



**New Jersey State Legislature
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Office of the State Auditor**

**Department of the Treasury
Division of Revenue and
Enterprise Services - Operations**

July 1, 2013 to February 29, 2016

**Stephen M. Eells
State Auditor**

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Enclosed is our report on the audit of the Department of the Treasury, Division of Revenue and Enterprise Services - Operations for the period of July 1, 2013 to February 29, 2016. If you would like a personal briefing, please call me at (609) 847-3470.

A handwritten signature in black ink, appearing to read "Stephen M. Eells".

Stephen M. Eells
State Auditor
May 11, 2016

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Scope

We have completed an audit of the Department of the Treasury, Division of Revenue and Enterprise Services (DORES) – Operations, which is comprised of the following three branches: Registry and Collection Services, Front End Processing Services and Records Management, and Contracting Compliance and Quality Assurance, for the period July 1, 2013 to February 29, 2016. We did not audit the Commercial Information Services Bureau within the Registry and Collection Services branch as it was included in our previous audit dated December 30, 2014. Our audit included financial activities accounted for in the state’s General Fund and the Property Tax Relief Fund.

The primary responsibility of the Registry and Collection Services branch is to maximize the collection of delinquent non-tax state debts and to administer the state’s cigarette license and tax stamp distribution programs. The primary responsibility of the Front End Processing Services and Records Management branch is to ensure accurate and timely deposit of payments; capture data for all state agencies and clients utilizing enterprise processing services; assist state and local agencies with their records inventories; and provide centralized storage and retrieval of records for state and local agencies. The primary responsibility of the Contracting Compliance and Quality Assurance branch is to increase the quality of processed documents by establishing and testing internal processes as well as those of outside contracted vendors to ensure the integrity and compliance with agreed-to standards.

Objectives

The objectives of our audit were to determine whether financial transactions were related to the branches’ programs, were reasonable, and were recorded properly in the accounting systems. We also tested compliance with contract terms for contracts related to DORES – Operations. An additional objective was to determine the adequacy of select application-level general controls over the division’s Revenue Delinquent Invoice (RDI) system, including security management, logical access, change management, and contingency planning.

This audit was conducted pursuant to the State Auditor’s responsibilities as set forth in Article VII, Section I, Paragraph 6 of the State Constitution and Title 52 of the New Jersey Statutes.

Methodology

Our audit was conducted in accordance with *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

In preparation for our testing, we studied legislation, the administrative code, circular letters promulgated by the Department of the Treasury, and policies of the branches. Provisions we considered significant were documented and compliance with those requirements was verified

by interview, observation, and through our testing of financial transactions. We also reviewed financial trends and interviewed division personnel to obtain an understanding of the programs and internal controls.

A non-statistical sampling approach was used. Our samples of financial transactions were designed to provide conclusions about the validity of transactions, as well as internal controls and compliance attributes. Sample populations were sorted and transactions were judgmentally selected for testing.

Conclusions

We found the financial transactions were related to the branches' programs, were reasonable, and were recorded properly in the accounting systems. We also found DORES - Operations and the vendors were in compliance with the terms of the contracts. In addition, the general controls over RDI were adequate except for logical access. In making these determinations, we noted an opportunity to improve dishonored check collection procedures and made an observation concerning the structure of future collection contracts.

Dishonored Check Collection

Dishonored check collection procedures could be improved with a standardized form and a written policy.

The Registry and Collection Services branch is responsible for recording dishonored checks for the state. It is also responsible for the collection of those checks, with the exception of checks issued to the Division of Taxation and the Motor Vehicle Commission. There were over 16,500 dishonored checks totaling \$23.7 million at June 30, 2015 that had been reported by state agencies on various forms of electronic files. The branch does not have a standardized form for agencies to report dishonored checks. A standardized electronic file would ease the organization and collection of dishonored checks as the branch must now convert files that contain inconsistent columns of information into a useful form. In addition, the branch has no written policy on the collection effort. We attempted to determine at what point the branch sends collection notices to the issuers of dishonored checks by testing all of the 1,237 dishonored checks the branch was responsible to collect at the time of our test. Our analysis disclosed 244 cases where a notice was sent within 30 days, 90 cases where a notice was sent after 30 days, and 37 cases where no evidence of a notice was sent. We could not determine when notices were sent for the remaining 866 cases, partially because of the inconsistent electronic files used by agencies.

Recommendation

We recommend the branch develop a standard electronic reporting form and a written policy on collection efforts for dishonored checks. A standardized form would simplify the reporting of dishonored checks as well as make collection efforts easier.

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Unauthorized System Access

Unauthorized system access could be prevented by implementing a password policy and procedures.

The Revenue Delinquent Invoice (RDI) system, which manages outstanding debt owed to the State of New Jersey, lacks sufficient controls to prevent or detect unauthorized system access. Authorized RDI users with read-only access could authenticate themselves through the mainframe and then access RDI through another's privileged account by using the standard password assignment. The risk is further compounded by the number of privileged accounts and the lack of system change logs. Once in the system, any changes made, including altering an account balance, would be visible only until the next change was made to that account.

The inability of the mainframe system (ACF2) and RDI security to communicate with each other, combined with the lack of password controls and standard password assignment for the

RDI system, allows an unauthorized user to gain greater access than what was intended by using the credentials of a privileged user. User access to the RDI system relies on ACF2 security for authentication of users to the mainframe, and then on RDI's internal security to control authorization to system functionality. Each user must log in at the ACF2 level with a user name and password, and at the RDI level with the same user name but a different password. However, the two systems do not pass any authentication information between them; the two logins are completely unique. This means that once users authenticate themselves to the mainframe through ACF2, they may use a completely different set of credentials to access RDI.

The RDI system's internal security has insufficient automated password controls. When an account is created, the password is automatically generated and is set to match the user's logon ID. There is no requirement to change the password at initial login, and passwords do not expire. The DORES does not have a documented and enforced password policy for the RDI system. The State of New Jersey IT Circular 14-32-S1-NJOIT states that "Passwords shall be changed on a regular rotational basis ... at least every ninety (90) days", and that "Privileged user accounts such as IT administrators or data owners with administrative access should have their password changed at least every sixty (60) days." In addition, the RDI system only records the last action made on an account, so a knowledgeable user could make unauthorized changes in succession, and only the final change would be recorded.

At the time of our review, there were 211 users throughout the state with logon access to the RDI system, including 17 privileged users with the capability of making data and access changes. A review of the 17 privileged users revealed that 13 still had their original password, 2 had changed their passwords, and 2 were removed by management as described below. Management immediately had the 13 privileged users change their passwords after we brought it to their attention. Our review also indicated that 26 of the 211 users are no longer employed by the state. Two of these users were privileged users, with one from DORES and one from the Office of Information Technology. Management promptly removed the access from these two users after it was brought to their attention but prior to us determining if the original password had been changed. The remaining 24 were from various other agencies. Although ACF2 access was removed for all but one of these users, the inability of ACF2 and RDI to communicate as described earlier makes this an ineffective control to prevent unauthorized access to the RDI system.

Recommendation

We recommend the DORES submit a change request to OIT to have the RDI system automatically require the users to change their password to be in compliance with the OIT standard or access will be denied. The DORES should also continue to review all users and remove RDI-level access for those users no longer requiring such access.

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Observation

Collection Contract

The collection contract should be restructured.

The Registry and Collection Services branch manages the collection of non-tax debt as recorded in the division's Revenue Delinquent Invoice (RDI) System and collected through various avenues including the Financial Asset Management Systems (FAMS) contract. The branch receives notification from other departments and agencies of non-tax debt that is over 90 days delinquent which requires further assistance for collection. The contracted vendor attempts to collect on this debt for a commission. The branch recorded total collections of \$12.7 million in fiscal year 2014 and \$11.7 million in fiscal year 2015 and paid FAMS \$477,312 in fiscal year 2014 and \$445,634 in fiscal year 2015 for their collection efforts.

The original Request for Proposal (RFP) provided a price schedule with seven commission levels that change at every \$2 million in collections, but there was no specific instruction for which direction the commission percentage should be scaled. Although both the prior contract and the current second referral collection contract pay an increased commission as collections increase, the FAMS contract is structured in a manner in which the commission rates decrease as total collections increase.

Structuring the commission schedule in a decreasing manner could encourage the vendor to target easier types of debt because there is more commission to be earned up front. It is stated in the RFP that the vendor bears all costs related to collections. It is difficult to determine to what extent the vendor attempts to collect more difficult types of debt when the commission rate is lower as more debt is collected.

With future contracts, the DORES should consider structuring the RFP so that the commission schedule for debt collections increases as more debt is collected. The direct relationship between debt collected and commission paid could motivate the vendor to attempt to collect more debt before the end of the contract year as the commission resets at the beginning of the year.

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May 3, 2016

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Dear Mr. Pica,

On the behalf of Acting State Treasurer Scudder, I would like to thank you for providing us with the opportunity to respond to your audit report on the Division's Registry and Collection Services. The professionalism of your staff throughout the audit was noteworthy. I believe that the effort has yielded constructive information that we can use to improve our programs.

Our response is attached, with each section corresponding to your findings and the observation found on pages 3-5 of your report. Please feel free to contact me if you have any questions.

Very truly yours,

James F. Fruscione
Director

- c. Ford M. Scudder, Acting State Treasurer
Peter Lowicki, Deputy Director, Operations
Robert Benco, Assistant Director, Registry and Collection Services

Dishonored Check Collection

While DORES has no statutory authority to compel other State agencies to adopt a standardized electronic file format for reporting dishonored checks, we concur that use of such a format would be beneficial. Accordingly, we have developed a format and will encourage agencies to begin using it within the next month.

We also concur that it is appropriate to document our long-standing procedures for processing dishonored checks, and accordingly, have written and filed the procedures for on-going use by staff.

Unauthorized System Access

We agree with the finding regarding the security of our non-tax system. While the analysis did not find any evidence of a breach or unauthorized access in this area, we recognized that remedial steps were in order. Accordingly, we reset all RDI internal passwords for privileged users. In addition, we are developing a policy for RDI internal passwords that will bring us into compliance with IT Circular 14-32-S1-NJOIT. Finally, we are in the process of enhancing the RDI system to automatically require periodic password changes and to maintain a record of account changes.

Collection Contract Observation

We agree that the current First Referral Non-Tax Debt Collection Services contract with Financial Asset Management Systems (FAMS) includes a pricing structure that does not incentivize collections to the maximum extent possible. We had previously corrected the structure to ensure our Second Referral Non-Tax Debt Collection Services contract (awarded in 2015) provides better incentives for performance, and will implement the same approach during the next procurement cycle for the First Tier contract.