

U.S. Department of Labor
Office of Inspector General—Office of Audit

**EMPLOYMENT AND
TRAINING ADMINISTRATION**



**The New Mexico Department of Labor
Improperly Charged Unemployment
Insurance Program Costs to Its Workforce
Investment Act Rapid Response Program**

Date Issued: September 30, 2005
Report Number: 06-05-005-03-390

BRIEFLY...

Highlights of Report Number: 06-05-005-03-390, to the Assistant Secretary for Employment and Training regarding the Workforce Investment Act (WIA) funds granted to the State of New Mexico.

WHY READ THE REPORT

The Office of Inspector General (OIG) reports on audit conclusions regarding New Mexico Department of Labor (NMDOL) Unemployment Insurance (UI) Program Costs charged to its WIA Rapid Response Program.

WHY OIG DID THE AUDIT

The Employment and Training Administration requested OIG's assistance in reviewing the allowability of UI automation project costs charged to grant funds reserved for WIA Rapid Response activities. In response we conducted a performance audit of the issue.

READ THE FULL REPORT

To view the report, including the scope, methodology, and full agency response, go to:

<http://www.oig.dol.gov/public/reports/oa/2004/06-05-005-03-390.pdf>

September 2005

Review of New Mexico UI Program Costs Charged to Its WIA Rapid Response Program

WHAT OIG FOUND

The OIG concluded that the NMDOL improperly charged approximately \$1.65 million of its UI automation project costs, UI personnel compensation costs, and other UI program costs to grant funds reserved for WIA Rapid Response activities.

WHAT OIG RECOMMENDED

We recommended that the Assistant Secretary for Employment and Training: (1) disallow and recover from the NMDOL, from non-Federal funds, the \$1,648,018 of WIA Rapid Response funds that were improperly used to help fund deficits in the NMDOL's UI automation project and to pay for UI staff compensation and other UI expenses; and (2) require the NMDOL to establish controls and procedures to ensure that costs incurred for one program are not shifted to other programs either through journal voucher adjustments or direct charges. Journal vouchers should be documented and properly approved.

The State of New Mexico's response stated that on January 22, 2004, the New Mexico Office of Workforce Training and Development was designated as the State agency responsible for administration of WIA funds and became responsible for repayment of any disallowed WIA costs. Also, the State disagreed with our audit conclusions on the basis that a WIA Rapid Response event is a jointly conducted activity with "Access to unemployment insurance" being a shared cost objective that may properly be allocated to WIA Rapid Response funds.

We considered the State's response. However, we reject the State's arguments and recommend that ETA disallow the amount of WIA costs that we questioned.

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Executive Summary

We conducted a performance audit to determine if the New Mexico Department of Labor (NMDOL) improperly used Workforce Investment Act (WIA) Rapid Response program funds to help finance the NMDOL's Unemployment Insurance (UI) Claims System Reengineering Project.

Results

We concluded that the NMDOL improperly charged to its WIA Rapid Response program \$1,648,018 of UI program costs as follows:

- \$748,657 of UI personnel compensation costs and other UI program expenses (finding 1.A), and
- \$899,361 of its UI claims system reengineering project costs (finding 1.B).

These costs are questioned as unallowable costs to the NMDOL's WIA Rapid Response program because the costs:

- were charged to the WIA Rapid Response program to use available funds for rapid response, to overcome a budget deficit in the NMDOL's UI claims system reengineering project; and
- were inallocable, unnecessary and unreasonable costs to the WIA Rapid Response program, because they provided no benefit to the Rapid Response program.

Recommendations

We recommend that the Assistant Secretary for Employment and Training:

1. disallow and recover from the NMDOL, from non-Federal funds, the \$1,648,018 of WIA Rapid Response funds that were improperly used to help fund deficits in the NMDOL's UI claims system re-engineering project and to pay for UI personnel compensation costs and other UI expenses; and
2. require the NMDOL to establish controls and procedures to ensure that costs incurred for one program are not shifted to other programs either through journal voucher adjustments or direct charges. Journal vouchers should be documented and properly approved.

State Response

The response, submitted jointly by the New Mexico Office of Workforce Training and Development and the New Mexico Department of Labor, states that our recommendation for disallowance of \$1,648,018 is based on an invalid premise that prorata costs for unemployment insurance claims from WIA rapid response participants could not be charged to the WIA program under 20 CFR 665.310(a) of the WIA Regulations. Also, the response notes that on January 22, 2004, the New Mexico Office of Workforce Training and Development was designated as the State agency responsible for administration of WIA funds and thereby became responsible for repayment of any disallowed WIA costs.

The State contends that “Access to unemployment insurance” is a shared cost objective under 20 CFR 665.310(a)(5); and that in accordance with the advice of NMDOL’s former legal counsel was a valid basis for allocating unemployment insurance benefits system costs to WIA. Additionally, the response states that we did not interview State staff members who engaged in communications with USDOL Regional Office staff that WIA Rapid Response funds would be used as one of the funding sources for the UI automation project. Further, the response states that our conclusion that Rapid Response funds were used to cover a deficit in the automation project is unsupported because Reed Act funds were available for appropriation.

The State also responded that our draft report failed to acknowledge that State policy makers requested a Federal review in July 2004 when presented with staff concerns about the automation project. Finally, the response indicates that, if the expenditures are not allowed, the State would use its available Reed Act appropriations to cover the questionable costs.

OIG Conclusion

Our report is focused on the NMDOL because it was the agency that administered the activities we examined. Although the State has since moved administration of WIA funded activities to the New Mexico Office of Workforce Training and Development, ETA will determine the amount of disallowance and collection procedures.

We disagree with the State’s characterization of our premise for recommending disallowance of the WIA Rapid Response funds used for the UI automation project. Although WIA rules allow Rapid Response funds to be used for providing designated dislocated workers access to UI, it is inappropriate to use WIA Rapid Response funds to supplement funding for UI administration, such as the UI automation project, that is provided by a separate Federal appropriation. Accordingly, our finding and recommendations remain unchanged. The entire State response is provided in Appendix D.

U.S. Department of Labor

Office of Inspector General
Washington, DC. 20210



Assistant Inspector General's Report

Ms. Emily Stover DeRocco
Assistant Secretary for
Employment and Training

At the Employment and Training Administration's (ETA) request, the Office of Inspector General (OIG) performed a performance audit to determine if the New Mexico Department of Labor (NMDOL) improperly used Workforce Investment Act (WIA) Rapid Response program funds to help finance its UI claims system reengineering project.

We concluded that the NMDOL improperly charged \$1,648,018 of UI program costs to grant funds reserved for WIA Rapid Response activities to fund a budget deficit in the agency's UI claims system reengineering project.

We conducted our performance audit in accordance with Government Auditing Standards. Our audit scope, methodology, and criteria are detailed in Appendix B.

Objective: Did the NMDOL improperly charge UI system reengineering project¹ costs to its WIA Rapid Response program?

Finding: The NMDOL improperly charged approximately \$1.65 million of its UI automation project costs, UI personnel compensation costs, and other UI program costs to grant funds reserved for WIA Rapid Response activities.

The NMDOL incurred a deficit of funds while developing a new UI system primarily under contract with TATA Consultancy Services.² As shown in documents prepared internally by NMDOL, \$1.5 million of available funds were identified under the WIA Rapid Response program to complete the UI automation project.

A NMDOL-prepared document titled "WIA Rapid Response History" provides:

¹ Hereafter referred to as "UI automation project"

² TATA Consultancy Services, also known as TCS, was the NMDOL's primary contractor for its UI system re-engineering project.

April 2002

- Additional WIA Rapid Response funds were identified and were to be obligated prior to June 20, 2002, **or funds were to revert to USDOL.**
- NMDOL Administration instructed staff to pursue options to obligate funds and to justify obligations and expenditures as specified under UDDOL guidelines and statute for WIA rapid response. [Emphasis added.]

According to an internal NMDOL email:

May 22, 2002

[NMDOL official] confirmed the availability of the \$1.5M rapid response money as proposed on the allocated costs spreadsheet. Please coordinate with legal and [Financial Management Bureau] for the necessary actions on contract amendments and budget transfer.

To use WIA funds available for rapid response and to cover the deficit³ created by contract amendment eight with TATA Consultancy Services, NMDOL improperly:

- **transferred** \$748,657 of UI program costs -- initially paid from and charged to the UI program -- to the WIA Rapid Response program via journal voucher adjustments; and
- **charged** \$899,361 of UI automation project costs directly to the WIA Rapid Response program that were initially approved and coded for payment as UI automation project costs.

A. The NMDOL improperly transferred to the Rapid Response program \$748,657 in UI program personnel compensation and UI program costs.

The NMDOL reclassified \$748,657 of UI personnel compensation and other expenses as UI automation project costs and improperly transferred this amount to the WIA Rapid Response program via four journal voucher adjustments. The justification the agency gave for the transfer was that its UI division incurs costs for processing claims for Rapid Response participants.

In April 2002, the NMDOL's legal counsel recommended using the following procedures to justify financing UI costs with WIA Rapid Response funds:

³ The \$1,648,018 actually mischarged exceeded the \$1.51 million deficit created by amendment eight.

- Calculate the total number of UI claims processed.
- Calculate the number of UI claims processed for rapid response claimants.
- Arrive at a percentage of rapid response UI claims processed to total UI claims processed.
- Apply the percentage to all expenditures related to claims.

To justify charging UI costs to the WIA Rapid Response program, the NMDOL identified employers who had layoffs of more than 50 employees and determined the number of UI claimants from these layoffs during the period July 2001 to April 2002. Such claims were classified as “rapid response” claims.

This justification for charging UI costs to the WIA Rapid Response program is flawed since processing UI claims for Rapid Response participants is no different than the procedures used when handling all other claimants. Additionally, even if UI claims were processed during a Rapid Response event, allocating UI claims processing staff costs to the Rapid Response program would not meet the criteria for a Rapid Response activity. The principles in OMB Circular A-87 require consistent application of common costs based on the proportionate benefit to the program being charged, whereas costs for processing UI claims do not benefit the Rapid Response program.

The NMDOL used its flawed methodology to transfer to its WIA Rapid Response program some UI personnel compensation and other UI program costs. The NMDOL determined the rate of its defined “rapid response” claims to be 6.6 percent for the first two adjustments, 12.2 percent for the second adjustment, and 5.29 percent for the last adjustment. The journal voucher adjustments were as follows:

Transaction	Adjustment Date	Description	Allocation Rate	Amount Charged Against Rapid Response
JV-729	6/30/2002	Personal Services & Benefits / Software Lease / Maintenance	6.6%	345,320
JV-765	6/30/2002	UIC Software Maintenance/IVR Annual Maintenance / ES Central Processing Unit	6.6%	32,556
JV-695	11/30/2002	Transfer of UI Administration and Project expenditures	12.2%	271,596
JV-069	2/28/2003	UI Administrative and Project expenditures	5.29%	99,185
Total				\$748,657

The NMDOL transferred these UI costs to WIA Rapid Response based on the availability of funds for rapid response (see prior reference to May 22, 2002 email) notwithstanding staff concerns evidenced by the following NMDOL internal e-mails:

- June 11, 2002

If this issue of continued funding for the [UI] claims re-engineering project is not resolved, then this project's successful completion will be jeopardized. I would rather we take a hit on an audit [that] can be fixed later rather than to face the wrath of the USDOL, the State Legislature and the public when we implement a system that is partially completed and does not do what is intended. . . . We need a fix and soon!!

- February 15, 2003

... the rapid [response] allocation was intended **to offset the deficit** [in UI automation project] . . . I don't mean to be critical but this [UI automation] project is running over budget and needs to be controlled. [Emphasis added.]

- April 10, 2003

I have received information from the regional [ETA] office regarding your query on transferring PY00 expenses into Rapid Response. Basically, how are you going to document the time? You would need time sheets and affidavits from the individuals involved, otherwise **I believe the feds would consider it a shifting of expenditures for budget purposes, not a true expense.** . . . [Emphasis added.]

- April 11, 2003

We had come up with a method of utilizing the number of claims processed that were rapid response related. Based upon that number, the cost of processing initial claims is being prorated. . . .

- April 15, 2003

[We] had a conversation with [USDOL official] this morning regarding the UI transfer of charges to Rapid Response.

Are the charges from PY00 that you want to transfer staff charges? If so, [we] feel it is too late to do this – **it would leave us vulnerable in an audit situation.** [She] feels it would be viewed as a way for UI to charge their legitimate program activity to another program – Rapid Response. . . . [Emphasis added.]

WIA Final Rules, Title 20 Code of Federal Regulations (20 CFR), Subpart 665.300(a) defines the purpose of Rapid Response as,

...activities necessary to plan and deliver services to enable dislocated workers to transition to new employment as quickly as possible, following either a permanent closure or mass layoff, or a natural or other disaster resulting in a mass job dislocation.

The purpose of UI is to provide eligible claimants benefits that allow them to continue to acquire the necessities of life, such as food, shelter, and clothing. The objectives of the UI and Rapid Response programs are different; they each have separate funding sources, and the success of one program is not dependent upon the results of the other. Incurring costs related to UI claims is not necessary to fulfill the purpose of Rapid Response; consequently, funds reserved for Rapid Response should not be used for UI program activities.

Therefore, we question the reasonableness and necessity of charging \$748,657 of UI staff compensation and other UI expenses to Rapid Response.

B. The NMDOL improperly charged directly to the WIA Rapid Response program \$899,361 of UI automation project costs that were initially approved and coded for payment as UI automation project costs.

In addition to transferring UI expenses via journal vouchers, NMDOL directly charged⁴ \$899,361 of their UI automation project's costs to the WIA Rapid Response program. The following internal e-mail documents (also cited in finding 1A) show the NMDOL's intent to use WIA Rapid Response funds to relieve the UI automation project deficit regardless of the potential for future disallowance:

- June 11, 2002
If this issue of continued funding for the [UI] claims re-engineering project is not resolved, then this project's successful completion will be jeopardized. **I would rather we take a hit on an audit** [that] can be fixed later rather than to face the wrath of the USDOL, the State Legislature and the public when we implement a system that is partially completed and does not do what is intended. . . . We need a fix and soon!! [Emphasis added.]

- February 15, 2003
... the rapid [response] allocation was intended **to offset the deficit** [in UI automation project] . . . I don't mean to be critical but this [UI automation] project is running over budget and needs to be controlled. [Emphasis added.]

⁴ The NMDOL charged approximately 77 percent of one invoice, 73 percent of another invoice, and 100 percent of three invoices.

***The NMDOL Improperly Charged UI Program
Costs to Its WIA Rapid Response Program***

The NMDOL had conceived numerous methods for allocating the UI automation project costs to Rapid Response. However the method they decided to use involved the eighth amendment to TCS's contract, which increased the total project cost by \$1.51 million.

NMDOL decided that 6.6 percent⁵ of the total system cost should be borne by the Rapid Response program. As a result, NMDOL had planned to charge \$1,115,095 of amendment eight to Rapid Response. However, this did not happen since only \$899,361 was actually allocated to the program as follows:

Transaction	Invoice Date Payment Date	Description	Payment Amount	Allocation Rate	Amount Charged Against Rapid Response
FO-34417	10/04/2002 01/22/2003	Development of UI Claims Management System Video-based online training.	\$90,000	76.94%	\$69,246
FO-34519	09/04/2002 01/27/2003	Testing of various tasks / Transition to the New System Strategy / Maintenance plan.	528,580	73.4913%	388,460
FO-40522	01/28/2003 07/30/2003	Final Data Migration / Acceptance of System Documentation	142,405	100%	142,405
FO-40523	11/02/2002 07/30/2003	Performance, Stress, and all Non-Functional Testing	142,500	100%	142,500
FO-40764	03/28/2003 08/08/2003	Transition to the new system	156,750	100%	156,750
Total					\$899,361

We question the allowability of charging \$899,361 of UI automation projects costs to the WIA Rapid Response program for the following reasons:

- The UI automation project was not designed to benefit Rapid Response.
- Costs were allocated inconsistently to Rapid Response.

1) The UI automation project was not designed to benefit Rapid Response.

Although NMDOL's amendment eight to the UI automation project contract added a system component specifically designated for mass layoffs (when UI claimants would be eligible for rapid response activities), none of the documentation supports the functionality of this component as being beneficial for Rapid Response. It appears that the component was simply tagged as mass layoff by NMDOL to justify

⁵ This percentage is based on the NMDOL's definition and calculation of UI "rapid response" claimants.

their use of Rapid Response funds. An internal NMDOL memorandum that was prepared in the process of seeking approval for the amendment described the objective to enhance UI claims processing as:

Development of supplemental requirements, missing functionality, address process improvements and include computer based video training and online help. This work is required to: ensure that the UI Claims Processing System is functionally complete; includes integration of external/internal partners; provides for efficient operation of processes and staff; addresses recent legislative mandates such as Temporary Emergency Unemployment Compensation; and enhances the system for exports to other states.

However, documents used to support payments applied to the Rapid Response account described the components for the UI automation project as follows:

Development of UI Claims Management System Video-based online training; Testing of various tasks/Transition to the New System Strategy/Maintenance plan; Final Data Migration/Acceptance of System Documentation; Performance, Stress, and all Non-Functional Testing; Transition to the new system.

In addition, development plans provided by the NMDOL showed the Mass Layoff component's capability as being limited to tracking Rapid Response participants, which is no different than the system's capability to track all other UI claimants.

Based on the descriptions of the internal memorandum, supporting payment documents, and development plan, the Mass Layoff component provides no benefits to the Rapid Response program. None of the documents revealed any features in the new system that would enable NMDOL to monitor the performance of the Rapid Response program or carry out any other functions that would make the program more effective or efficient. Therefore, we concluded that even with this new system in place, NMDOL will continue to administer the program and incur its normal expense as it has in the past.

2) Although the UI automation project costs are not allowable charges to the NMDOL's WIA Rapid Response program, the NMDOL was not consistent in how it allocated such costs to WIA.

NMDOL used a variety of rates to charge their UI automation project costs to WIA Rapid Response. The agency's documentation shows its initial intent was to charge to WIA Rapid Response 73.85 percent (or \$1,115,095) of the \$1.51 million cost for the UI automation contract amendment eight. However, without any explanation, only \$899,361 was charged to Rapid Response. Two invoices were allocated

The NMDOL Improperly Charged UI Program Costs to Its WIA Rapid Response Program

among various programs including WIA Rapid Response; while three invoices were charged 100 percent to WIA Rapid Response (see chart below).

CONTRACT AMENDMENT EIGHT ALLOCATION					
	UI Reengineering	Rapid Response	Internet Grant	Reed Act	Total
Original Plan	\$139,905 9.27%	\$1,115,095 73.85%	\$10,000 .66%	\$245,000 16.23%	\$1,510,000 100%
Payment F034417	\$0 0%	\$69,246 76.94%	\$17,379 19.31%	\$3,375 3.75%	\$90,000 100%
Payment F034519	\$48,999 9.27%	\$388,460 73.49%	\$86,325 16.33%	\$4,796 .91%	\$528,580 100%
Payment F040522	\$0 0%	\$142,405 100%	\$0 0%	\$0 0%	\$142,405 100%
Payment F040523	\$0 0%	\$142,500 100%	\$0 0%	\$0 0%	\$142,500 100%
Payment F040764	\$0 0%	\$156,750 100%	\$0 0%	\$0 0%	\$156,750 100%
Total	\$48,999 4.62%	\$899,361 84.83%	\$103,704 9.78%	\$8,171 .77%	\$1,060,235 100%

Initially, these five invoices were approved and coded for payment as UI automation project costs. Before the invoices were paid, the payment coding was changed: two invoices' costs were allocated among various programs including WIA Rapid Response; three invoices' costs were charged 100 percent to WIA Rapid Response. These coding changes resulted in \$899,361 of UI automation project costs being shifted to the WIA Rapid Response program. Therefore, these costs are questionable WIA Rapid Response costs.

Even though the UI automation project costs are not considered allowable expenses for the Rapid Response program, the inconsistency of NMDOL's methodology for allocating costs among the various funding sources violated OMB Circular A-87, Attachment A, Paragraph C.1.e, that requires allowable costs to:

Be consistent with policies, regulations, and procedures that apply uniformly to both Federal awards and other activities of the governmental unit

In charging approximately \$1.65 million of UI program costs to its WIA Rapid Response program, the NMDOL violated the following provisions of Office of Management and Budget (OMB) Circular No. A-87, Attachment A.

A cost is allocable to a particular cost objective if the goods or services involved are chargeable or assignable to such cost

objective in accordance with relative benefits received.
(paragraph C.3.a)

Any cost allocable to a particular Federal award or cost objective under the principles provided for in this Circular may not be charged to other Federal awards to overcome fund deficiencies (paragraph C.3.c)

To be allowable under Federal awards, costs must be adequately documented. (paragraph C.1.j)

[To be allowable a costs must be] Necessary and reasonable for proper and efficient performance and administration of Federal awards. (paragraph C.1.a)

We question the allowability of \$1,648,018 of UI automation project costs (see Exhibit A) and other expenses charged to the WIA Rapid Response program because:

- The NMDOL used WIA Rapid Response funds to cover their UI automation program deficit.
- The WIA Rapid Response program received no benefit from the UI automation project.
- UI costs were not necessary and reasonable for the effective and efficient performance of the WIA Rapid Response program.

Recommendations

We recommend the Assistant Secretary for Employment and Training:

1. disallow and recover from the NMDOL, from non-Federal funds, the \$1,648,018 of WIA Rapid Response funds that were improperly used to help fund deficits in the NMDOL's UI automation project and to pay for UI staff compensation and other UI expenses; and
2. require the NMDOL to establish controls and procedures to ensure that costs incurred for one program are not shifted to other programs either through journal voucher adjustments or direct charges. Journal vouchers should be documented and properly approved.

NMDOL's Response

The response, submitted jointly by the New Mexico Office of Workforce Training and Development and the New Mexico Department of Labor, states that our recommendation for disallowance of \$1,648,018 is based on an invalid premise that pro-rata costs for unemployment insurance claims from WIA rapid response participants could not be charged to the WIA program under 20 CFR 665.310(a) of the WIA Regulations.

The State contends that “access to unemployment insurance” is a shared cost objective under 20 CFR 665.310(a)(5), and that, in accordance with the advice of NMDOL’s former legal counsel there was a valid basis for allocating unemployment insurance benefits system costs to WIA. The response also states that we did not interview State staff members who engaged in communications with USDOL Regional Office staff regarding the use of WIA Rapid Response funds as one of the funding sources for the UI automation project.

Further, the response states that our conclusion that Rapid Response funds were used to cover a deficit in the automation project is unsupported. According to the response, several million dollars of Reed Act funds were available for appropriation for the automation project; but Rapid Response funds were used because the State’s legal advisor and financial management staff thought it was a legal and proper source of funds.

The State further responded that the use of WIA Rapid Response as one of the funding sources for the UI automation project was discussed several times with ETA Regional Office staff, that Federal staff stated the cost allocation methodology was good, and that the draft report failed to acknowledge that State policy makers requested a federal review in July 2004 when presented with staff concerns about the automation project. Finally, the response indicates that, if the expenditures are not allowed, the State would use its available Reed Act appropriations to cover the questionable costs.

OIG Conclusion

We disagree with the State characterization of our premise for recommending disallowance of the WIA Rapid Response funds used for the UI automation project. WIA rules allow Rapid Response funds to be used for providing designated dislocated workers access to UI, but it is inappropriate to use WIA Rapid Response funds to supplement UI administration funding, such as the UI automation project, that is provided by a separate Federal appropriation.

Regarding the State’s assertion that the use of WIA Rapid Response funds for the UI automation project was discussed several times with ETA Regional Office staff,

we do not believe that such discussions relieve the State of Federal requirements regarding the allowability of WIA costs. Also, although we may not have interviewed all State employees who discussed the UI automation project with the ETA Regional Office, we spoke with a former State employee involved in conversations with ETA staff. The former employee said there was nothing in writing to substantiate the claim that ETA endorsed the State's methodology. Also, we spoke with the ETA representative and she denied the claim made by the State staff.

The State also contends that our conclusion that Rapid Response funds were used to cover a deficit in the UI automation project is unsupported. The State responded that funding required for the UI automation project was met partially with the use of WIA Rapid Response, and, according to the response, could have been met alternatively with use of State appropriated Reed Act funds.

In an internal e-mail dated February 15, 2003, State staff stated, ". . . Your current Reed Act budget by itself cannot cover this expenditure. I am working on the 4th Quarter Rapid Response allocation which can be used for this purpose . . ." The e-mail goes on to further say, "Spending this additional \$200,000 is based upon the bet that the department will be appropriated FY 04 Reed Act dollars for this purpose because the rapid [response] allocation was intended to offset the deficit."

We believe the documents cited in the finding referencing a concern about a potential funding deficit support our conclusions, which remain unchanged from our draft report. The State response has been fully considered. However, we reject the State's arguments and have retained the recommendation unchanged from the draft report. ETA will determine the amount of disallowance and debt collection procedures.



Elliot P. Lewis
April 8, 2005

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Exhibit

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SCHEDULE OF QUESTIONED COSTS Rapid Response Transactions

Transaction	General Ledger Date	Description	Payment Amount	Allocation Rate	QUESTIONED COSTS Charged Against WIA Rapid Response
FO-34417	01/22/2003	Development of UI Claims Management System Video-based online training.	\$90,000	76.94%	\$69,246
FO-34519	01/27/2003	Testing of various tasks / Transition to the New System Strategy / Maintenance plan.	528,580	73.4913%	388,460
FO-40522	07/30/2003	Final Data Migration / Acceptance of System Documentation	142,405	100%	142,405
FO-40523	07/30/2003	Performance, Stress, and all Non-Functional Testing	142,500	100%	142,500
FO-40764	08/08/2003	Transition to the new system	156,750	100%	156,750
JV-729	06/30/2002	Personal Services & Benefits / Software Lease / Maintenance		6.6% (Note 1)	345,320
JV-765	06/30/2002	UIC Software Maintenance/IVR Annual Maintenance / ES Central Processing Unit		6.6% (Note 1)	32,556
JV-695	11/30/2002	Transfer of UI Administration and Project expenditures		12.2% (Note 2)	271,596
JV-069	02/28/2003	UI Administrative and Project expenditures		5.29% (Note 3)	99,185
Total					\$1,648,018

Note 1	6.6% = 3,086 Rapid Response participants / 47,064 total unemployment population. For the period of July 2001 to April 2002 (10 months) <i>Calculation does not account for June 2002 statistics</i>
Note 2	12.2% = 2,090 Rapid Response participants / 17,101 total unemployment population. For the period of July 2002 to September 2002 (3 months) <i>Calculation does not account for June 2002 statistics</i>
Note 3	5.29% = 964 Rapid Response participants / 18,219 total unemployment population. For the period of October 2002 to December 2002 (3 months)

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Appendices

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BACKGROUND

The Employment and Training Administration (ETA) requested the Office of Inspector General (OIG) to determine if the New Mexico Department of Labor (NMDOL) improperly used WIA Rapid Response funds to help finance its UI Claims System Reengineering Project.

WIA Rapid Response Program

Each program year, ETA awards Workforce Investment Act (WIA) grants to each State that include funds to finance Rapid Response programs that are intended to provide:

. . . activities necessary to plan and deliver services to enable dislocated workers to transition to new employment as quickly as possible, following either a permanent closure or mass layoff, or a natural or other disaster resulting in a mass job dislocation.

States can use its DOL-funded Rapid Response program to take a proactive approach in minimizing the time dislocated workers are out of work.

UI Claims System Reengineering Project

The NMDOL's 30-year old UI claims system limited the functionality and efficiency of its unemployment insurance (UI) operations. Consequently, the USDOL, ETA awarded the NMDOL a UI infrastructure grant of \$7,184,253 to reengineer the agency's UI claims system.

As the UI automation project progressed, the NMDOL implemented several changes that increased the total project cost to an estimated \$14.5 million⁶ (as of March 2004) and delayed the project completion date from December 31, 2001, to May 15, 2004.

The NMDOL had a budget deficit for the UI automation project and used WIA Rapid Response funds to fund the deficit. The methodology the NMDOL used to justify allocating UI costs to the Rapid Response program was based on a legal opinion from the agency's legal counsel. The legal counsel recommended the following:

⁶ Per Agreed Upon Procedures Report Issued by Henderson, Black and Company, Certified Public Accountants and Management Consultants, August 5, 2004.

- For expenditures directly related or beneficial to the program, allocate 100 percent of costs to the program.
- For expenditures related to or benefiting numerous programs, allocate costs among the programs. (This opinion does not address any specific allocation calculation or formula.)
- For all expenditures related to UI claims, allocate costs to Rapid Response based on the percentage of Rapid Response claims processed.

NMDOL used the third method to allocate its UI claims system reengineering costs to the WIA Rapid Response program.

The OIG conducted a performance audit to determine if NMDOL improperly charged UI benefits system reengineering costs to its WIA Rapid Response program.

OBJECTIVE, SCOPE, METHODOLOGY, AND CRITERIA

Objective

Our audit objective was to determine if NMDOL improperly charged UI benefits systems reengineering costs to its WIA Rapid Response program

Scope

We examined the UI claims system costs charged to the WIA funded Rapid Response program during the period July 1, 2001, through January 2005, the month when we conducted our examination on-site at NMDOL's central offices in Albuquerque, New Mexico. While we planned to use an ending cut-off period of June 30, 2004, for the costs to be examined; the latest NMDOL compilation of costs for the UI claims system occurred in February 2004. We also performed additional analytical procedures through April 8, 2005.

We did not use sampling. Our audit was limited to an allegation that WIA Rapid Response funds had been improperly used to help fund a UI system re-engineering project. The individual accounting transactions and related evidence for UI claims system costs that were charged to Rapid Response were examined.

We did not necessarily determine the full extent of UI or other costs improperly allocated to Rapid Response because NMDOL failed to implement needed controls in their accounting system to segregate costs for the UI claims system re-engineering project and to maintain the integrity of its cost accounting process.

Methodology

We examined the NMDOL process for allocating UI systems reengineering costs, UI staff compensation and other UI program costs to the WIA Rapid Response program. Specifically, we:

- Interviewed ETA staff.
- Reviewed NMDOL's legal opinion.
- Reviewed ETA's response to our questions regarding applicable criteria.
- Interviewed NMDOL staff.
- Reviewed development plans for new UI system Rapid Response component.
- Analyzed charges to Rapid Response for UI systems costs.
- Reviewed ETA's report on their review of NMDOL's UI reengineering project.
- Reviewed an Agreed Upon Procedures report regarding the UI claims system reengineering project, prepared by Henderson, Black and Company, Certified Public Accountants and Management Consultants, August 5, 2004.

- Reviewed OIG's 1999 audit working papers related to Audit of New Mexico Balance of State JTPA program.
- Reviewed NMDOL's last financial statement audit (single audit) which contained a qualified opinion on the ETA-funded WIA grant program.

We did not assess or rely on NMDOL's system of internal controls for allocating its costs to USDOL funded programs in defining the scope of our audit or determining the extent of our examination. Rather, we conducted substantive tests of the UI costs that allegedly had been misapplied to the WIA Rapid Response program. Therefore, we do not provide any assurance over NMDOL's system of internal controls.

We conducted our performance audit in accordance with Generally Accepted Government Auditing Standards.

Criteria

We used the following criteria to perform this audit:

- Workforce Investment Act of 1998
- Final WIA Rules dated August 11, 2000, published in 20 CFR, Subpart(s) 665.300, 665.310, 665.320, 667.200
- OMB Circular A-87, Federal Cost Principles for State and Local Grantees

ACRONYMS AND ABBREVIATIONS

ETA	Employment And Training Administration
NMDOL	New Mexico Department of Labor
OIG	Office of Inspector General
RRA	Rapid Response Activity
TCS	TATA Consultancy Services
TRA	Trade Readjustment Act
UI	Unemployment Insurance
USDOL	United States Department of Labor
WIA	Workforce Investment Act

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Appendix D

Agency Response to Draft Report

BILL RICHARDSON
GOVERNOR



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DEPUTY SECRETARY

CONROY CHINO
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MARLIN MACKEY
DEPUTY SECRETARY

September 19, 2005

Mr. John F. Riggs
Regional Inspector General for Audit
United States Department of Labor - OIG
Dallas/Denver Regional Office
525 Griffin Street, Room 415
Dallas, Texas 75202

Dear Mr. Riggs:

This is the State of New Mexico's response to the August 18, 2005 discussion draft of Audit Report No. 06-05-03-390. The draft audit concludes that New Mexico improperly used Workforce Investment Act grant-in-aid funds to help finance its Unemployment Insurance (UI) claims system re-engineering project.

This response is submitted jointly by the New Mexico Office of Workforce Training and Development and the New Mexico Department of Labor. On January 22, 2004 the New Mexico Office of Workforce Training and Development was designated by the Governor as the State agency responsible for administration of Workforce Investment Act (WIA) funds. This designation includes responsibility for repayment of any disallowed WIA costs. We have already furnished a copy of the Governor's Executive Order to the auditors. The New Mexico Department of Labor was the designated State WIA grant administrator at the time the questioned costs were incurred. The discussion draft is in error in stating that the New Mexico Department of Labor is liable for repayment of disallowed WIA funds. We agree that the recommended administrative finding regarding the financial controls applies to the New Mexico Department of Labor.

In your discussion draft you recommend the disallowance and recovery, from non-Federal funds, of \$1,648,018 of WIA funds. This recommendation is based on a premise that pro-rata costs for unemployment insurance claims from WIA rapid response participants could not be charged to the WIA program under 20 CFR 665.310(a) of the WIA Regulations.

New Mexico respectfully disagrees: A WIA Rapid Response event is a jointly conducted activity involving multiple funding sources which combine their efforts and deliver integrated program services for the benefit of dislocated workers. These services include "information and access to unemployment insurance" for the workers being laid off. "Access to unemployment insurance" is a shared cost objective that may properly be allocated to WIA Rapid Response funds.

This interpretation of the law, although different from the interpretation of WIA relied upon by the auditors, is a reasonable reading of 20 CFR 665.310(a)(5) and it is the interpretation of law provided to

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the State's decision-makers by their former legal counsel. The State's policy makers acted in good faith when they relied upon the written opinion of legal counsel as the basis for allocating unemployment insurance benefits system costs to WIA. In point of fact, the cost methodology used to allocate these costs was specifically recommended by legal counsel.

The State's utilization of WIA Rapid Response funds for the UI automation project was discussed several times with the United States Department of Labor ETA Regional Office staff. The Federal/State Team Review of the New Mexico Department of Labor Fiscal Year 1999 Infrastructure Grant and Telephonic Claims Grants, a joint report prepared by the State and the USDOL Regional Office staff, specifically identifies Rapid Response as one of three funding sources for the automation project. Additionally, the State Labor Department financial staff spoke with our WIA federal liaison about the specific cost allocation methodology for allocation of pro-rata costs to Rapid Response and was told by the federal representative "the methodology is good." The State staff members who engaged in these communications with the USDOL Regional Office staff were never interviewed by the auditors.

There is an unsupported conclusion in the draft report that Rapid Response funds were used to cover a deficit in the automation project. This conclusion about the motivation of the State's policy makers is not based on fact. The auditors never verified available fund balances nor did they interview the staff who made the decision to use Rapid Response funds. The State had several million dollars of Reed Act funds available for appropriation for the automation project. Rapid Response funds were used because the State's legal advisor and financial management staff thought this was a legal and proper use of these funds.

The discussion draft finds that the UI automation project does not benefit the Rapid Response program. This finding is not consistent with 20 CFR 665.300(a) and 20 CFR 665.310(a)(5) which specifically recognize that provision of unemployment insurance benefits to Rapid Response participants is a legitimate Rapid Response activity. Accordingly, costs for provision of unemployment insurance are therefore "necessary and reasonable for the program and efficient performance and administration" of the WIA program.

The draft audit fails to acknowledge that State policy makers requested a federal review when presented with staff concerns about the automation project. When these concerns were presented in July 2004, the Office of Workforce Training and Development and the State Department of Labor jointly requested the USDOL Regional Office to conduct an on-site review and to provide guidance.

In our review of the discussion draft, we find some important facts regarding the allocation of WIA Rapid Response funds were omitted or misstated. We request that you add the following findings:

1. Effective January 22, 2004 New Mexico Office of Workforce Training and Development became the State agency responsible for administration of WIA funds and it is the agency responsible for resolution of any disallowed costs as a result of this audit.
2. New Mexico's decision to allocate WIA Rapid Response funds for pro-rata costs of unemployment insurance claims for Rapid Response participants was based upon advice of legal counsel. The methodology used to allocate these costs was specifically recommended by legal counsel and was specifically discussed with USDOL Regional office staff.
3. On July 16, 2004 the Director of the New Mexico Office of Workforce Training and Development and the Cabinet Secretary of the New Mexico Department of Labor notified the United States Department of Labor ETA Regional Office about concerns regarding the allocation of WIA funds

for the UI automation project and requested the Regional Office to conduct an on-site review and provide guidance to the State administrators.

We request that you correct multiple misstatements in the audit report regarding your conclusion that Rapid Response funds were used to "cover a deficit" in the agency's claims system re-engineering project. There was no budget deficit. Fund balances were available. Furthermore, the State had more than thirty million dollars in Reed Act funds available for appropriation.


The State was always open and forthcoming about the decision to use Rapid Response funds. If there was a problem with the propriety of this decision, the federal officials with whom we dealt never alerted our responsible decision makers. Now we are faced with this serious problem which might have been avoided if we had been notified that the legal opinion upon which the State relied was not in accord with the federal interpretation.


We believe our interpretation of the Workforce Investment Act is valid and that the Rapid Response expenditures should be allowed. Nevertheless, if the arguments we have provided do not resolve the issues, we want to correct this problem. According to the draft audit report, all of the questionable costs for the project should have been borne by the Unemployment Insurance program. Our solution is to make appropriate accounting adjustments to charge the questionable costs to New Mexico's available Reed Act appropriations, funds which may be properly used for unemployment insurance administration expenses.

If permitted, we would like another opportunity to personally present our arguments to the auditors.

Finally, we want you to know we appreciate the work of your auditors, Ms. Mary Stepney and Mr. Orval Harden. Although we do disagree with some aspects of the audit, we consider them to be very professional.

Sincerely,


Reese Fullerton, Director
Office of the Workforce
Development Center


Conroy Chino, Cabinet Secretary
Department of Labor

xc: Joseph Juarez