim Plan Receivables	5,738,772	947,747
Total Employer Accounts Receivable	42,820,135	2,371,057
Other Receivables:		
Federally Funded Unemployment Benefit Programs	17,206,539	4,737
Due from the State of Wisconsin	2,076,473	175,792
Total Other Receivables	19,283,012	180,529
Total Increases	62,103,147	2,551,586
DECREASES		
Employer Overpayments	12,478,000	12,929,582
Due to State of Wisconsin	68,602,184	1,987,847
Due to the Federal Government	170,035	225,282
Benefit Overpayments Due Other States	47,174	16,634
Other	5,109,858	213,525
Total Decreases	86,407,251	15,372,870
Cash Balance Related to Taxable Employers	<u>\$ 1,520,753,718</u>	<u>\$ 1,861,960,695</u>

The accompanying Note to the Schedule of Cash Balance Related to Taxable Employers is an integral part of this schedule.

Note to the Schedule of Cash Balance Related to Taxable Employers ■

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES FOR DETERMINING THE CASH BALANCE

The Schedule of Cash Balance Related to Taxable Employers as of June 30, 2019, and June 30, 2020, is presented for informational purposes. Section 108.18 (3m), Wis. Stats., provides for one of four tax rate schedules to be in effect during a particular calendar year, depending on the preceding June 30 cash balance in the Unemployment Reserve Fund. Tax rate Schedule D was in effect during 2018, 2019, and 2020 because the preceding June 30 balances were all more than the \$1.2 billion level specified in Wisconsin Statutes. Tax rate Schedule D is in effect again during 2021 because the June 30, 2020 balance was \$1,520,753,718.

A. Cash Balance

The cash and cash equivalent balance reported in the Unemployment Reserve Fund financial statements is reduced by overdrafts to arrive at a net cash balance. Restricted cash is not included because it is not available for the payment of benefits on behalf of taxable employers. The cash balance is then adjusted for balance sheet accounts that are unrelated to taxable employers to arrive at the cash balance related to taxable employers. Accruals that have no effect on the cash balance are removed from the balance sheet accounts.

B. Increases

The cash balance is increased for the cash payments to be reimbursed to the Fund by:

- local and federal governmental units and nonprofit organizations, gross of the allowance for uncollectible accounts, for benefits paid to their former employees;

44 › NOTE TO THE SCHEDULE OF CASH BALANCE

- other states for combined wage claims;
- the federal government for federally funded unemployment benefit programs; and
- the State of Wisconsin for benefits paid to its former employees.

C. Decreases

The net cash balance is reduced for the cash receipts from:

- employers for overpayments of tax contributions;
- claimants and employers for interest and penalty assessments, state withholding taxes, and federal loan interest assessments to be remitted to the State of Wisconsin;
- the federal government for federally funded unemployment benefit programs in excess of the benefits paid;
- claimants for benefit overpayments to be remitted to other states; and
- claimants for other items to be remitted elsewhere, such as federal withholding taxes.

■ ■ ■ ■

Auditor's Report



STATE OF WISCONSIN

Legislative Audit Bureau

Joe Chrisman
State Auditor

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Report 21-9

Independent Auditor's Report on Internal Control over Financial Reporting and on Compliance and Other Matters

Senator Robert Cowles and
Representative Samantha Kerkman, Co-chairpersons
Joint Legislative Audit Committee

Amy Pechacek, Secretary
Department of Workforce Development

We have audited the financial statements and the related notes of the State of Wisconsin Unemployment Reserve Fund as of and for the years ended June 30, 2020, and June 30, 2019, and have issued our report thereon dated May 25, 2021. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, which is issued by the Comptroller General of the United States.

Internal Control over Financial Reporting

Management of the Unemployment Reserve Fund is responsible for establishing and maintaining effective internal control over financial reporting (internal control). In planning and performing our audits of the financial statements, we considered the Unemployment Reserve Fund's internal control as a basis for designing audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Unemployment Reserve Fund's internal control. Accordingly, we do not express an opinion on the effectiveness of the Unemployment Reserve Fund's internal control.

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 misstatements, or to 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 Unemployment Reserve Fund's financial statements will not be prevented, or that a material misstatement will not be detected and corrected on a timely basis. 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.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies, and therefore, material weaknesses or significant deficiencies may exist that were not identified. However, we identified a deficiency in internal control that we consider to be a material weakness.

We consider the deficiency related to financial reporting for the Unemployment Reserve Fund financial statements included in the accompanying Finding and Response Schedule, to be a material weakness. Because the Unemployment Reserve Fund's financial statements are also included in the State of Wisconsin's Comprehensive Annual Financial Report for the fiscal year ended June 30, 2020, this material weakness was also included in the Independent Auditor's Report on Internal Control over Financial Reporting and on Compliance and Other Matters related to our audit of the State of Wisconsin's financial statements (report 20-30) as Finding 2020-004.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Unemployment Reserve Fund's financial statements are free from material misstatement, we performed tests of compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a material effect on the financial statements. 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*.

Response to Finding

The Department of Workforce Development's written response to the findings identified in our audit is included in the accompanying Finding and Response Schedule. The response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

Purpose of This Report

This report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be used when considering the Unemployment Reserve Fund's internal control and compliance. The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the result of that testing, and not to provide an opinion on the effectiveness of the Unemployment Reserve Fund's internal control or on compliance. Accordingly, this report is not suitable for any other purpose.

LEGISLATIVE AUDIT BUREAU



Joe Chrisman
State Auditor

May 25, 2021

FINDING AND RESPONSE SCHEDULE

Unemployment Insurance Benefits Payable

Background:

DWD administers the Unemployment Insurance program, which pays monetary benefits to certain individuals who have lost their jobs. Unemployed individuals file initial benefit claim applications and subsequent weekly benefit claims. DWD verifies the information provided in order to establish the statutory eligibility of individuals and the amount of weekly benefits to pay. DWD then processes the weekly benefit claim payments to eligible individuals. DWD is responsible for preparing financial statements for the program's activity that are reported as the Unemployment Reserve Fund.

In March 2020, the public health emergency resulted in a significant increase in unemployment claims being filed. In addition, DWD began making payments through several new federal programs that were aimed at providing monetary benefits to unemployed individuals. DWD experienced a significant backlog of claims that needed to be processed, including claims that had issues that needed resolution. As of September 1, 2020, DWD reported a backlog of over 685,000 weekly claims.

Criteria:

DWD is responsible for preparing financial statements in accordance with Governmental Accounting Standards Board (GASB) standards. The State of Wisconsin *Uniform GAAP Conversion Policies and Procedures Manual* (GAAP Manual), which is published by the Department of Administration, State Controller's Office (DOA-SCO), provides guidance to state agencies in preparing financial statements. To assess whether payments relate to the prior year and then to report those expenses and a related accounts payable in the financial statements, the GAAP Manual requires agencies to review payments that occurred within a reasonable period of time after the end of the fiscal year (after June 30), typically July and August. In addition, the GAAP Manual requires agencies to identify other payables that meet the criteria for reporting. In following these standards, DWD should calculate a payable representing benefits that will be paid to claimants after the end of the fiscal year, but relate to benefit weeks that occurred within the fiscal year.

Condition:

In preparing the financial statements for the Unemployment Reserve Fund for FY 2019-20, DWD identified benefit payments that had been processed in July and August 2020. DWD calculated that \$546.8 million of those benefit payments related to weekly claims for periods prior to June 30, 2020, and prepared an adjusting entry to report this benefit payable amount. However, DWD did not identify whether other payables existed as of June 30, 2020, related to its backlog of claims. On September 1, 2020, DWD reported that there was a backlog of 685,447 weekly claims, with 79,086 that related to the period March 15 through May 2, 2020. DWD did not identify these backlogged claims, nor other claims for weeks prior to June 30, 2020, when it calculated the payable that existed as of June 30, 2020.

At our request, DWD prepared the benefit payment report detailing benefit payments that occurred in September through November 2020. This report identified an additional \$214.8 million in benefit payments that related to weekly claims prior to June 30, 2020, but that DWD had not identified for inclusion in the payable for benefit payments.

Context:

We interviewed DWD staff to gain an understanding of the process used to develop the benefit payable as of June 30, 2020. We also reviewed the adjusting entry prepared by DWD for benefit claims paid after June 30, 2020, that related to weekly claims for weeks prior to June 30, 2020.

Effect:

The financial statements for the Unemployment Reserve Fund were materially misstated. Benefits Paid and Benefits Payable in the Unemployment Reserve Fund were understated by at least \$214.8 million. In addition, because federal revenue will be received for a significant portion of these claims, Other Receivables—Federally Funded Unemployment Benefit Programs and Benefits Reimbursed by Federal Government for Benefit Programs were each understated by at least \$185.1 million. After we brought these concerns to its attention, DWD adjusted the financial statements for these amounts.

Cause:

DWD followed its procedures from prior years and used payment information from July and August to calculate the amount of the payable to report for benefit payments for FY 2019-20. DWD staff stated that data was not readily available to allow them to calculate an additional payable amount for the backlog of claims that existed. However, DWD did not discuss additional payable amounts with DOA-SCO or the Legislative Audit Bureau, or suggest a note disclosure to disclose the potential for additional outstanding payables that could not easily be determined.

☑ Recommendation

We recommend the Wisconsin Department of Workforce Development revise its procedures for calculating benefit payables as of the end of the fiscal year to ensure the effect of changes in circumstances, such as the backlog of claims that occurred for FY 2019-20 claims, is reflected in the payable.

Response from the Wisconsin Department of Workforce Development: The Department of Workforce Development agrees with the finding and recommendation and will revise its procedures for calculating benefit payables as of the end of the fiscal year. The financial statements are prepared to balance timeliness and accuracy. At the time the financial statements were prepared, there was no way for staff to calculate the \$214.8 million in additional benefits. While DWD identified there was a backlog of claims for weeks prior to June 30, staff determined there was not enough information available to allow them to calculate an additional payable that was both timely and accurate.

■ ■ ■ ■

Response

**Department of Workforce Development
Secretary's Office**
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Tony Evers, Governor
Amy Pechacek, Secretary-designee

May 25, 2021

Joe Chrisman, State Auditor
Legislative Audit Bureau
22 E Mifflin St Suite 500
Madison WI 53703

Dear Mr. Chrisman,

Thank you for the opportunity to comment on the Unemployment Reserve Fund financial audit for the fiscal years ended June 30, 2019 and June 30, 2020.

DWD is pleased to receive an unmodified opinion on the Unemployment Reserve Fund financial statements and wishes to thank LAB for their diligence and effort extended to the audit.

DWD appreciates and accepts the Audit Bureau's recommendations and will report back to the Joint Legislative Audit Committee by September 16, 2021, on the status of our continued efforts to pay unemployment under new and continued federal programs, calculate employer tax rates, and assess claimant overpayments when appropriate.

We appreciate the efforts of your staff in conducting the financial audit for the Unemployment Reserve Fund.

Sincerely,

A handwritten signature in black ink, appearing to read "Amy Pechacek".

Amy Pechacek
Secretary-designee