

<b>EMPLOYMENT AND TRAINING ADMINISTRATION</b> <b>ADVISORY SYSTEM</b> <b>U.S. DEPARTMENT OF LABOR</b> <b>Washington, D.C. 20210</b>	<b>CLASSIFICATION</b> Unemployment Insurance
	<b>CORRESPONDENCE SYMBOL</b> OUI/DUIO
	<b>DATE</b> September 29, 2023

**ADVISORY: UNEMPLOYMENT INSURANCE PROGRAM LETTER NO. 16-23**

**TO:** STATE WORKFORCE AGENCIES

**FROM:** BRENT PARTON /s/  
Principal Deputy Assistant Secretary

**SUBJECT:** Issuance of Revised Appendix E of the Employment and Training (ET) Handbook No. 407

1. **Purpose.** To notify states that Appendix E of ET Handbook No. 407, 4<sup>th</sup> Edition, Tax Performance System (TPS), regarding state employer Unemployment Insurance (UI) audit functions (formerly “field audit functions”) and procedures, has been revised.

2. **Action Requested.** Administrators are requested to distribute this advisory and the attachment to appropriate UI tax managers, employer audit staff, and TPS reviewers. There will be two different effective dates for the revisions to Appendix E: October 1, 2023, or January 1, 2024 (explanations of each effective date are below).

3. **Summary and Background.**

- a. Summary – This Unemployment Insurance Program Letter (UIPL) announces a revision to Appendix E of ET Handbook No. 407, 4<sup>th</sup> Edition, TPS, which concerns state employer UI tax audits of employers. State employer audit tax staff audit the records of selected employers to ensure that the employers have complied with state UI laws and regulations. Appendix E applies to employer audits of contributory employers<sup>1</sup> conducted by state auditors. The revised Appendix E Employer Audits can be found here: [https://www.dol.gov/sites/dolgov/files/ETA/handbooks/2023/Handbook\\_407/ETA\\_Appendix-E\\_Employer\\_Tax\\_Audits\\_\(Accessible\\_PDF\).pdf](https://www.dol.gov/sites/dolgov/files/ETA/handbooks/2023/Handbook_407/ETA_Appendix-E_Employer_Tax_Audits_(Accessible_PDF).pdf).

Appendix E was last updated in 1999. The U.S. Department of Labor (Department) Employment and Training Administration (ETA) has revised Appendix E because states have asked for clarification of prior guidance and changes since 1999 in the audit program, such as implementation of the Effective Audit Measure (EAM) and the ability for states to conduct audits remotely. The revised Appendix E replaces Appendix E in

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<sup>1</sup> Contributory employers pay contributions into a state unemployment fund based on contribution rates the state had assigned to each employer.

<b>RESCISSIONS</b> Appendix E-Field Audit	<b>EXPIRATION DATE</b> Continuing
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ET Handbook 407, 4<sup>th</sup> Edition, TPS, and discontinues the Employment Security Manual (ESM) Part V, Section 3670-3693.<sup>2</sup>

- b. Background – State employer audits are required under the Federal UI Performs Management System, which the Department developed to meet its responsibilities under Title 20 C.F.R. Part 602. This regulation requires the Department to assess the timeliness and accuracy of administration of state UI programs. In accordance with UIPL No. 03-11, state audit activity is a core measure in the UI Performs Management System. A comprehensive employer audit program is vital to the administration of a state UI system. A well-planned and cost-effective employer audit program, executed with other state UI administrative functions, is an efficient means of ensuring compliance with state UI law and timely collection of taxes on an equitable basis. Completed audits that meet the guidelines set forth in Appendix E are reported on the ETA 581 Contribution Operations report, and they are included in the universe of employer audits that may be subject to review by TPS acceptance sampling.

#### 4. Guidance.

- a. **Summary of Major Revisions.** A summary of major revisions to Appendix E of ET Handbook 407, TPS, is below. The revised Appendix E Employer Audits can be found here: [https://www.dol.gov/sites/dolgov/files/ETA/handbooks/2023/Handbook\\_407/ETA\\_Appendix-E\\_Employer\\_Tax\\_Audits\\_\(Accessible\\_PDF\).pdf](https://www.dol.gov/sites/dolgov/files/ETA/handbooks/2023/Handbook_407/ETA_Appendix-E_Employer_Tax_Audits_(Accessible_PDF).pdf).
  - i. Changes “Field Audits” to “Employer Audits” to align more closely with current employer audit practices, which may include both in-person field audits and remote audits.
  - ii. Revises the definition of what constitutes a completed employer audit. Prior guidance listed seven minimum requirements for a completed audit. These seven requirements remain unchanged. Two requirements have been singled out to further clarify these already-existing requirements.
    - A. The revised definition requires that an audited employer paid wages in covered employment in at least one audited quarter, in accordance with prior guidance that an auditor verifies the taxable amounts of payments made by an employer to employees and contributions paid for covered employment. If an auditor investigated an employer and found that the employer did not pay wages to employees in covered employment during the scope of the audit, this activity is not considered an employer audit. For example, an audit did not occur if the auditor found that the employer reported all wages to the state as covered employment erroneously.
    - B. The revised definition of a completed audit includes that an auditor verified the existence of a business. This addition is consistent with prior

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<sup>2</sup> ESM, Part V, Section 3670-3693, addressed state employer UI tax audit functions and procedures and was included in Appendix E of ET Handbook No. 407, 4<sup>th</sup> Edition.

guidance that an auditor must include information that the existence of a business was verified in the audit report.

- iii. Includes a detailed description of an auditor's tests to verify the accuracy and completeness of an employer's payroll posting system and reported total and taxable wages. These tests remain unchanged from prior guidance, as described in Chapter 7 of ET Handbook No. 407. The tests must be completed as a requirement for an audit to be counted as a completed audit. Since Appendix E is the primary source of guidance on state audit programs, a description of the tests has been added to Appendix E for the convenience of Federal and state staff.
- iv. Provides a new definition for calendar quarters audited. The term is defined in revised Appendix E since states report the number of calendar quarters audited on the ETA 581 report and the term is not clearly defined in current guidance. The new definition will provide consistency for reporting data on the ETA 581 report.
- v. Provides updates for employer selection criteria for audits and includes two policy changes. These changes provide more flexibility for states to select employers for audit with the goal to pass all factors of the EAM rather than meet specific measures. For information on the EAM, see Section 17 in this revised Appendix and UIPLs No. 30-10 and 03-11.
  - A. Prior guidance that at least 10% of audit assignments must be randomly selected from the total universe of contributory employers has been changed from a requirement to a recommendation.
  - B. The requirement that at least 1% of total audits required to meet the audit DLA (now factor 1 of the Effective Audit Measure (EAM)) must be large employers has been removed.
- vi. Revises the definitions for what constitutes the scope of employer audits. Prior guidance stated that the scope of an audit is the number of quarters examined without defining "examined." To clarify what is meant by "examined," the revised Appendix established new terms "original quarters" (normally four) and "extended quarters" because each term deserves separate guidance.

For example, the revised Appendix E reaffirms the difference between auditing original quarters and extended quarters. Whereas, an auditor is required to verify the accuracy of the employer's payroll posting system for the original quarters, the auditor may omit verifying the accuracy of the employer's payroll posting system during the period the audit is extended to cover. However, the auditor must still verify the employer's total and taxable wages that were reported to the state for the extended quarters. In addition, the revised Appendix reaffirms that the auditor must search for unreported employees in all quarters that the audit was extended to cover.

- vii. Eliminates the current provision that within the context of an audit report, auditors should collect additional taxes at the time of the audit, and the mention in the audit report if taxes due were collected or explain why taxes were not collected.

The revised Appendix recommends an auditor's manager or designated staff to review each audit report to ensure that the report summarizes adjustments to an employer's total wages, taxable wages and/or contributions due that may be required because of the auditor's final determination. A manager should check that adjustments were processed in the state's automated system.

The state should follow its normal procedures to bill and collect amounts due.

- viii. Recommends that states establish timeliness standards for the completion of audits and audit reports. Since many audits result in adjustments that either bill employers for additional taxes due or provide credits for overpaid taxes, it is important to complete audits and prepare audit reports as soon as possible. For example, a state may establish a policy that an audit should be completed within 90 calendar days from the start of the audit (i.e., when the auditor has a pre-audit discussion with the employer) and an audit report should be completed within 30 days after the closeout conference. (Note: Each state has the flexibility to establish its own policy for timely completion of audits and audit reports in accordance with its UI law and/or regulations.)
- ix. Addresses the use of remote audits (or e-audits), which are audits conducted remotely versus in-person.
- x. Adds information on the EAM to the guidance. The prior version of the Appendix did not include information about the EAM since the EAM was established after the most recent update to the Appendix. The new information about the EAM in the revised Appendix is only a summary and a cross reference to information on the EAM as provided in UIPLs No. 30-10 and 03-11.
- xi. Clarifies when states should report audit activity on the ETA 581 Contributions Operations Report and when to include the audits in TPS acceptance sampling if the audits involve other states. Prior guidance did not address three specific situations described below.

- A. If, while conducting an audit, an auditor finds workers and wages covered in another state, the auditor documents the correct payroll for the auditor's state. The audit and other adjustments to the wages reported to the auditor's state are counted in the state's ETA 581 Contribution Operations report and included in the state's TPS universe of employer audits. Information regarding wages covered in another state is shared with the other state based on the auditing state's procedures on initiating out-of-state contact.

- B. A state that receives data and information from an audit that another state completed on its behalf, is not counted in the state's ETA 581 Contribution Operations Report and is not included in the state's TPS acceptance sampling universe of employer audits.
  - C. A joint audit, where auditors from more than one state perform an audit together, are counted in a state's ETA 581 Contribution Operations report and included in a state's TPS universe of employer audits if employees and wages are covered in the state.
- xii. Reminds states that tax auditors must be merit-staffed governmental employees and not contractors if the auditors have the responsibility for making determinations of monetary liability or coverage decisions based on their findings. The basic UI audit function, as well as certain program audit functions may be outsourced to the extent they do not involve the exercise of discretion in applying governmental authority, but rather, involve only the investigation and verification of past actions taken by governmental or contract employees. The outsourcing of employer audit activities to contractors is limited to investigations that only gather data and facts that will be transmitted to a merit-staffed employee who will make any determination after reviewing the information. See UIPL No.12-01, Change 2 for more information.<sup>3</sup>
  - xiii. Encourages states to participate in the Questionable Employment Tax Program (QETP) with the IRS. See UIPL No. 17-07 and Training and Employment Notice No. 03-21 for more information,
- b. **Effective Dates.** ET Handbook No. 407 provides two different timeframes for conducting employer audit TPS reviews. State TPS reviewers conduct acceptance sampling of completed employer audits to determine if the audits were completed in accordance with the Handbook. The effective date of the revision announced in this UIPL will differ, depending on the timeframe used for TPS audit reviews.

The Handbook allows state TPS reviewers to conduct acceptance sampling of audits completed in the fourth quarter of the previous calendar year, and the first, second, and third quarters of the current calendar year. Under this first option, a state reviewer can begin to review cases in October of the current calendar year. This option of beginning the review in October instead of January may lessen the workload burden of reviewing acceptance sampling for other tax functions and the audit function at the same time in January.

The Handbook provides a second option whereby a state reviewer would conduct acceptance sampling of audits completed in the four quarters of the calendar year

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<sup>3</sup> Unemployment Insurance Program Letter No, 12-01, Change 2, States' Ability to Exercise Flexibility in Staffing Models for the Performance of Certain Unemployment Compensation (UC) Administrative Activities, Issued January 8, 2021

under review. Under this option, a state reviewer begins to review sample cases in January of the next year.

- The revision to Appendix E is effective October 1, 2023, for states choosing to conduct TPS employer audit reviews that examine audits completed in the fourth quarter of the previous calendar year, and the first, second, and third quarters of the calendar year under review (i.e., for calendar year 2024, this would be the fourth quarter of 2023 and first three quarters of 2024).
- The revision to Appendix E is effective January 1, 2024, for states choosing to conduct TPS employer audit reviews that examine audits completed in the four quarters of the calendar year under review (i.e., for calendar year 2024, all four quarters of 2024).

5. **Inquiries.** Please contact your ETA Regional Office for inquiries.

6. **References.**

- Title 20 C.F.R. Part 602, <https://www.ecfr.gov/current/title-20/chapter-V/part-602>;
- UIPL No. 03-11, *Implementation of the Effective Audit Measure*, issued December 30, 2010, <https://www.dol.gov/agencies/eta/advisories/unemployment-insurance-program-letter-no-03-11>;
- UIPL No. 30-10, *Proposed Effective Audit Measure for State Unemployment Insurance (UI) Employer Audit Programs*, issued September 2, 2010, <https://www.dol.gov/agencies/eta/advisories/unemployment-insurance-program-letter-no-30-10>;
- UIPL No. 13-10, *Tax Performance System Handbook Updates*, issued February 16, 2010, <https://www.dol.gov/agencies/eta/advisories/unemployment-insurance-program-letter-no-13-10>;
- UIPL No. 29-10, *Tax Performance System Handbook Updates, ET HANDBOOK NO. 407, 4th EDITION, CHANGE 5*, issued August 4, 2010, <https://www.dol.gov/agencies/eta/advisories/unemployment-insurance-program-letter-no-29-10>;
- UIPL 17-07, *Initiative to Address Questionable Employment Tax Practices*, issued April 10, 2007, <https://www.dol.gov/agencies/eta/advisories/unemployment-insurance-program-letter-no-17-07>;
- UIPL No. 12-01, *Outsourcing of Unemployment Compensation Administrative Functions* issued December 28, 2000, <https://www.dol.gov/agencies/eta/advisories/unemployment-insurance-program-letter-no-12-01>;
- UIPL No. 12-01, Change 1, *Outsourcing of Unemployment Compensation Administrative Functions – Claims Taking*, issued November 26, 2007, <https://www.dol.gov/agencies/eta/advisories/unemployment-insurance-program-letter-no-12-01-change-1>;
- UIPL No. 12-01, Change 2, *States' Ability to Exercise Flexibility in Staffing Models for the Performance of Certain Unemployment Compensation (UC) Administrative Activities*, issued January 28, 2021,

<https://www.dol.gov/agencies/eta/advisories/unemployment-insurance-program-letter-no-12-01-change-2>;

- ET Handbook No. 407, 4<sup>th</sup> Edition, Issued November 20, 2003, [https://www.dol.gov/sites/dolgov/files/ETA/handbooks/2010/ETA\\_Handbook407c4.pdf](https://www.dol.gov/sites/dolgov/files/ETA/handbooks/2010/ETA_Handbook407c4.pdf);
- ET Handbook No. 407, 4<sup>th</sup> Edition, *Tax Performance System Handbook Updates*, issued December 9, 2004, [https://oui.doleta.gov/dmstree/handbooks/407/hb\\_407\\_4thc1.htm](https://oui.doleta.gov/dmstree/handbooks/407/hb_407_4thc1.htm);
- ET Handbook No. 407, 4<sup>th</sup> Edition, Change 2, issued July 31, 2006, <https://www.dol.gov/agencies/eta/advisories/handbooks/et-handbook-no-407-4th-edition-change-2>;
- ET Handbook No. 407, 4<sup>th</sup> Edition, Change 3, issued December 11, 2007, <https://www.dol.gov/agencies/eta/advisories/handbooks/et-handbook-no-407-4th-edition-change-3>;
- TEN No. 03-21 *Questionable Employment Tax Practices (QETP) Program*, issued August 20, 2021, [https://www.dol.gov/sites/dolgov/files/ETA/advisories/TEN/2021/TEN\\_03-21.pdf](https://www.dol.gov/sites/dolgov/files/ETA/advisories/TEN/2021/TEN_03-21.pdf); and

7. **Attachment.** None.