

**STATE OF ILLINOIS
DEPARTMENT OF EMPLOYMENT SECURITY**

**Individual Nonshared Governmental Funds
Nonshared Proprietary Fund
Financial Statements
For the Year Ended June 30, 2013**

Performed as Special Assistant Auditors
for the Auditor General, State of Illinois



E.C. ORTIZ & CO., LLP
CERTIFIED PUBLIC ACCOUNTANTS

**State of Illinois
 Department of Employment Security
 Financial Audit
 For the Year Ended June 30, 2013**

Table of Contents	Page
Agency Officials	1
<u>Individual Nonshared Governmental Funds:</u>	
Financial Statement Report Summary	2
Independent Auditors' Report	3
Individual Nonshared Governmental Funds Financial Statements:	
Balance Sheets	6
Statements of Revenues, Expenditures, and Changes in Fund Balances	7
Notes to Financial Statements	8
Independent Auditors' Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with <i>Government Auditing Standards</i>	20
Schedule of Finding	22
<u>Nonshared Proprietary Fund:</u>	
Financial Statement Report Summary	28
Independent Auditors' Report	29
Nonshared Proprietary Fund Financial Statements:	
Statement of Net Position	32
Statement of Revenues, Expenses, and Changes in Net Position	33
Statement of Cash Flows	34
Notes to Financial Statements	35
Independent Auditors' Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with <i>Government Auditing Standards</i>	47
Schedule of Finding	49
Prior Findings Not Repeated	55

**State of Illinois
Department of Employment Security
Agency Officials
June 30, 2013**

Director	Mr. Jay Rowell
Executive Deputy Director, Administration September 19, 2011 to present May 8, 2011 to September 18, 2011	Ms. Barbara Piwowarski Vacant
Executive Deputy Director, Service Delivery	Mr. Amit Singla
Deputy Director, Business Services May 7, 2012 to present	Mr. Gideon Blustein
Assistant Deputy Director, Business Services October 9, 2012 to present July 1, 2012 to October 8, 2012	Ms. Bethani Whiting Vacant
Chief Information Officer (formerly Deputy Director, Information Service) August 17, 2011 to present January 14, 2011 to August 16, 2011	Ms. Monica Carranza Vacant
Assistant Deputy Director, Service Delivery February 1, 2013 to present Previous to February 1, 2013	Mr. Julian Federle Vacant
Chief Financial Officer December 10, 2012 to present Acting, August 22, 2012 to December 9, 2012 Previous to August 22, 2012	Ms. Linda DeMore Mr. L. Briant Coombs Mr. Jon Gingrich
Chief Internal Auditor	Mr. Marcus A. Dodd
Chief Technology Officer	Mr. Thomas Revane
Equal Employment Opportunity Officer Acting, June 1, 2013 to present Previous to June 1, 2013	Ms. Caroline Alamillo Mr. Carlos Charneco Mr. Joseph P. Mueller
General Counsel	Mr. L. Briant Coombs
Manager, Accounting Services Division	Ms. Evelina Loescher, PhD
Manager, Economic Information and Analysis Division	Ms. Lois Cuevas
Manager, Revenue Division	
Manager, Field Operations February 16, 2013 to present February 1, 2013 to February 15, 2013 August 29, 2011 to January 31, 2013 July 1, 2011 to August 28, 2011	Ms. Christine Cornell Vacant Mr. Julian Federle Vacant
Manager, Unemployment Insurance Programs December 16, 2012 to present October 1, 2012 to December 15, 2012 Previous to October 1, 2012	Ms. Trina Taylor Vacant Mr. Frank DeMore

The Department's Administrative offices are located at:

33 South State Street
Chicago, IL 60603-2802

607 East Adams Street, 9th floor
Springfield, IL 62701-1606

**STATE OF ILLINOIS
DEPARTMENT OF EMPLOYMENT SECURITY**

**Individual Nonshared Governmental Funds
Financial Statements
For the Year Ended June 30, 2013**

Performed as Special Assistant Auditors
for the Auditor General, State of Illinois

**State of Illinois
Department of Employment Security
Financial Statements
For the Year Ended June 30, 2013**

FINANCIAL STATEMENT REPORT SUMMARY

The audits of the accompanying individual nonshared governmental funds financial statements of the State of Illinois, Department of Employment Security (Department) were performed by E. C. Ortiz & Co., LLP.

Based on their audits, the auditors expressed unmodified opinions on the Department's individual nonshared governmental funds financial statements.

SUMMARY OF FINDING

The auditors identified a matter involving the Department's internal control over financial reporting that they considered to be a material weakness. The material weakness is described in the accompanying Schedule of Finding on pages 22 - 27 of this report as item 2013-001 (*Inadequate Controls Over Financial Close and Reporting*).

EXIT CONFERENCE

The finding and recommendation appearing in this report were discussed with Department personnel at an exit conference conducted on January 24, 2014. Attending were:

Illinois Department of Employment Security

Jay Rowell, Director
Joseph Mueller, General Counsel (via video conference)
Barbara Piwowarski, Executive Deputy Director, Administration
Amit Singla, Executive Deputy Director, Service Delivery
Monica Carranza, Chief Information Officer
Linda DeMore, Chief Financial Officer
Marcus Dodd, Chief Internal Auditor
Brian Hooper, Legislative Liaison
Kathy Harlan, Audit Liaison

Office of the Auditor General

Thomas Kizziah, Manager

E. C. Ortiz & Co., LLP

Edilberto Ortiz, Partner
Leilani Rodrigo, Partner
Emily Causon, Manager
Marceliana Caragan, IT Manager

The response to the recommendation was provided by Kathy Harlan, Audit Liaison, in a letter dated January 30, 2014.



INDEPENDENT AUDITORS' REPORT

Honorable William G. Holland
Auditor General
State of Illinois

Report on the Financial Statements

As Special Assistant Auditors for the Auditor General, we have audited the accompanying financial statements of the Operating Fund and Special Programs Fund (Individual Nonshared Governmental Funds) of the State of Illinois, Department of Employment Security (Department), as of and for the year ended June 30, 2013, and the related notes to the financial statements, as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management 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.

Auditors' Responsibility

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 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 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 audit opinions.

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Individual Nonshared Governmental Funds of the Department, as of June 30, 2013, and the changes in financial position, thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As discussed in Note 2, the financial statements present only the Individual Nonshared Governmental Funds and do not purport to, and do not, present fairly the financial position of the State of Illinois or the Department, as of June 30, 2013, and the changes in its financial position, for the year then ended in accordance with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

Other Matter

Required Supplemental Information

Management has omitted management's discussion and analysis for the Individual Nonshared Governmental Funds that accounting principles generally accepted in the United States of America require to be presented to supplement the financial statements. Such missing information, although not a part of the financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the financial statements in an appropriate operational, economic, or historical context. Our opinion on the financial statements is not affected by this missing information.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated January 30, 2014 on our consideration of the Department's internal control over financial reporting of the Individual Nonshared Governmental Funds and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Department's internal control over financial reporting of the Individual Nonshared Governmental Funds and its compliance.

Restricted Use of This Auditors' Report

This report is intended solely for the information and use of the Auditor General, the General Assembly, the Legislative Audit Commission, the Governor, the Comptroller, Department

management, 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.

E. C. Gray & Co. LLC
Chicago, Illinois
January 30, 2014

State of Illinois
Department of Employment Security
Individual Nonshared Governmental Funds
Balance Sheets
June 30, 2013
(Amounts in \$000's)

	Operating Fund	Special Programs Fund
	<u> </u>	<u> </u>
Assets		
Cash and cash equivalents	\$ 13,376	\$ -
Intergovernmental receivables	22,079	254
Due from other State funds	3,369	-
Inventories	312	-
	<u> </u>	<u> </u>
Total assets	<u>\$ 39,136</u>	<u>\$ 254</u>
 Liabilities and fund balances		
Liabilities		
Accounts payable and accrued liabilities	\$ 8,362	\$ 254
Intergovernmental payables	375	-
Due to other State funds	40,961	-
Deferred revenues	3,176	-
	<u> </u>	<u> </u>
Total liabilities	<u>52,874</u>	<u>254</u>
Fund balances (deficit)		
Nonspendable - inventories	312	-
Restricted	15,691	-
Unassigned	(29,741)	-
	<u> </u>	<u> </u>
Total fund balances (deficit)	<u>(13,738)</u>	<u>-</u>
	<u> </u>	<u> </u>
Total liabilities and fund balances	<u>\$ 39,136</u>	<u>\$ 254</u>

See Notes to Financial Statements.

State of Illinois
Department of Employment Security
Individual Nonshared Governmental Funds
Statements of Revenues, Expenditures, and Changes in Fund Balances
For the Year Ended June 30, 2013
(Amounts in \$000's)

	Operating Fund	Special Programs Fund
Revenues		
Federal government	\$ 233,027	\$ 8,120
Other revenues	589	-
Licenses and fees	3	-
Interest and investment income	8	-
Total revenues	<u>233,627</u>	<u>8,120</u>
Expenditures		
Employment and economic development	241,362	8,120
Capital outlays	19	-
Total expenditures	<u>241,381</u>	<u>8,120</u>
Deficiency of revenues over expenditures	<u>(7,754)</u>	<u>-</u>
Other financing sources		
Transfers in	19,910	-
Net changes in fund balances	<u>12,156</u>	<u>-</u>
Fund balances (deficit), July 1, 2012	<u>(25,894)</u>	<u>-</u>
Fund balances (deficit), June 30, 2013	<u>\$ (13,738)</u>	<u>\$ -</u>

See Notes to Financial Statements.

State of Illinois
Department of Employment Security
Individual Nonshared Governmental Funds
Notes to Financial Statements
June 30, 2013
(Amounts in \$000's)

NOTE 1 - DESCRIPTION OF FUNDS

The State of Illinois, Department of Employment Security (Department) administers the nonshared governmental funds described below. A nonshared fund is a fund in which a single State agency is responsible for administering substantially all financial transactions of the fund. The nonshared funds administered by the Department are summarized below.

A. Operating Fund

The following have been combined for financial reporting purposes as the Operating Fund:

a) *Title III Social Security and Employment Services Fund*

The Department is organized to administer grant and program activities under various federal mandates, statutes and regulations. This fund accounts for all general disbursements for the everyday operation of the Department.

b) *Unemployment Compensation Special Administration Fund*

This fund accounts for collections of interest and penalties from employers and judgment interest from claimants. Funds are used as provided by law as necessary for the proper administration of the Unemployment Insurance Act or transferred to the Unemployment Compensation Trust Fund.

The Governmental Accounting Standard Board (GASB) has issued Statement No. 54, *Fund Balance Reporting and Governmental Type Definitions*. This Statement indicates that a fund that has a significant amount in revenue from transfers in should not be reported as its own special revenue fund. As the Unemployment Compensation Special Administration Fund does not have a "specific revenue source," it was not shown as an independent special revenue fund.

B. Special Programs Fund

This fund accounts for paying unemployment benefits under the Trade Readjustment Act (TRA) program, the Alternative Trade Adjustment Assistance (ATAA) program, and the Disaster Unemployment Assistance (DUA) program.

State of Illinois
Department of Employment Security
Individual Nonshared Governmental Funds
Notes to Financial Statements
June 30, 2013
(Amounts in \$000's)

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The financial statements of the individual nonshared governmental funds administered by the Department have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP), as prescribed by the GASB. To facilitate the understanding of the financial statements, significant accounting policies are summarized below.

A. Reporting Entity

As defined by GAAP, the financial reporting entity consists of the primary government, as well as its component units, which are legally separate organizations for which the elected officials of the primary government are financially accountable.

Financial accountability is defined as:

- a) Appointment of a voting majority of the component unit's board and either (a) the primary government's ability to impose its will, or (b) the possibility that the component unit will provide financial benefit to or impose a financial burden on the primary government; or
- b) Fiscal dependency on the primary government.

Based upon the required criteria, neither of the Individual Nonshared Governmental Funds have component units, nor is either one a component unit of any other entity. However, because the Individual Nonshared Governmental Funds are not legally separate from the State of Illinois, they are included in the financial statements of the State as governmental funds. The State of Illinois' Comprehensive Annual Financial Report (CAFR) may be obtained by writing to the State Comptroller's Office, Financial Reporting Department, 325 West Adams Street, Springfield, Illinois, 62704-1871.

The financial statements present only the Operating Fund and the Special Programs Fund administered by the Department and do not purport to, and do not, present fairly the financial position of the Department as of June 30, 2013, nor changes in its financial position for the year then ended in conformity with GAAP.

State of Illinois
Department of Employment Security
Individual Nonshared Governmental Funds
Notes to Financial Statements
June 30, 2013
(Amounts in \$000's)

B. Basis of Presentation

In government, the basic accounting and reporting entity is a fund. A fund is defined as an independent fiscal and accounting entity with a self-balancing set of accounts recording cash and/or other resources together with all related liabilities, obligations, reserves, and equities, which are segregated for the purpose of carrying on specific activities or attaining certain objectives in accordance with special regulations, restrictions, or limitations. A Balance Sheet and Statement of Revenues, Expenditures, and Changes in Fund Balances have been presented for each Individual Nonshared Governmental Fund administered by the Department.

Each of the Individual Nonshared Governmental Funds is a special revenue fund. Transactions related to resources obtained from specific revenue sources (other than for expendable trusts) that are legally restricted for specified purposes are accounted for in special revenue funds. Special revenue funds are not shared with other State agencies. The Department administers grant and program activities under various federal mandates, statutes and regulations. The major federally funded administrative activities conducted by the Department are accounted for in the Title III Social Security and Employment Service Fund presented as part of the Operating Fund.

The Unemployment Compensation Special Administration Fund, presented as part of the Operating Fund, accounts for collections of interest and penalties from employers and judgment interest from claimants. The funds are used as provided by law as necessary for the administration of the Unemployment Insurance Act. The Special Programs Fund accounts for paying unemployment benefits under various federal programs.

All special revenue funds are held in the State treasury, except for the Special Programs Fund, which is held locally. The funds are appropriated by the General Assembly, except for the unemployment benefits paid from the Special Programs Fund and certain expenditures of the Unemployment Compensation Special Administration Fund that are excluded from appropriation by the Illinois Unemployment Insurance Act.

C. Basis of Accounting

The Individual Nonshared Governmental Funds are reported using the current financial resources measurement focus and the modified accrual basis of accounting.

Revenues are recognized as soon as they are both measurable and available. Nonexchange transactions, in which the Department gives (or receives) value without directly receiving (or

State of Illinois
Department of Employment Security
Individual Nonshared Governmental Funds
Notes to Financial Statements
June 30, 2013
(Amounts in \$000's)

giving) equal value in exchange, include grants from the federal and other State governments.

Revenue from grants, entitlements, and similar items is recognized in the fiscal year in which all eligibility requirements imposed by the provider have been met and the resources are 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 State considers revenues to be available if they are collected within 60 days of the end of the current fiscal year.

Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, principal and interest on long-term debt obligations, claims and judgments, and compensated absences are recorded only when payment is due. General capital asset acquisitions are reported as expenditures. Proceeds of long-term debt obligations and acquisitions under capital leases are reported as other financing sources.

Significant revenue sources of the Individual Nonshared Governmental Funds that are susceptible to accrual include grants from the federal government. All other revenue sources including fees, interest, and investment income are considered to be measurable and available only when cash is received.

Grant revenues earned but not drawn or received by the Department within 60 days after June 30, 2013 are reported under liabilities as deferred revenues.

D. Cash and Cash Equivalents

Cash and cash equivalents consist principally of deposits held in the State Treasury. Cash and cash equivalents also include cash on hand, cash in banks for locally held funds, and pooled investments funds held by other governmental agencies with a maturity of three months or less.

E. Inventories

Inventories, consisting primarily of printed forms and supplies, are valued at the lower of cost or market value. Management of the Department estimates that market value approximates cost for these supplies, and, accordingly, has not recorded an impairment to inventory valuation at June 30, 2013. Inventories for each fund are recorded as expenditures when consumed rather than when purchased.

State of Illinois
Department of Employment Security
Individual Nonshared Governmental Funds
Notes to Financial Statements
June 30, 2013
(Amounts in \$000's)

F. Interfund Transactions

The Individual Governmental Nonshared Funds have the following types of interfund transactions with other funds of the State:

a) *Services provided and used*

Sales and purchases of goods and services between funds for a price approximating their external exchange value. Interfund services provided and used are reported as revenues in seller funds and expenditures or expenses in purchaser funds. Unpaid amounts are reported as interfund receivables and payables in the fund Balance Sheets or fund Statement of Net Position.

b) *Reimbursements*

Repayments from the funds responsible for particular expenditures or expenses to the fund that initially paid for them. Reimbursements are reported as expenditures in the reimbursing fund and as a reduction of expenditures in the reimbursed fund.

c) *Operating transfers*

Flows of assets (such as cash or goods) without equivalent flows of assets in return and without a requirement for repayment. Transfers are reported as other financing uses in the funds making the transfers and as other financing sources in the funds receiving transfers.

G. Compensated absences

A liability for unpaid, accumulated vacation and sick leave balances for the Department's employees is reported in the nonshared funds only if they have matured, for example, as a result of employee resignations and retirements. There was no liability for compensated absences recorded as of June 30, 2013.

H. Fund Balances

Fund balances are classified in the following categories:

State of Illinois
Department of Employment Security
Individual Nonshared Governmental Funds
Notes to Financial Statements
June 30, 2013
(Amounts in \$000's)

a) Nonspendable

Nonspendable fund balance consists of amounts that cannot be spent because they are either (a) not in spendable form or (b) legally required to be maintained intact. The Title III Social Security and Employment Services Fund comprises the Department's nonspendable fund balance as of June 30, 2013.

b) Restricted

Restricted fund balance consists of amounts that are restricted to specific purposes, that is, when constraints placed on the use of resources are either (a) externally imposed by creditors, grantors, contributors, or laws or regulations of other governments or (b) imposed by law through constitutional provisions or enabling legislation. The Unemployment Compensation Special Administration Fund comprises the Department's restricted fund balance as of June 30, 2013.

c) Committed

Committed fund balance consists of amounts constrained by limitation that the Department imposes upon itself through resolutions. The commitment amount will be binding unless removed or amended in the same manner. There are no committed fund balances as of June 30, 2013.

d) Assigned

Assigned fund balance consists of net amounts that are constrained by the Department's intent to be used for specific purposes, but are neither restricted nor committed. There are no assigned fund balances as of June 30, 2013.

e) Unassigned

Unassigned fund balance consists of amounts that are available and are not designated for specific purposes. The Title III Social Security and Employment Services Fund has a negative residual balance and comprises the Department's unassigned fund balance as of June 30, 2013.

When both restricted and unrestricted fund balances are available for use, generally it is the Department's policy to use restricted resources first, then unrestricted resources when they are needed. Unrestricted resources that are committed are generally used before assigned resources, and assigned resources are generally used before unassigned resources.

State of Illinois
Department of Employment Security
Individual Nonshared Governmental Funds
Notes to Financial Statements
June 30, 2013
(Amounts in \$000's)

I. Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenditures during the reporting period. Actual results could differ from those estimates.

NOTE 3 - DEPOSITS

The State Treasurer is the custodian of the State's cash and cash equivalents for funds maintained in the State Treasury. The Department independently manages cash and cash equivalents maintained outside the State Treasury.

As of June 30, 2013, deposits in the Operating Fund represent cash on hand amounting to \$4 and deposits in the custody of the State Treasurer (or in transit) amounting to \$13,372.

Deposits in the custody of the State Treasurer are pooled and invested with other State funds in accordance with the Deposit of State Moneys Act of Illinois Compiled Statutes (15 ILCS 520/11). Funds held by the State Treasurer have not been categorized as to credit risk because the Department does not own individual securities. Details on the nature of these investments are available within the State of Illinois' CAFR.

NOTE 4 - INTERGOVERNMENTAL RECEIVABLES AND PAYABLES

In the Operating Fund, intergovernmental receivables represent reimbursements due from the federal government and other local governments for administrative expenses incurred, totaling \$21,989 and \$90, respectively. In the Special Programs Fund, intergovernmental receivables represent reimbursements due from the federal government for unemployment benefits paid under the TRA, ATAA, and DUA programs, totaling \$254.

In the Operating Fund, intergovernmental payables represent federal payroll tax withholdings due to the federal government and recording fees due to local county governments, totaling \$336 and \$39, respectively.

State of Illinois
Department of Employment Security
Individual Nonshared Governmental Funds
Notes to Financial Statements
June 30, 2013
(Amounts in \$000's)

NOTE 5 - INTERFUND BALANCES AND ACTIVITIES

(a) Balances Due from/to Other Funds

The following balances at June 30, 2013 represent amounts due from other Department and State of Illinois funds.

Fund	Amount	Description/Purpose
Operating Fund	\$ 5	Due from the Unemployment Compensation Trust Fund representing discretionary transfers of non-sufficient funds (NSF) fees
	5	Due from Department of Public Aid for weekly statistical services and monthly intercept of unemployment insurance benefits
	100	Due from the Department of Commerce and Economic Opportunity for Workforce Investment Act grants
	3,231	Due from the Unemployment Compensation Trust Fund representing transfers of penalties and interest
	28	Due from the Department of Labor for staff reimbursement
	\$ 3,369	

State of Illinois
Department of Employment Security
Individual Nonshared Governmental Funds
Notes to Financial Statements
June 30, 2013
(Amounts in \$000's)

The following balances at June 30, 2013 represent amounts due to other Department and State of Illinois funds.

Fund	Amount	Description/Purpose
Operating Fund	\$ 39,216	Due to other State funds for payment of services
	1,745	Due to the Unemployment Compensation Trust Fund for reimbursement of unemployment benefits paid to former employees of the Department
	\$ 40,961	

(b) Transfers From Other Funds

Interfund transfers in for the year ended June 30, 2013, were as follows:

Fund	Amount	Description/Purpose
Operating Fund	\$ 13	Discretionary transfer of NSF fees from Unemployment Compensation Trust Fund
	19,897	Discretionary transfer of penalties and interest from Unemployment Compensation Trust Fund
	\$ 19,910	

NOTE 6 - PENSION PLAN

Substantially all of the Department's full-time employees who are not eligible for participation in another State-sponsored retirement plan participate in the State Employees' Retirement System (SERS), which is a pension trust fund in the State of Illinois reporting entity. The SERS is a single-employer defined benefit public employee retirement system in which State employees participate, except those covered by the State Universities, Teachers', General Assembly, and Judges' Retirement Systems. The financial position and results of operations of the SERS for fiscal year 2013 are included in the State of Illinois' CAFR for the year ended June 30, 2013. The SERS issues a separate CAFR that may be obtained by writing to the SERS, 2101 South Veterans Parkway, Springfield, Illinois, 62794-9255.

State of Illinois
Department of Employment Security
Individual Nonshared Governmental Funds
Notes to Financial Statements
June 30, 2013
(Amounts in \$000's)

A summary of SERS benefit provisions, changes in benefit provisions, employee eligibility requirements including eligibility for vesting, and the authority under which benefit provisions are established are included as an integral part of the SERS' CAFR. Also included is a discussion of employer and employee obligations to contribute, and the authority under which those obligations are established.

The Department pays employer retirement contributions in the individual nonshared governmental funds based upon an actuarially determined percentage of payroll expense. For fiscal year 2013, the employer contribution rate was 37.99%.

NOTE 7 - POST-EMPLOYMENT BENEFITS

The State provides health, dental, vision and life insurance benefits for retirees and their dependents in a program administered by the Department of Central Management Services (DCMS). Substantially all State employees become eligible for post-employment benefits if they eventually become annuitants of one of the State sponsored pension plans. Health, dental, and vision benefits include basic benefits for annuitants and dependents under the State's self-insurance plan and insurance contracts currently in force. Annuitants may be required to contribute towards health, dental, and vision benefits with the amount based on factors such as date of retirement, years of credited service with the State, whether the annuitant is covered by Medicare, and whether the annuitant has chosen a managed health care plan. Annuitants who retired prior to January 1, 1998, and who are vested in the SERS do not contribute towards health, dental, and vision benefits. For annuitants who retired on or after January 1, 1998, the annuitant's contribution amount is reduced five percent for each year of credited service with the State allowing those annuitants with twenty or more years of credited service to not have to contribute towards health, dental, and vision benefits. Annuitants also receive life insurance coverage equal to the annual salary of the last day of employment until age 60, at which time the benefit becomes \$5.

However, Public Act 97-0695, effective, July 1, 2012, alters the contributions to be paid by the State, annuitants, survivors, and retired employees under the State Employees Group Insurance Act. This Act requires the Director of DCMS to, on an annual basis, determine the amount that the State should contribute. The remainder of the cost of coverage shall be the responsibility of the annuitant, survivor, or retired employee. These costs will be assessed beginning July 1, 2013.

The total cost of the State's portion of health, dental, vision, and life insurance benefits of all members, including post-employment health, dental, vision, and life insurance benefits, is

State of Illinois
Department of Employment Security
Individual Nonshared Governmental Funds
Notes to Financial Statements
June 30, 2013
(Amounts in \$000's)

recognized as an expenditure by the State in the Illinois' CAFR. The State finances the costs on a pay-as-you-go basis. The total costs incurred for health, dental, vision, and life insurance benefits are not separated by department or component unit for annuitants and their dependents nor active employees and their dependents.

A summary of post-employment benefits provisions, changes in benefit provisions, employee eligibility requirements including eligibility for vesting, and the authority under which benefit provisions are established are included as an integral part of the financial statements of the DCMS. A copy of the financial statements of the DCMS may be obtained by writing to the Department of Central Management Services, 715 Stratton Building, 401 South Spring Street, Springfield, Illinois, 62606-4100.

NOTE 8 - RISK MANAGEMENT

The Department is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omission; workers' compensation and natural disasters. The State retains the risk of loss (i.e., is self-insured) for these risks. There has been no reduction in self-insurance coverage from coverage in the prior year. Settlement amounts have not exceeded coverage for the current or prior two fiscal years. The Department's risk management activities for workers' compensation are financed through appropriations to the DCMS and are accounted for in the General Fund of the State. The claims are not considered to be liabilities of the Department and accordingly, have not been reported in the Department's financial statements for the year ended June 30, 2013.

NOTE 9 - COMMITMENTS AND CONTINGENCIES

a) Federal funding

The Department receives federal grants, which are subject to review and audit by federal grantor agencies. Certain costs could be questioned as not being eligible expenditures under the terms of the grants. At June 30, 2013, there were no material questioned costs that have not been resolved with the federal awarding agencies. However, questioned costs could still be identified during audits to be conducted in the future. Management of the Department believes no material adjustments to the federal grants will be required and, accordingly, has not recorded any provision for repayment.

State of Illinois
Department of Employment Security
Individual Nonshared Governmental Funds
Notes to Financial Statements
June 30, 2013
(Amounts in \$000's)

b) Litigation

The Department is routinely involved in a number of legal proceedings and claims that cover a wide range of matters. In the opinion of management, the outcome of these matters is not expected to have any material adverse effect on the financial position or results of operations of the Department.

c) Due to Illinois Department of Central Management

Included in the Department's current liabilities classified as Due to Other State Funds are amounts owed to DCMS totaling \$37,072, primarily for services provided to the Department in the current and prior years. During the lapsed period, the Department paid DCMS \$10,572 of the outstanding amount, leaving a remaining balance of \$26,500.



E.C. ORTIZ & CO., LLP
CERTIFIED PUBLIC ACCOUNTANTS

**INDEPENDENT AUDITORS' 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***

Honorable William G. Holland
Auditor General
State of Illinois

As Special Assistant Auditors for the Auditor General, we have audited, in accordance with the 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, the financial statements of the Operating Fund and Special Programs Fund (Individual Nonshared Governmental Funds) of the State of Illinois, Department of Employment Security (Department), as of and for the year ended June 30, 2013, and the related notes to the financial statements, and have issued our report thereon dated January 30, 2014.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Department's internal control over financial reporting (internal control) of the Individual Nonshared Governmental Funds to determine the 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 Department's internal control. Accordingly, we do not express an opinion on the effectiveness of the Department's internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph 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, as described in the accompanying Schedule of Finding, we identified a certain deficiency in internal control that we consider to be a material weakness.

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 in the accompanying Schedule of Finding as item 2013-001 to be a material weakness.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Individual Nonshared Governmental Funds of the Department's financial statements are free from 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*.

Department's Response to Finding

The Department's response to the finding identified in our audit is described in the accompanying Schedule of Finding. The Department's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on the response.

Purpose of this Report

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

C. C. King & Co. LLP
Chicago, Illinois
January 30, 2014

**State of Illinois
Department of Employment Security
Schedule of Finding
For the Year Ended June 30, 2013**

Current Finding - *Government Auditing Standards*

2013-001 Inadequate Controls Over Financial Close and Reporting

The Department of Employment Security (Department) did not have adequate controls over financial close and reporting to allow management or employees in the normal course of performing their assigned functions to prevent or detect financial statement misstatements in a timely manner.

During our audit, we noted the following:

- a) The Department submitted “GAAP Reporting Packages” to the Illinois Office of the Comptroller (Comptroller) 1 to 21 days late. As part of the year-end accounting and financial reporting closing process, State Agencies are required to prepare and submit to the Comptroller “GAAP Reporting Packages” which summarize their yearly financial activities and the status of their funds at year-end. The “GAAP Reporting Packages” are used by the Comptroller to prepare the State’s Basic Financial Statements.
- b) Several errors and omissions during financial close and reporting process were identified for the following funds:

Title III Social Security and Employment Services Fund (Fund 52)

- The accrual for outstanding unpaid facilities, statistical, and telecommunication services provided by another governmental agency was understated by \$3.8 million. The Department’s yearend accrual (1) did not include invoices totaling \$4.5 million which have been reviewed and vouchered but not yet paid as of June 30, 2013; and (2) included invoices originally posted in September 2012 and duplicated in June 2013 totaling \$0.7 million.

Unemployment Compensation Special Administration Fund (Fund 55)

- Adjusting entries posted by the Comptroller at the request of the Department in relation to a fund transfer made in August of the following fiscal year which increased expenditures and accounts payable, resulting in an overstatement of \$2.9 million.

Master Bond Fund (Fund 1368)

- Assets and liabilities were not presented in a classified format to distinguish between current and long-term assets and liabilities. The noncurrent portion of

**State of Illinois
Department of Employment Security
Schedule of Finding
For the Year Ended June 30, 2013**

Current Finding - *Government Auditing Standards* (Continued)

2013-001 Inadequate Controls Over Financial Close and Reporting (Continued)

unamortized bond issue cost of \$3.0 million was presented as part of current assets. The noncurrent revenue bonds payable and unamortized bond premium of \$1,106.1 million and \$84.3 million, respectively, were presented as part of current liabilities.

- Financial statement disclosures did not include information related to (1) debt service requirements to maturity and (2) future minimum payments of the debt obligation.
- The “Due to Other Funds” amount in the Statement of Net Position did not agree with the amount presented in the Notes to Financial Statements. An adjusting entry to remove effects of interfund transactions totaling \$62.9 million was not included when summarizing the information presented in the Notes to Financial Statements. The Notes to Financial Statements was subsequently corrected by the Department to present correct amount of “Due to Other Funds.”

Unemployment Compensation Trust Fund (Fund 1138) and Master Bond Fund (Fund 1368)

- Eliminating entries for interfund transfers totaling \$323.9 million were not recorded.
- The Department did not present its draft financial statements in accordance with Government Accounting Standards Board Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*. Statement of Net Position and Statement of Revenues, Expenses, and Changes in Net Position were presented as Statement of Net Assets and Statement of Revenues, Expenses, and Changes in Net Assets.
- The Notes to Financial Statements included a disclosure on federal expenditures totaling \$1,019.3 million, identified under the American Recovery and Reinvestment Act of 2009 programs. The disclosure was not applicable for the current year’s financial statements.

The Department subsequently corrected the financial statements for the above adjustments and omissions.

**State of Illinois
Department of Employment Security
Schedule of Finding
For the Year Ended June 30, 2013**

Current Finding - *Government Auditing Standards* (Continued)

2013-001 Inadequate Controls Over Financial Close and Reporting (Continued)

We also noted the following:

Special Programs Fund (Fund 1136)

- Accounts payable and accrued liabilities was understated by \$0.05 million. The Department recorded benefit payments through July of the following fiscal year while the auditors identified FY 2013 benefit payments paid by the Department through mid-November.

Unemployment Compensation Trust Fund (Fund 1138)

- The allowance for uncollectible taxes, interest and penalties was erroneously calculated resulting in an overstatement of \$8.9 million to the allowance for uncollectible taxes, interest and penalties and understatement to contribution revenues.
- The “Receivables - Others” and its related allowance for uncollectible accounts were understated by \$2.0 million. The Department made a yearend adjustment to reconcile the general ledger and subsidiary ledger but failed to include this adjustment in the financial statements resulting in an understatement of these accounts.
- Benefit payments payable was understated \$5.3 million. The Department recorded benefit payments through July of the following fiscal year while the auditors identified FY 2013 benefit payments paid by the Department through mid-November.

These adjustments were not material to the financial statements and were not booked by the Department as of June 30, 2013.

The Statewide Accounting Management System (SAMS) Procedure 27.10.10 states that all State agencies (excluding those agencies whose GAAP reporting packages are completed by the Comptroller’s staff in consultation with agency personnel - referred to as “in-house”) are required to submit annual GAAP reporting packages for any fund or funds in which they expend from and/or deposit receipts. For fiscal year ended June 30, 2013, the GAAP reporting packages due dates for locally held funds was on August 9, 2013 and treasury-held fund on August 16, 2013, except for

**State of Illinois
Department of Employment Security
Schedule of Finding
For the Year Ended June 30, 2013**

Current Finding - *Government Auditing Standards* (Continued)

2013-001 Inadequate Controls Over Financial Close and Reporting (Continued)

governmental fund (Fund 52) and proprietary funds (Fund 1138 and Fund 1368) which was extended to September 9, 2013.

Generally accepted accounting principles (GAAP) require that expenditures for goods and services and related payables reported in the financial statements exist and represent valid transactions that occurred during the period. In addition, Procedure 03.50.10 of the SAMS Manual states that expenditures and related liabilities should be recognized in the accounting period in which the liability is incurred.

Paragraph 59 of GASB Statement No. 34, *Basic Financial Statements and Management's Discussion and Analysis—for State and Local Governments*, states that the eliminations should be made in the statement of activities to remove the doubling up effect of internal service fund activity.

Paragraph 97 of GASB Statement No. 34, *GASB Codification of Governmental Accounting and Financial Reporting Standards* Section 2200.172, also states that the Statement of Net Position should be presented in a classified format to distinguish between current and long-term assets and liabilities.

Paragraph 10 of GASB Statement No. 38, *Certain Financial Statement Note Disclosures*, states that government should disclose the following details of debt service requirements to maturity: (a) principal and interest requirements to maturity, presented separately, for each of the five subsequent fiscal years and in five-year increment thereafter. Interest requirements for variable-rate debt should be determined using the rate in effect at the financial statement date. (b) The terms by which interest rates change for variable debt.

Paragraph 8 of GASB Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*, states that the statement of net position should report the residual amount as *net position*, rather than net assets, proprietary or fiduciary fund balance, or equity. Net position represents the difference between all other elements in a statement of financial position and should be displayed in three components—*net investment in capital assets; restricted* (distinguishing between major categories of restrictions); and *unrestricted*.

Fiscal Control and Internal Auditing Act (Act) (30 ILCS 10/3001) requires the Department to establish and maintain a system or systems of internal fiscal and

State of Illinois
Department of Employment Security
Schedule of Finding
For the Year Ended June 30, 2013

Current Finding - *Government Auditing Standards* (Continued)

2013-001 Inadequate Controls Over Financial Close and Reporting (Continued)

administrative controls, which shall provide assurance that revenues, expenditures, and transfers of assets, resources or funds applicable to operations are properly recorded and accounted for to permit preparation of accounts and reliable financial and statistical reports. When estimation is used to record financial statement amounts, a subsequent analysis should be performed to determine if the estimate should be updated or corrected to ensure reasonable amounts are being recorded in the financial statements.

Department officials stated that due in large part to federal funding reductions, IDES staff has dropped by a third in the past two years. As a result, over a hundred employees moved into new positions via the bargaining unit contract's layoff provisions. As a result, IDES did not complete the submission of the GAAP reports timely and made errors in presentation. IDES was in contact with the Comptroller and the auditors on dates and status for submission of the reports with the focus on accurate financial information.

The accrual adjustment was due to timing of the expenditures with the Comptroller. The items were submitted for payment in June and thought were paid in June, but were actually paid by the Comptroller on July 3rd. The Department's current accounting system does not allow for the recording of payables and assumes paid when submitted to the Comptroller.

The cause for the error on the reporting of the Master Bond fund is due to the agency not having bond reporting in ten years. There were changes in the reporting requirements on bonds since the last time the agency presented financial information resulting in minor errors in presentation.

The GASB Statement No. 63 change resulted in a change in wording from Assets to Position on two schedules. The agency used the draft from the previous year with the incorrect terminology.

The "also noted section" references the Department's agreed estimates for the reporting of accounts payable and accrued liabilities. GAAP requires management to make estimates and assumptions to prepare timely reports. The Department has used the actual amounts through July for the estimate of their liability for over 10 years and the method provides an estimate that is within 0.1% of actual expenditures and, therefore, is a reasonable estimate for GAAP basis financial statement reporting.

**State of Illinois
Department of Employment Security
Schedule of Finding
For the Year Ended June 30, 2013**

Current Finding - *Government Auditing Standards* (Continued)

2013-001 Inadequate Controls Over Financial Close and Reporting (Continued)

Inadequate internal controls over financial close and reporting prevent the Department from preparing financial statements in accordance with GAAP and could result in inaccurate, incomplete and untimely preparation of financial statements. Also, management or employees in the normal course of performing their assigned functions may not be able to prevent or detect financial statement misstatements in a timely manner. (Finding Code No. 2013-001)

Recommendation

We recommend the Department establish and implement procedures to ensure required financial information is prepared and submitted to the Comptroller in a timely manner. We also recommend the Department improve controls over yearend financial closure and reporting to ensure accurate presentation and disclosure of the Department's financial statements.

Department Response

The Department accepts the recommendation. The modest amounts at issue involve a time period in which the Department paid over \$3 billion in unemployment insurance benefits and bonded over \$1.6 billion to support those payments. The discrepancies noted have already been corrected. To improve the process, the Department is already training employees and upgrading portions of its 15 year old accounting systems.

It is important to note that during this time period the Department lost a third of its staff due in large part to federal funding reductions. In addition, over a hundred employees moved into new positions via the bargaining unit contract's layoff provisions. This resulted in reduced staffing as well as inexperienced staff participating in many efforts.

**STATE OF ILLINOIS
DEPARTMENT OF EMPLOYMENT SECURITY**

**Nonshared Proprietary Fund
Financial Statements
For the Year Ended June 30, 2013**

Performed as Special Assistant Auditors
for the Auditor General, State of Illinois

**State of Illinois
Department of Employment Security
Financial Statements
For the Year Ended June 30, 2013**

FINANCIAL STATEMENT REPORT SUMMARY

The audits of the accompanying nonshared proprietary fund financial statements of the State of Illinois, Department of Employment Security (Department) were performed by E. C. Ortiz & Co., LLP.

Based on their audit, the auditors expressed unmodified opinion on the Department's nonshared proprietary fund financial statements.

SUMMARY OF FINDING

The auditors identified a matter involving the Department's internal control over financial reporting that they considered to be a material weakness. The material weakness is described in the accompanying Schedule of Finding on pages 49 - 54 of this report as item 2013-001 (*Inadequate Controls Over Financial Close and Reporting*).

EXIT CONFERENCE

The finding and recommendation appearing in this report were discussed with Department personnel at an exit conference conducted on January 24, 2014. Attending were:

Illinois Department of Employment Security

Jay Rowell, Director

Joseph Mueller, General Counsel (via video conference)

Barbara Piwowarski, Executive Deputy Director, Administration

Amit Singla, Executive Deputy Director, Service Delivery

Monica Carranza, Chief Information Officer

Linda DeMore, Chief Financial Officer

Marcus Dodd, Chief Internal Auditor

Brian Hooper, Legislative Liaison

Kathy Harlan, Audit Liaison

Office of the Auditor General

Thomas Kizziah, Manager

E. C. Ortiz & Co., LLP

Edilberto Ortiz, Partner

Leilani Rodrigo, Partner

Emily Causon, Manager

Marceliana Caragan, IT Manager

The response to the recommendation was provided by Kathy Harlan, Audit Liaison, in a letter dated January 30, 2014.



INDEPENDENT AUDITORS' REPORT

Honorable William G. Holland
Auditor General
State of Illinois

Report on the Financial Statements

As Special Assistant Auditors for the Auditor General, we have audited the accompanying financial statements of the Unemployment Compensation Trust Fund (Nonshared Proprietary Fund) of the State of Illinois, Department of Employment Security (Department), as of and for the year ended June 30, 2013, and the related notes to the financial statements, as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management 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.

Auditors' Responsibility

Our responsibility is to express an opinion 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 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 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 audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Nonshared Proprietary Fund of the Department, as of June 30, 2013, and the changes in financial position and where applicable, cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As discussed in Note 2, the financial statements present only the Nonshared Proprietary Fund and do not purport to, and do not, present fairly the financial position of the State of Illinois or the Department, as of June 30, 2013, and the changes in its financial position or where applicable, its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

Other Matter

Required Supplementary Information

Management has omitted management's discussion and analysis for the Nonshared Proprietary Fund that accounting principles generally accepted in the United States of America require to be presented to supplement the financial statements. Such missing information, although not a part of the financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the financial statements in an appropriate operational, economic, or historical context. Our opinion on the financial statements is not affected by this missing information.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated January 30, 2014 on our consideration of the Department's internal control over financial reporting of the Nonshared Proprietary Fund and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Department's internal control over financial reporting of the Nonshared Proprietary Fund and its compliance.

Restricted Use of This Auditors' Report

This report is intended solely for the information and use of the Auditor General, the General Assembly, the Legislative Audit Commission, the Governor, the Comptroller, Department

management, 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.

C. C. O'Leary & Co. LLC
Chicago, Illinois
January 30, 2014

State of Illinois
Department of Employment Security
Nonshared Proprietary Fund
Statement of Net Position
June 30, 2013
(Amounts in \$000's)

	Unemployment Compensation Trust Fund
Current assets	
Cash and cash equivalents, unrestricted	\$ 75,397
Cash and cash equivalents, restricted	27,108
Deposits held by federal government	1,104,400
Receivables, net	
Taxes	693,459
Intergovernmental	63,280
Other	224,394
Due from State funds	7,192
Due from component units	229
Unamortized bond issuance costs	1,430
Total current assets	2,196,889
Noncurrent asset	
Unamortized bond issuance costs	3,006
Total assets	2,199,895
Current liabilities	
Benefit payments payable	164,231
Intergovernmental payables	4,441
Due to other State funds	3,236
Accrued bond interest expense	2,596
Revenue bonds payable, net	197,309
Total current liabilities	371,813
Noncurrent liability	
Revenue bonds payable, net	1,190,409
Total liabilities	1,562,222
Net position	
Restricted for payment of benefits	1,933,527
Unrestricted	(1,295,854)
Total net position	\$ 637,673

See Notes to Financial Statements.

State of Illinois
Department of Employment Security
Nonshared Proprietary Fund
Statement of Revenues, Expenses, and Changes in Net Position
For the Year Ended June 30, 2013
(Amounts in \$000's)

	Unemployment Compensation Trust Fund
Operating revenues	
Contributions - unemployment taxes	\$ 3,209,923
Federal government	1,440,204
Total operating revenues	<u>4,650,127</u>
Operating expenses	
Benefit payments and refunds	3,560,948
Interest expense	2,351
Total operating expenses	<u>3,563,299</u>
Operating income	<u>1,086,828</u>
Nonoperating revenues (expenses)	
Interest and investment income	15,431
Interest expense	(24,020)
Amortization expense	(2,327)
Other nonoperating revenues	842
Total nonoperating revenues (expenses)	<u>(10,074)</u>
Income before transfers	1,076,754
Other financing uses	
Transfers out	(19,910)
Total other financing uses	<u>(19,910)</u>
Change in net position	1,056,844
Net position (deficit), July 1, 2012	<u>(419,171)</u>
Net position, June 30, 2013	<u><u>\$ 637,673</u></u>

See Notes to Financial Statements.

State of Illinois
Department of Employment Security
Nonshared Proprietary Fund
Statement of Cash Flows
For the Year Ended June 30, 2013
(Amounts in \$000's)

	Unemployment Compensation Trust Fund
Cash flows from operating activities	
Contributions - unemployment taxes received	\$ 3,177,936
Federal grants received	1,451,215
Unemployment benefits paid	(3,687,718)
Net cash provided by operating activities	<u>941,433</u>
Cash flows from noncapital financing activities	
Proceeds from loans	95,134
Loan repayments	(1,233,398)
Proceeds from revenue bonds	1,626,932
Principal paid on revenue bonds	(203,055)
Interest paid on revenue bonds	(57,583)
Interest paid on federal advance	(48,391)
Bond issuance costs	(6,763)
Miscellaneous receipts	2,720
Transfers out	(19,910)
Net cash provided by noncapital financing activities	<u>155,686</u>
Cash flows from investing activity	
Interest and investment income	15,431
Cash provided by investing activity	<u>15,431</u>
Net increase in cash and cash equivalents	1,112,550
Cash and cash equivalents, July 1, 2012	<u>94,355</u>
Cash and cash equivalents, June 30, 2013	<u>\$ 1,206,905</u>
 <i>Reconciliation of cash and cash equivalents to the Statement of Net Position</i>	
Cash and cash equivalents, unrestricted	\$ 75,397
Cash and cash equivalents, restricted	27,108
Deposits held by federal government	1,104,400
Cash and cash equivalents, June 30, 2013	<u>\$ 1,206,905</u>
 Reconciliation of operating income to net cash provided by operating activities:	
Operating income	\$ 1,086,828
Adjustments to reconcile operating income to net cash provided by operating activities:	
Interest expense	2,351
Provision for uncollectible accounts	(35,647)
Changes in assets and liabilities:	
Receivables	(147,373)
Intergovernmental receivables	32,219
Due from State funds	6,942
Due from component units	10
Benefit payments payable	(1,922)
Intergovernmental payables	(1,947)
Due to other State funds	(28)
Net cash provided by operating activities	<u>\$ 941,433</u>

See Notes to Financial Statements.

State of Illinois
Department of Employment Security
Nonshared Proprietary Fund
Notes to Financial Statements
June 30, 2013
(Amounts in \$000's)

NOTE 1 - DESCRIPTION OF FUNDS

The State of Illinois, Department of Employment Security (Department) administers the nonshared proprietary fund as described below. A nonshared fund is a fund in which a single State agency is responsible for administering substantially all financial transactions of the fund.

Unemployment Compensation Trust Fund

The following have been combined for financial reporting purposes as Unemployment Compensation Trust Fund (UCTF):

a) Unemployment Compensation Trust Fund

The Unemployment Compensation Trust Fund (UTF) accounts for assets held by the Department in a trustee capacity, for which the principal and income may be expended in the course of the fund's designated operations. The fund, a locally held fund, receives employer contributions and disburses money in the form of unemployment benefits paid to eligible claimants. This fund also receives federal funding to pay eligible claimants for any federally mandated benefit programs. The UTF is not appropriated by the General Assembly and is intended to be self-supporting.

b) Master Bond Fund

The Master Bond Fund (MBF) accounts for fund building receipts which are used for the payment of obligations in connection with bond issuance, including principal and interest and bond administrative expenses. This locally held fund, was reestablished in July 2012 by an amendment to the Unemployment Insurance Act by the Authorizing Legislation (Public Act 93-0634, as supplemented by Public Act 93-0676) where employers' contributions attributable to the fund building rate shall be directed for deposit into the MBF. The authorizing legislation authorizes the State to issue bonds to (1) repay principal and interest on unpaid advances to the State's unemployment trust account within the Federal Unemployment Trust Fund; (2) pay unemployment benefits by depositing a portion of the proceeds in the State's unemployment trust account within the Federal Unemployment Trust Fund; and (3) pay costs of issuance. The MBF is not appropriated by the General Assembly and is intended to be self-supporting.

State of Illinois
Department of Employment Security
Nonshared Proprietary Fund
Notes to Financial Statements
June 30, 2013
(Amounts in \$000's)

The Governmental Accounting Standard Board (GASB) has issued Statement No. 54, *Fund Balance Reporting and Governmental Type Definitions*. This Statement indicates that a fund that has a significant amount in revenue from transfers in should not be reported as its own special revenue fund. As the MBF does not have a “specific revenue source,” it was not shown as an independent special revenue fund.

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The financial statements of the nonshared proprietary fund have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP), as prescribed by the Governmental Accounting Standards Board (GASB). To facilitate understanding of the financial statements, significant accounting policies are summarized below.

A. Reporting Entity

As defined by GAAP, the financial reporting entity consists of a primary government, as well as its component units, which are legally separate organizations for which the elected officials of the primary government are financially accountable. Financial accountability is defined as:

- a) Appointment of a voting majority of the component unit's board and either (a) the primary government's ability to impose its will, or (b) the possibility that the component unit will provide financial benefit to or impose a financial burden on the primary government; or
- b) Fiscal dependency on the primary government.

Based upon the required criteria, neither of the Nonshared Proprietary Fund has component units, nor is either a component unit of any other entity. However, because the Nonshared Proprietary Fund is not legally separate from the State of Illinois, they are included in the financial statements of the State as proprietary fund. The State of Illinois' Comprehensive Annual Financial Report (CAFR) may be obtained by writing to the State Comptroller's Office, Financial Reporting Department, 325 West Adams Street, Springfield, Illinois, 62704-1871.

The financial statements present only the Nonshared Proprietary Fund administered by the Department and do not purport to, and do not, present fairly the financial position of the Department as of June 30, 2013, nor changes in its financial position and cash flows for the year then ended in conformity with GAAP.

State of Illinois
Department of Employment Security
Nonshared Proprietary Fund
Notes to Financial Statements
June 30, 2013
(Amounts in \$000's)

B. Basis of Presentation

In government, the basic accounting and reporting entity is a fund. A fund is defined as an independent fiscal and accounting entity with a self-balancing set of accounts recording cash and/or other resources together with all related liabilities, obligations, reserves, and equities, which are segregated for the purpose of carrying on specific activities or attaining certain objectives in accordance with special regulations, restrictions, or limitations. A Statement of Net Position, Statement of Revenues, Expenses, and Changes in Net Position, and Statement of Cash Flows have been presented for the Nonshared Proprietary Fund administered by the Department.

The Nonshared Proprietary Fund is an enterprise fund. Enterprise funds are used to report any activity for which a fee is charged to external users for goods and services. Activities are required to be reported as enterprise funds if any one of the following criteria is met when applied in the context of the activity's principal revenue sources: the activity is financed with debt that is secured solely by a pledge of net revenues from fees and charges of the activity; laws and regulations require that the activity's costs of providing service, including capital costs, be recovered with fees and charges, rather than taxes or similar revenues; or the pricing policy of the activity establishes fees and charges designed to recover its costs, including capital costs.

The Department administers the unemployment insurance program under various federal and State statutes and regulations. The UTF was established under Title IX of the Social Security Act to provide partial protection to workers against the loss of wages when they are out of work due to no fault of their own. To fund this program, the agency receives monies from employers to maintain the fund, which are then used to pay benefits to the unemployed workers who meet the eligibility requirements of the law.

These funds are held by the United States Treasury in an unemployment trust fund and are restricted to the payment of unemployment benefits. Unemployment benefits drawn from the fund are awarded to qualified former employees of covered Illinois employers. Employers are required to contribute to the unemployment trust fund based on employees' wages and their past experience level of causing unemployment. The overall rate used to determine contributions for the Illinois Unemployment Insurance Trust Fund is designed to recover the payment of unemployment benefits plus maintain a reasonable balance to protect the solvency of the fund if unemployment rates rise significantly.

State of Illinois
Department of Employment Security
Nonshared Proprietary Fund
Notes to Financial Statements
June 30, 2013
(Amounts in \$000's)

Operating revenues, such as collections of unemployment tax contributions, result from exchange transactions associated with the principal activity of the fund. Exchange transactions are those in which each party receives and gives up essentially equal values. Nonoperating revenues, such as investment earnings, result from nonexchange transactions or ancillary activities.

Interest expense arising from loans to the federal government is classified operating expenses by the Department management. Interest expense on MBF is classified as noncapital financing activity. The Department management classifies expenses based on the purposes of the funds to which it was created.

C. Basis of Accounting

The Nonshared Proprietary Fund is reported using the economic resources measurement focus and the accrual basis of accounting.

Revenues are recorded when earned and expenses are recorded at the time liabilities are incurred, regardless of when the related cash flow takes place. Nonexchange transactions, in which the Department gives (or receives) value without directly receiving (or giving) equal value in exchange, include federal funding for federally mandated benefit programs. On an accrual basis, revenues from employer contributions are recognized in the fiscal year in which the underlying exchange transaction occurs. Revenues from grants, entitlements, and similar items are recognized in the fiscal year in which all eligibility requirements imposed by the provider have been met.

D. Cash and Cash Equivalents

Cash and cash equivalents consist principally of cash in banks for locally held funds, U.S. government securities, and pooled investment funds held by other governmental agencies with a maturity of three months or less.

E. Interfund Transactions

The Nonshared Proprietary Fund has the following types of interfund transactions with other funds of the State:

a) *Reimbursements*

Repayments from the funds responsible for particular expenditures or expenses to the

State of Illinois
Department of Employment Security
Nonshared Proprietary Fund
Notes to Financial Statements
June 30, 2013
(Amounts in \$000's)

fund that initially paid for them. Reimbursements are reported as expenditures in the reimbursing fund and as a reduction of expenditures in the reimbursed fund.

b) Transfers

Flows of assets (such as cash or goods) without equivalent flows of assets in return and without a requirement for repayment. Transfers are reported after nonoperating revenues and expenses.

F. Net Position

Net position consists of the following:

- a) Restricted - consists of restricted assets reduced by liabilities and deferred inflows of resources related to those assets. Net position restricted for payment of unemployment benefits totaled \$1,933,527 as of June 30, 2013.
- b) Unrestricted - is the net amount of the assets, liabilities and deferred outflows of resources that are not included in the determination of the restricted component of net position. Unrestricted net deficit pertaining to MBF totaled \$1,295,854 as of June 30, 2013.

When both restricted and unrestricted resources are available for use, generally it is the State's policy to use restricted resources first, then unrestricted resources when they are needed.

G. Use of Estimates

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

H. New Accounting Pronouncements

Effective July 1, 2012, the Department adopted the following accounting pronouncements:

State of Illinois
Department of Employment Security
Nonshared Proprietary Fund
Notes to Financial Statements
June 30, 2013
(Amounts in \$000's)

- GASB Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*, which incorporated into the GASB's authoritative literature certain accounting and financial reporting guidance that is included in the Financial Accounting Standards Board Statements and Interpretations, Accounting Principles Board Opinions, and Accounting Research Bulletins of the American Institute of Certified Public Accountants' Committee on Accounting Procedure that were issued on before November 30, 1989, which does not conflict with or contradict GASB pronouncements.
- GASB Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*, provided financial reporting guidance for deferred outflows of resources and deferred inflows of resources.

The implementation of these statements had no significant impact on the Department's financial statements.

NOTE 3 - DEPOSITS

At June 30, 2013, cash and cash equivalents for the UTF for a locally held fund has a carrying amount in the accompanying financial statements of \$75,397.

At June 30, 2013, cash on deposit for the UTF for locally held funds has a negative carrying amount and bank balance of \$969 and \$924, respectively. Bank balances are fully insured by the Federal Depository Insurance Corporation (FDIC). On June 30, 2013, a transfer from the bank to the deposits held by the federal government was made for more than what the Department approved and briefly caused an overdrawn bank balance.

Deposits in Illinois Funds and in the custody of the State Treasurer for the UTF totaled \$77,261 and have a carrying amount of \$76,365 at June 30, 2013. The State Treasurer is the custodian of the State's cash and cash equivalents for funds maintained in the State Treasury. The Department independently manages cash and cash equivalents maintained outside the State Treasury. The State of Illinois' CAFR may be obtained by writing to the State Comptroller's Office, Financial Reporting Department, 325 West Adams Street, Springfield, Illinois, 62704-1871.

Funds deposited in Illinois Funds and held by the State Treasurer are pooled and invested with other State funds in accordance with the Deposit of State Moneys Act of Illinois Compiled Statute (15 ILCS 520/11). These deposits have not been categorized as to credit risk because the

State of Illinois
Department of Employment Security
Nonshared Proprietary Fund
Notes to Financial Statements
June 30, 2013
(Amounts in \$000's)

Department does not own individual securities. Detail on the nature of these investments is available within the State of Illinois' CAFR.

Illinois Funds is not registered with the SEC as an investment company, but does operate in a manner consistent with Rule 2a7 of the Investment Company Act of 1940. Investments in Illinois Funds are valued at Illinois Funds' share price, which is the price at which the investment could be sold.

Deposits held by the federal government totaled \$1,104,400 as of June 30, 2013. These deposits are pooled and invested with other States' funds and are not categorized as to credit risk because the Department does not own individual securities.

At June 30, 2013, deposit for the MBF locally held fund, is as follows:

	<u>Credit Rating</u>	<u>Maturity</u>	<u>Carrying Amount</u>	<u>Fair Value</u>
Goldman Sachs Financial	AAAm by S & P			
Square Government Fund	<u>Aaa-mf by Moody's</u>	<u>< 90 days</u>	<u>\$27,108</u>	<u>\$27,108</u>

This is restricted for the purposes described in Note 1. Those deposits are invested in the Goldman Sachs Financial Square Government Fund and held by the Bond Trustee in accordance with the Master Indenture of Trust.

Custodial credit risk is the risk that in the event of custodian failure, investment principal may not be returned. At June 30, 2013, investments consisted solely of money market funds held at Goldman Sachs. An investment in a money market portfolio is not insured or guaranteed by the Federal Deposit Insurance Corporation or any other government agency.

Interest rate risk exists when there is a possibility that changes in interest rates could adversely affect an investment's value. The Department does not have formal policy that limits investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates. The Fund's investment return and principal value will fluctuate so that an investor's shares, when redeemed, may be worth more or less than their original cost.

Credit risk exists when there is a possibility that the issuer or other counterparty to an investment may be unable to fulfill its obligations. The Department does not have a formal policy limiting credit risk.

State of Illinois
Department of Employment Security
Nonshared Proprietary Fund
Notes to Financial Statements
June 30, 2013
(Amounts in \$000's)

NOTE 4 - TAXES RECEIVABLE

Taxes receivable represent unemployment taxes, known as contributions, owed by private and non-governmental employers. The allowance for uncollectible taxes has been based on historical collection experience which, per statute, is typically on a 4-year collection cycle.

Balances as of June 30, 2013, are as follows:

Unemployment taxes	\$ 807,538
Interest and penalties receivables on taxes	89,354
Total taxes receivable	<u>896,892</u>
Less allowance for uncollectible taxes	<u>(203,433)</u>
Taxes receivable, net	<u><u>\$ 693,459</u></u>

NOTE 5 - INTERGOVERNMENTAL RECEIVABLES

Intergovernmental receivables represent reimbursements due from other State and local governments and from the federal government for unemployment benefits paid to those governments' ex-employees totaling \$21,754 and \$41,526, respectively, at June 30, 2013.

NOTE 6 - OTHER RECEIVABLES

Other receivables represent amounts due from claimants who received benefits that exceeded their allowable amounts. The allowance for uncollectible accounts has been based on historical collection experience which, per statute, is typically on a 5-year collection cycle.

Balances as of June 30, 2013 are as follows:

Other receivables	\$ 790,670
Less allowance for uncollectible accounts	<u>(566,276)</u>
Other receivables, net	<u><u>\$ 224,394</u></u>

State of Illinois
Department of Employment Security
Nonshared Proprietary Fund
Notes to Financial Statements
June 30, 2013
(Amounts in \$000's)

NOTE 7 - INTERFUND BALANCES AND ACTIVITIES

(a) Balances Due from/to Other Funds

The following balances at June 30, 2013 represent amounts due from other Department and State of Illinois funds.

<u>Description/Purpose</u>	<u>Due from Other Funds</u>	<u>Due to Other Funds</u>
Due from General Revenue Fund for reimbursement of unemployment benefits paid to employees of other State agencies	\$ 5,447	\$ —
Due from Operating Fund for reimbursement of unemployment benefits to former employees of the Department	1,745	—
Due to Operating Fund for discretionary transfers of penalties and interests	—	3,231
Due to Operating Fund for discretionary transfers of non-sufficient funds (NSF) fees	—	5
Total	<u>\$ 7,192</u>	<u>\$ 3,236</u>

Due from component units of the State of Illinois balance at June 30, 2013 of \$229 represents reimbursement of unemployment benefits paid to employees of State universities.

(b) Transfers to Other Funds

Interfund transfers out for the year ended June 30, 2013, were as follows:

<u>Description/Purpose</u>	<u>Amount</u>
Discretionary transfers of penalties and interests to Operating Fund	\$ 19,897
Discretionary transfers of NSF fees to Operating Fund	13
Total	<u>\$ 19,910</u>

State of Illinois
Department of Employment Security
Nonshared Proprietary Fund
Notes to Financial Statements
June 30, 2013
(Amounts in \$000's)

NOTE 8 - INTERGOVERNMENTAL PAYABLES

Intergovernmental payables of \$4,441 represent interstate combined wage claim benefits payable.

NOTE 9 - BONDS PAYABLE

On July 31, 2012, the Unemployment Insurance Fund Building Receipts Revenue Bonds, Series 2012 totaling \$1,469,940 were issued pursuant to the Master Indenture of Trust, dated as of July 18, 2012 with U.S. Bank as Trustee. The payment of principal, premiums and interest is secured by a pledge of and lien on the pledged revenues, the sole source of which is the fund building receipts. The bonds were issued as follows:

<u>Bonds</u>	<u>Amount</u>
Series 2012A	\$ 652,075
Series 2012B	707,865
Series 2012C	110,000

Series 2012A Bonds - original issues \$652,075, dated July 31, 2012, provides for retirement of principal and interest on June 15 and December 15 at rates of 2% - 5%. Maturity is from June 15, 2013 to December 15, 2016.

Series 2012B Bonds - original issues \$707,865, dated July 31, 2012, provides for retirement of principal and interest on June 15 and December 15 at rates of 4% - 5%. Maturity is from June 12, 2017 to June 20, 2020.

Series 2012C Bonds - original issues \$110,000, dated July 31, 2012, provides for retirement of principal on June 15, 2021 and interest on June 15 and December 15 at rate of 1.5%. This bond is subject to special mandatory super sinker redemption in accordance with the Trust Indenture.

The bonds were issued due to the depletion of the UTF in July 2009 and continued borrowing from the federal government to pay unemployment benefits. The State, acting by and through the Department, is authorized to issue bonds pursuant to Public Act 93-0634, as supplemented by Public Act 93-0676 (the Authorizing Legislation) for the purposes of repaying principal and interest on unpaid advances to the State's unemployment trust accounts with the Federal Unemployment Trust Fund; paying unemployment benefits by depositing a portion of the proceeds in the State's unemployment trust fund; paying a portion of the interest on the series 2012 bonds; and paying costs of issuance.

State of Illinois
Department of Employment Security
Nonshared Proprietary Fund
Notes to Financial Statements
June 30, 2013
(Amounts in \$000's)

On July 31, 2012, all Series 2012 bonds were issued and part of the proceeds were used to pay the outstanding loan to the federal government as follows:

Loan balance at June 30, 2012	\$ 1,138,264
July 2012 loan advances	95,134
July 2012 loan repayments	(48,013)
SFY 2013 applied FUTA credit	<u>(2,283)</u>
Loan balance, net	<u>1,183,102</u>
Payment from bond proceeds	<u>(1,183,102)</u>
Balance	<u><u>\$ -</u></u>

The interest on federal loans through July 1, 2012, totaling \$48,391 and the balance of the loans were paid on July 31, 2012 from the proceeds of the bonds issued.

The following is a summary of the bond transactions of the Department for the year ended June 30, 2013:

Series	Balance as of June 30, 2012	Additions	Retirements	Balance as of June 30, 2013	Amount Due Within One Year
2012A	\$ -	\$ 652,075	\$ (93,055)	\$ 559,020	\$ 160,790
2012B	-	707,865	-	707,865	-
2012C	-	110,000	(110,000)	-	-
Unamortized premium	-	156,992	(36,159)	120,833	36,519
Total	<u>\$ -</u>	<u>\$ 1,626,932</u>	<u>\$ (239,214)</u>	<u>\$ 1,387,718</u>	<u>\$ 197,309</u>

The first specific bond maturity was due on June 15, 2013 in Series 2012A and \$93,055 was redeemed on June 17, 2013. Additionally, an interest payment of \$32,904 for all Series 2012 bonds was paid on June 17, 2013. Series 2012C bonds are subject to mandatory early redemption when funds are available from excess pledged revenue and surplus program receipts. All of the Series 2012C bonds were redeemed on June 17, 2013 in the amount of \$110,000 from the proceeds of excess pledged revenue in the amount of \$42,740 and surplus program receipts in the amount of \$67,260. Retained Pledged Revenues after the redemption is \$25,000.

Accrued bond interest expense as of June 30, 2013 totaled \$2,596.

State of Illinois
Department of Employment Security
Nonshared Proprietary Fund
Notes to Financial Statements
June 30, 2013
(Amounts in \$000's)

The future debt service requirements for revenue bonds as of June 30, 2013, including interest payments are as follows:

Fiscal Period Ending June 30	Principal	Interest	Total
2014	\$ 160,790	\$ 61,311	\$ 222,101
2015	168,320	53,353	221,673
2016	176,690	44,952	221,642
2017	185,635	36,127	221,762
2018	194,845	26,802	221,647
2019 - 2020	380,605	23,717	404,322
Total	<u>\$ 1,266,885</u>	<u>\$ 246,262</u>	<u>\$ 1,513,147</u>

Bond issuance costs and bond premium are amortized over the term of the bonds using straight line method. The following changes occurred during the year:

	Balance as of June 30, 2012	Addition	Amortization	Balance as of June 30, 2013	Amount Due Within One Year
Bond issuance costs	<u>\$ —</u>	<u>\$ 6,763</u>	<u>\$ 2,327</u>	<u>\$ 4,436</u>	<u>\$ 1,430</u>

NOTE 10 - CONTINGENCIES

The Department is involved in various claims and legal actions arising in the ordinary course of business. It is the opinion of management that the ultimate disposition of these matters will not have a material effect on the Nonshared Proprietary Fund financial statements.



E.C. ORTIZ & CO., LLP
CERTIFIED PUBLIC ACCOUNTANTS

**INDEPENDENT AUDITORS' 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***

Honorable William G. Holland
Auditor General
State of Illinois

As Special Assistant Auditors for the Auditor General, we have audited, in accordance with the 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, the financial statements of the Unemployment Compensation Trust Fund (Nonshared Proprietary Fund) of the State of Illinois, Department of Employment Security (Department), as of and for the year ended June 30, 2013, and the related notes to the financial statements, and have issued our report thereon dated January 30, 2014.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Department's internal control over financial reporting (internal control) of the Nonshared Proprietary Fund to determine the 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 Department's internal control. Accordingly, we do not express an opinion on the effectiveness of the Department's internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph 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, as described in the accompanying Schedule of Finding, we identified a certain deficiency in internal control that we consider to be a material weakness.

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 in the accompanying Schedule of Finding as item 2013-001 to be a material weakness.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Individual Nonshared Governmental Funds of the Department's financial statements are free from 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*.

Department's Response to Finding

The Department's response to the finding identified in our audit is described in the accompanying Schedule of Finding. The Department's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on the response.

Purpose of This Report

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

E. C. G. & Co. LLC
Chicago, Illinois
January 30, 2014

**State of Illinois
Department of Employment Security
Schedule of Finding
For the Year Ended June 30, 2013**

Current Finding - *Government Auditing Standards*

2013-001 Inadequate Controls Over Financial Close and Reporting

The Department of Employment Security (Department) did not have adequate controls over financial close and reporting to allow management or employees in the normal course of performing their assigned functions to prevent or detect financial statement misstatements in a timely manner.

During our audit, we noted the following:

- a) The Department submitted “GAAP Reporting Packages” to the Illinois Office of the Comptroller (Comptroller) 1 to 21 days late. As part of the year-end accounting and financial reporting closing process, State Agencies are required to prepare and submit to the Comptroller “GAAP Reporting Packages” which summarize their yearly financial activities and the status of their funds at year-end. The “GAAP Reporting Packages” are used by the Comptroller to prepare the State’s Basic Financial Statements.
- b) Several errors and omissions during financial close and reporting process were identified for the following funds:

Title III Social Security and Employment Services Fund (Fund 52)

- The accrual for outstanding unpaid facilities, statistical, and telecommunication services provided by another governmental agency was understated by \$3.8 million. The Department’s yearend accrual (1) did not include invoices totaling \$4.5 million which have been reviewed and vouchered but not yet paid as of June 30, 2013; and (2) included invoices originally posted in September 2012 and duplicated in June 2013 totaling \$0.7 million.

Unemployment Compensation Special Administration Fund (Fund 55)

- Adjusting entries posted by the Comptroller at the request of the Department in relation to a fund transfer made in August of the following fiscal year which increased expenditures and accounts payable, resulting in an overstatement of \$2.9 million.

Master Bond Fund (Fund 1368)

- Assets and liabilities were not presented in a classified format to distinguish between current and long-term assets and liabilities. The noncurrent portion of

**State of Illinois
Department of Employment Security
Schedule of Finding
For the Year Ended June 30, 2013**

Current Finding - *Government Auditing Standards* (Continued)

2013-001 Inadequate Controls Over Financial Close and Reporting (Continued)

unamortized bond issue cost of \$3.0 million was presented as part of current assets. The noncurrent revenue bonds payable and unamortized bond premium of \$1,106.1 million and \$84.3 million, respectively, were presented as part of current liabilities.

- Financial statement disclosures did not include information related to (1) debt service requirements to maturity and (2) future minimum payments of the debt obligation.
- The “Due to Other Funds” amount in the Statement of Net Position did not agree with the amount presented in the Notes to Financial Statements. An adjusting entry to remove effects of interfund transactions totaling \$62.9 million was not included when summarizing the information presented in the Notes to Financial Statements. The Notes to Financial Statements was subsequently corrected by the Department to present correct amount of “Due to Other Funds.”

Unemployment Compensation Trust Fund (Fund 1138) and Master Bond Fund (Fund 1368)

- Eliminating entries for interfund transfers totaling \$323.9 million were not recorded.
- The Department did not present its draft financial statements in accordance with Government Accounting Standards Board Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*. Statement of Net Position and Statement of Revenues, Expenses, and Changes in Net Position were presented as Statement of Net Assets and Statement of Revenues, Expenses, and Changes in Net Assets.
- The Notes to Financial Statements included a disclosure on federal expenditures totaling \$1,019.3 million, identified under the American Recovery and Reinvestment Act of 2009 programs. The disclosure was not applicable for the current year’s financial statements.

The Department subsequently corrected the financial statements for the above adjustments and omissions.

**State of Illinois
Department of Employment Security
Schedule of Finding
For the Year Ended June 30, 2013**

Current Finding - *Government Auditing Standards* (Continued)

2013-001 Inadequate Controls Over Financial Close and Reporting (Continued)

We also noted the following:

Special Programs Fund (Fund 1136)

- Accounts payable and accrued liabilities was understated by \$0.05 million. The Department recorded benefit payments through July of the following fiscal year while the auditors identified FY 2013 benefit payments paid by the Department through mid-November.

Unemployment Compensation Trust Fund (Fund 1138)

- The allowance for uncollectible taxes, interest and penalties was erroneously calculated resulting in an overstatement of \$8.9 million to the allowance for uncollectible taxes, interest and penalties and understatement to contribution revenues.
- The “Receivables - Others” and its related allowance for uncollectible accounts were understated by \$2.0 million. The Department made a yearend adjustment to reconcile the general ledger and subsidiary ledger but failed to include this adjustment in the financial statements resulting in an understatement of these accounts.
- Benefit payments payable was understated \$5.3 million. The Department recorded benefit payments through July of the following fiscal year while the auditors identified FY 2013 benefit payments paid by the Department through mid-November.

These adjustments were not material to the financial statements and were not booked by the Department as of June 30, 2013.

The Statewide Accounting Management System (SAMS) Procedure 27.10.10 states that all State agencies (excluding those agencies whose GAAP reporting packages are completed by the Comptroller’s staff in consultation with agency personnel - referred to as “in-house”) are required to submit annual GAAP reporting packages for any fund or funds in which they expend from and/or deposit receipts. For fiscal year ended June 30, 2013, the GAAP reporting packages due dates for locally held funds was on August 9, 2013 and treasury-held fund on August 16, 2013, except for

**State of Illinois
Department of Employment Security
Schedule of Finding
For the Year Ended June 30, 2013**

Current Finding - *Government Auditing Standards* (Continued))

2013-001 Inadequate Controls Over Financial Close and Reporting (Continued)

governmental fund (Fund 52) and proprietary funds (Fund 1138 and Fund 1368) which was extended to September 9, 2013.

Generally accepted accounting principles (GAAP) require that expenditures for goods and services and related payables reported in the financial statements exist and represent valid transactions that occurred during the period. In addition, Procedure 03.50.10 of the SAMS Manual states that expenditures and related liabilities should be recognized in the accounting period in which the liability is incurred.

Paragraph 59 of GASB Statement No. 34, *Basic Financial Statements and Management's Discussion and Analysis—for State and Local Governments*, states that the eliminations should be made in the statement of activities to remove the doubling up effect of internal service fund activity.

Paragraph 97 of GASB Statement No. 34, *GASB Codification of Governmental Accounting and Financial Reporting Standards* Section 2200.172, also states that the Statement of Net Position should be presented in a classified format to distinguish between current and long-term assets and liabilities.

Paragraph 10 of GASB Statement No. 38, *Certain Financial Statement Note Disclosures*, states that government should disclose the following details of debt service requirements to maturity: (a) principal and interest requirements to maturity, presented separately, for each of the five subsequent fiscal years and in five-year increment thereafter. Interest requirements for variable-rate debt should be determined using the rate in effect at the financial statement date. (b) The terms by which interest rates change for variable debt.

Paragraph 8 of GASB Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*, states that the statement of net position should report the residual amount as *net position*, rather than net assets, proprietary or fiduciary fund balance, or equity. Net position represents the difference between all other elements in a statement of financial position and should be displayed in three components—*net investment in capital assets; restricted* (distinguishing between major categories of restrictions); and *unrestricted*.

Fiscal Control and Internal Auditing Act (Act) (30 ILCS 10/3001) requires the Department to establish and maintain a system or systems of internal fiscal and

**State of Illinois
Department of Employment Security
Schedule of Finding
For the Year Ended June 30, 2013**

Current Finding - *Government Auditing Standards* (Continued))

2013-001 Inadequate Controls Over Financial Close and Reporting (Continued)

administrative controls, which shall provide assurance that revenues, expenditures, and transfers of assets, resources or funds applicable to operations are properly recorded and accounted for to permit preparation of accounts and reliable financial and statistical reports. When estimation is used to record financial statement amounts, a subsequent analysis should be performed to determine if the estimate should be updated or corrected to ensure reasonable amounts are being recorded in the financial statements.

Department officials stated that due in large part to federal funding reductions, IDES staff has dropped by a third in the past two years. As a result, over a hundred employees moved into new positions via the bargaining unit contract's layoff provisions. As a result, IDES did not complete the submission of the GAAP reports timely and made errors in presentation. IDES was in contact with the Comptroller and the auditors on dates and status for submission of the reports with the focus on accurate financial information.

The accrual adjustment was due to timing of the expenditures with the Comptroller. The items were submitted for payment in June and thought were paid in June, but were actually paid by the Comptroller on July 3rd. The Department's current accounting system does not allow for the recording of payables and assumes paid when submitted to the Comptroller.

The cause for the error on the reporting of the Master Bond fund is due to the agency not having bond reporting in ten years. There were changes in the reporting requirements on bonds since the last time the agency presented financial information resulting in minor errors in presentation.

The GASB Statement No. 63 change resulted in a change in wording from Assets to Position on two schedules. The agency used the draft from the previous year with the incorrect terminology.

The "also noted section" references the Department's agreed estimates for the reporting of accounts payable and accrued liabilities. GAAP requires management to make estimates and assumptions to prepare timely reports. The Department has used the actual amounts through July for the estimate of their liability for over 10 years and the method provides an estimate that is within 0.1% of actual expenditures and, therefore, is a reasonable estimate for GAAP basis financial statement reporting.

**State of Illinois
Department of Employment Security
Schedule of Finding
For the Year Ended June 30, 2013**

Current Finding - *Government Auditing Standards* (Continued))

2013-001 Inadequate Controls Over Financial Close and Reporting (Continued)

Inadequate internal controls over financial close and reporting prevent the Department from preparing financial statements in accordance with GAAP and could result in inaccurate, incomplete and untimely preparation of financial statements. Also, management or employees in the normal course of performing their assigned functions may not be able to prevent or detect financial statement misstatements in a timely manner. (Finding Code No. 2013-001)

Recommendation

We recommend the Department establish and implement procedures to ensure required financial information is prepared and submitted to the Comptroller in a timely manner. We also recommend the Department improve controls over yearend financial closure and reporting to ensure accurate presentation and disclosure of the Department's financial statements.

Department Response

The Department accepts the recommendation. The modest amounts at issue involve a time period in which the Department paid over \$3 billion in unemployment insurance benefits and bonded over \$1.6 billion to support those payments. The discrepancies noted have already been corrected. To improve the process, the Department is already training employees and upgrading portions of its 15 year old accounting systems.

It is important to note that during this time period the Department lost a third of its staff due in large part to federal funding reductions. In addition, over a hundred employees moved into new positions via the bargaining unit contract's layoff provisions. This resulted in reduced staffing as well as inexperienced staff participating in many efforts.

**State of Illinois
Department of Employment Security
Prior Findings Not Repeated
For the Year Ended June 30, 2013**

A. Inadequate Controls Over Computer Security

In the prior engagement, the Department of Employment Security (Department) had inadequate controls over the security and use of Super IDs. The Information Services Division programmers were sharing and using Super ID almost daily in the Production environment for resolving transactional or application-related problems that occurred during batch processing. Since the Super IDs were shared, the individual accountability over its use was limited.

Status: Partially implemented

During the current engagement, The Department made significant improvements and implemented measures to reduce reliance on the usage of Super IDs as indicated in the decline in the number of instances of Super ID usage. In addition, the Department implemented an approval process for using Super ID which provides sufficient information to determine the nature of changes made using the Super ID. The transaction logs of Super ID usage were reviewed by the Data Processing Analyst and the review ensured each entry in the log was supported by a written approval of the use of the Super ID. This finding has been moved to IM2013-013. (Finding Code No. 12-1, 11-1, 10-1, 09-2 and 08-2)

B. Improper Accounting of Unapplied Credits

In the prior engagement, the Department of Employment Security (Department) did not properly account for unapplied credits relating to unemployment tax contributions received from other State agencies and component units, totaling to \$4.9 million.

Status: Implemented

During the current engagement, no significant exceptions were noted in relation to our review of unapplied credits. (Finding Code No. 12-2)