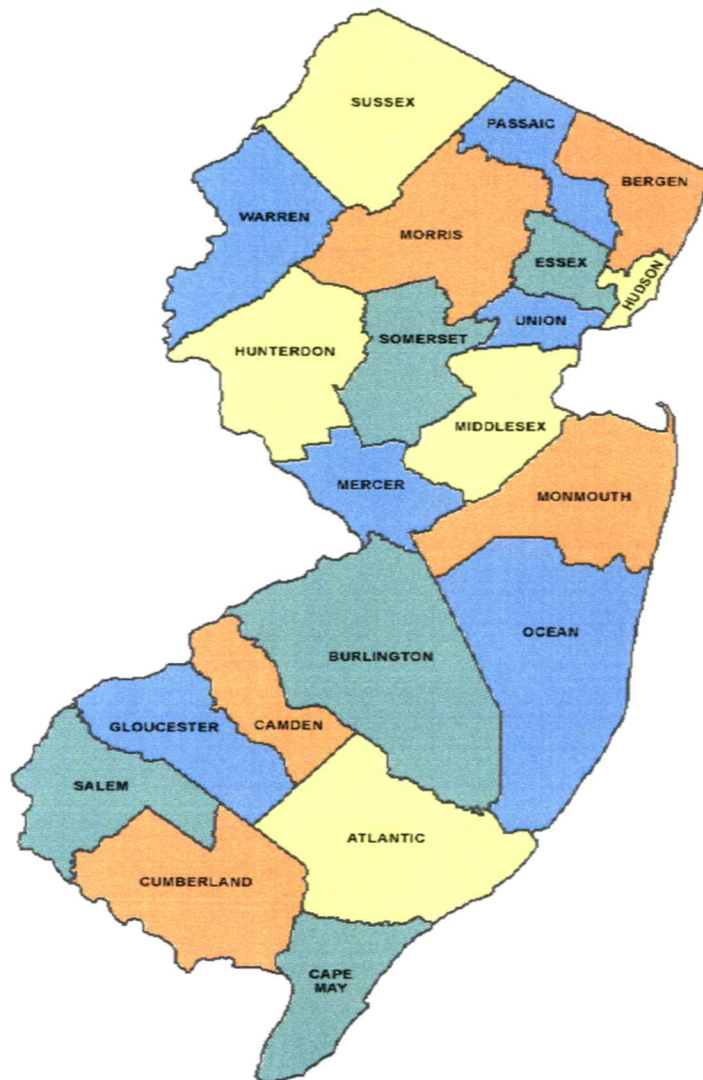

Annual Report of the New Jersey Office of Legislative Services Office of the State Auditor

For the Calendar Year Ended December 31,



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Richard L. Fair
State Auditor

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New Jersey State Legislature

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The Honorable Members of the Senate and General Assembly

Mr. Albert Porroni, Executive Director
Office of Legislative Services

I am pleased to present to you the *Annual Report of the New Jersey Office of Legislative Services, Office of the State Auditor* for calendar year 2006. In conformance with our responsibilities to perform financial and compliance audits, all state agencies are audited periodically. During 2006, we issued 35 reports which identified \$218.7 million in potential cost savings/revenue enhancements. In addition, the state continues to save substantial dollars as a result of the resolution of issues previously reported by the Office of the State Auditor. If you or members of your staff would like additional information or a personal briefing, please contact me.

Our mission is to improve the accountability for public funds and to improve the operations of state government. We serve the public interest by providing members of the Legislature and other policymakers with unbiased accurate information and objective recommendations on how to best use public resources. In addition to fulfilling our audit mission, we have focused on maximizing the quality of our services and maintaining communication with the Legislature and the agencies that we audit. We are committed to providing high quality audit reports. You may be assured that we will continue our efforts to improve state government accountability to the Legislature through an effective and constructive audit process.

Richard L. Fair
State Auditor
March 1, 2007

TABLE OF CONTENTS

Introduction

Background	1
Mission Statement.....	2
Vision Statement	2
Accomplishments.....	2
Schedule of Cost Savings and Revenue Enhancements	3

Audit Reports

Types of Audits Performed	4
Distribution of Audit Hours.....	5
How and to Whom Audit Reports Are Issued	6

Organization

Human Resources	7
Audit Staff.....	7
Quality Assurance	7
Administrative Staff.....	8
Staff Roster	9

Accomplishments and Results

Summary	11
New Jersey Schools Construction Corporation	12
Department of Labor and Workforce Development	
Unemployment Insurance Services.....	18
Department of Environmental Protection	
Site Remediation and Waste Management Funds	20
New Jersey Transportation Trust Fund Authority	
Appropriations and Department of Transportation	
Contract Administration.....	21
Department of Human Services	
Division of Developmental Disabilities	
Woodbridge Developmental Center	22
Department of Education	
Administration	23
Department of the Treasury	
Division of the State Lottery.....	25
Department of Corrections	
Life Skills Academy	26
Department of Education	
Marie H. Katzenbach School for the Deaf.....	27
Department of Law and Public Safety,	
Juvenile Justice Commission	
New Jersey Training School for Boys	29

TABLE OF CONTENTS

Department of the Treasury	
Division of Property Management and Construction	30
Motor Vehicle Commission	
Central Office.....	31
Information Technology Management	33
New Brunswick School District.....	34
New Jersey Commerce, Economic Growth and Tourism Commission	
Urban Enterprise Zone Program	36
<i>Schedule of Reports Issued During 2006</i>	38

INTRODUCTION

BACKGROUND

The Office of the State Auditor, which is in the legislative branch of government, was originally established in 1934 pursuant to P.L. 1933, c.295. A number of statutory amendments dealing with the powers and duties of the State Auditor have been enacted in the ensuing years. The Office of the State Auditor is within the Office of Legislative Services under the provisions of the Legislative Services Act.

The State Auditor is a constitutional officer, appointed by the Legislature for a term of five years and until his successor shall be appointed and qualified. On September 26, 1989, Mr. Richard L. Fair, CPA, was appointed State Auditor Designate and was confirmed by a joint session of the Legislature on March 15, 1990.

The organization of the office within the legislative branch permits the State Auditor to be independent of the executive and judicial branches of government. This independence is critical in terms of meeting professional standards and in providing fair and objective reviews and audits of governmental operations.

Under the provisions of Article VII, Section 1, Paragraph 6 of the State Constitution and N.J.S.A. 52:24-1 et seq., the Office of the State Auditor is required to conduct post-audits of all transactions and accounts kept by or for all departments, offices, and agencies of state government. Reports are submitted to the Legislature, the Governor, and the Executive Director of the Office of Legislative Services.

The Public Laws of 2006, Chapter 82 authorized the State Auditor to conduct a performance review of any program of any accounting agency, any independent authority, or any public entity or grantee that receives state funds. The law also requires the State Auditor to conduct a post-audit review to determine compliance with the State Auditor's recommendations.

The State Auditor shall personally or by any of his authorized assistants or by contract with independent public accounting firms, examine and post-audit all accounts, reports, and statements and make independent verification of all assets, liabilities, revenues, and expenditures of the state, its departments, institutions, boards, commissions, officers, and any and all other state agencies now in existence or subsequently created.

In addition, at the request of the Legislature or the Legislative Services Commission, the State Auditor conducts studies on the operation of state and state-supported agencies with respect to their economy, internal management control, and compliance with applicable laws and regulations.

INTRODUCTION

MISSION STATEMENT

The State Auditor provides independent, unbiased, timely, and relevant information to the Legislature, agency management, and the citizens of New Jersey which can be used to improve the operations and accountability of public entities.

VISION STATEMENT

The State Auditor and his staff will approach all work in an independent, unbiased, and open-minded manner.

The State Auditor will provide timely reporting to the Legislature, agency management, and the citizens of New Jersey.

Reporting will be in clear and concise language so it is understood by all users of the report.

Reporting will include recommendations on how to improve the workings of government and how to strengthen agency internal controls.

The State Auditor and his staff will perform all work in a professional manner utilizing appropriate standards.

ACCOMPLISHMENTS

During calendar year 2006 we identified \$218.7 million in new cost savings or revenue enhancements. The schedule of cost savings is presented on page 3. In addition, we found that auditees resolved 57 percent of the significant issues noted in our prior reports.

OFFICE OF LEGISLATIVE SERVICES
OFFICE OF THE STATE AUDITOR
SCHEDULE OF COST SAVINGS AND
REVENUE ENHANCEMENTS
REPORTS ISSUED DURING 2006

REPORT

**COST SAVINGS/
REVENUE ENHANCEMENTS**
(In Thousands)

Department of Corrections	
Mid-State Correctional Facility	\$5
Department of Education	
Administration	1,507
Marie H. Katzenbach School for the Deaf	92
Department of Environmental Protection	
Site Remediation and Waste Management Funds	10,000
Department of Health and Senior Services	
Division of Aging and Community Services	4
Department of Human Services	
Division of Developmental Disabilities	
New Lisbon Developmental Center	37
Woodbridge Developmental Center	2,917
Department of Labor and Workforce Development	
Unemployment Insurance Services	20,067
Department of Law and Public Safety	
Juvenile Justice Commission	
New Jersey Training School for Boys	40
Department of the Treasury	
Division of the State Lottery	900
New Brunswick School District	45
New Jersey Commerce, Economic Growth, and Tourism Commission	
Urban Enterprise Zone Program	123
New Jersey Schools Construction Corporation	181,000
New Jersey Transportation Trust Fund Authority Appropriations and Department of Transportation Contract Administration	2,000
<i>Total Cost Savings and Revenue Enhancements</i>	<u><u>\$218,737</u></u>

AUDIT REPORTS

TYPES OF AUDITS PERFORMED

Financial Audits

Financial audits are designed to provide reasonable assurance about whether the financial statements of an audited entity are fairly presented in conformity with generally accepted accounting principles. The primary annual financial audit conducted by the office is the opinion on the state's Comprehensive Annual Financial Report (CAFR) which is published by the Department of the Treasury. The CAFR engagement includes the audit of 200 funds and component units which had a total asset value of \$168 billion at June 30, 2006 based on full accrual accounting. Two other financial audits were issued in calendar year 2006.

Audits of Agencies

The objectives of this type of audit are to determine whether financial transactions are related to an agency's programs, are reasonable, and are recorded properly in the accounting systems. Where appropriate, these engagements may also provide economy and efficiency comments. Audits are selected using a risk-based approach. Larger departments are audited on a divisional, agency, or program basis rather than department-wide because of their size and complexity. We performed 28 of these audits in calendar year 2006. These audits encompassed \$12.9 billion and \$4.2 billion of expenditures and revenues, respectively.

Information Technology Audits

The objectives of this type of audit are to determine whether the financial data relating to a particular computer system are reliable, valid, safeguarded, and recorded properly. During calendar year 2006, we reported on the College of New Jersey, Information Technology; Motor Vehicle Commission, Information Technology Management; and the Department of Labor and Workforce Development, Tax Revenue Systems.

School District Audits

N.J.S.A. 18A:7F-6d authorizes the Office of the State Auditor to audit the accounts and financial transactions of any school district in which the state aid equals 80 percent or more of its net budget for the year. We audited the New Brunswick School District in calendar year 2006. This audit encompassed \$244.4 million of expenditures.

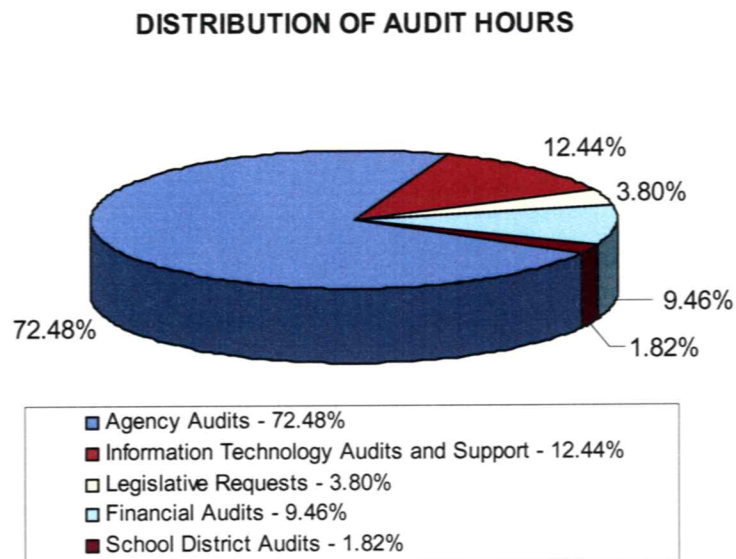
Legislative Requests

From time to time the Legislative Services Commission requested the State Auditor to conduct special projects of the fiscal practices and procedures of the major departments and agencies of the State, and to report his findings to the Commission.

AUDIT REPORTS

DISTRIBUTION OF AUDIT HOURS

The distribution of audit hours used in performing audits during calendar year 2006 is depicted on the following chart.



AUDIT REPORTS

HOW AND TO WHOM AUDIT REPORTS ARE ISSUED

The findings and recommendations in our reports are developed as results of independent objective audits and are intended to provide accountability to the legislature and recommendations for improvement of government operations. All reports issued are discussed with agency officials prior to finalizing the report. Modifications to the draft report are made if warranted. Agency comments to the final report are incorporated in the document. All issued reports of the Office of the State Auditor are public documents and since 1996 are available on the Internet through the New Jersey Legislature's Home Page. Reports are statutorily required to be sent to:

- the Governor,
- the President of the Senate,
- the Speaker of the General Assembly, and
- the Executive Director of the Office of Legislative Services.

In addition, copies of reports are routinely sent to:

- the chairs of the pertinent Senate and the General Assembly committees,
- the Executive Directors of partisan staff,
- the management of the audited entity,
- the State Treasurer, and
- the State Library.

Finally, reports are placed on the Internet at:

<http://www.njleg.state.nj.us/legislativepub/auditreports.asp>

ORGANIZATION

HUMAN RESOURCES

The Office of the State Auditor is one of eight units within the Office of Legislative Services. The State Auditor's office is comprised of 88 professionals and five support staff. All auditors must have a bachelor's degree in accounting or a related field and a minimum of 24 credit hours in accounting. Fifty-two staff members, 59 percent of the professional staff, possess professional certifications or advanced degrees.

The office provides a minimum of 40 continuing professional education credits annually and diversified work experience to enhance each individual's professional development. The audit staff attends professional development programs encompassing a myriad of accounting and auditing topics. In addition, staff members actively participated as officers, board members, and committee members of local, state, and national accounting and auditing organizations, including the Association of Government Accountants, Institute of Internal Auditors, National State Auditors Association, and New York/New Jersey Intergovernmental Audit Forum. The office also participates in the national peer review program under the auspices of the National State Auditors Association.

AUDIT STAFF

The audit staff is the primary operating group in the office. They plan, conduct, and control the audit engagements and prepare and edit the reports. The audit teams report the results of their work to the auditee on an ongoing basis, and at the conclusion of the engagement by means of a written report. In an effort to develop expertise, field managers are assigned specific departments. This practice enhances the quality and efficiency of our audits and ensures all programs are audited within a reasonable cycle. Information technology support is also provided by the field staff.

The office maintains eight active committees staffed by individuals in various titles to provide guidance in the areas of administration, IT communication, information technology, personnel, planning, policy, sampling, and training. An intranet site is also maintained that contains staff information, budget and appropriation information, and commonly used accounting and auditing research and reference internet sites which the audit staff can access through their computers.

QUALITY ASSURANCE

The quality assurance staff is responsible for technical compliance and quality control, oversight of staff training, and research of technical issues. Quality assurance is achieved

ORGANIZATION

through reviews of working papers and reports to ensure adherence to professional standards. The quality assurance staff, through its research of accounting and auditing issues, also responds to surveys, questionnaires, and exposure drafts relating to proposed accounting and auditing standards.

ADMINISTRATIVE STAFF

The administrative staff processes, files, and distributes all reports. This group is responsible for maintenance of the audit working papers and the office library, purchasing and maintaining office supplies, and other general administrative functions.

**OFFICE OF THE STATE AUDITOR
STAFF ROSTER
As of December 31, 2006**

STATE AUDITOR

Richard L. Fair, CPA, CGFM
Evelyn T. Richardson, Administrative Assistant

ASSISTANT STATE AUDITOR

Stephen M. Eells, CPA
Jean Horner, Secretary

ASSISTANT STATE AUDITOR

Thomas R. Meseroll, CPA, CGFM
Deborah S. Tucker, Secretary

AUDIT MANAGERS

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Timothy D. Bush, CPA
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William Kowalski, CISA
Kenneth Kramli, CPA
Linda Maher, CGFM
J. Robert Malone, MBA
Donna Mooney
Stacey O'Brien, MBA, CPA

Charles Paslawsky
William D. Robinson, CPA
Donna M. Shemansky
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Thomas Troutman, CPA, CIA, CGFM
Edward J. Tyson
Robert D. Wills, CFE
John C. Wouters, CISA

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Edward A. Backer, CPA
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Hal Bauman
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Ngoc Cao
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Sean Duffy
Thomas M. Fenerty
Louis A. Finney, CFE

Robert F. Gatti, CPA
Richard Grahovac, CFE, CGFM
Grant Hopkins
Vishal Jhaveri
Petagay Johnson
Joshua Keller, CMFO
Kristin Kenney
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Carrie L. Meyer-Still, CPA
Nadia Negro
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Michael A. Tantom, MBA
Kevin Titus
Stephanie Titus
Jon Trauger
Shrushti Trivedi
Patrick Whalin
Peter Wozniak, CPA
Kurt Zadworney

ADMINISTRATIVE STAFF

Anthony Arena, Support Services Assistant

Robyn Boyer, Support Services Assistant

**ACCOMPLISHMENTS
AND RESULTS**

ACCOMPLISHMENTS AND RESULTS

SUMMARY

This section highlights seven of the more significant audits issued during the past year which individually contained cost savings/revenue enhancements greater than \$500,000 and collectively totaled \$218.4 million. Information on these reports is presented on pages 12 through 25. The office issued seven other reports with individual cost savings totaling \$346,000. This section also contains the significant findings from eight audits on pages 26 through 37 which address areas of noncompliance with laws or regulations, weaknesses in internal controls, and comments on economy and efficiency to improve operations.

All reports issued in calendar year 2006 are identified on a schedule on pages 38 to 39 and are available for review on our internet website.

NEW JERSEY SCHOOLS CONSTRUCTION CORPORATION

Strategic Plan and Comprehensive Budget

When the New Jersey Economic Development Authority (EDA) and the Department of Education (DOE) were assigned the task of implementing the requirements of the Educational Facilities Construction and Financing Act, an overall strategic plan was not formulated to determine how to best spend the \$6 billion in the Abbott districts. When the New Jersey Schools Construction Corporation (Corporation) was created the priority was to get projects started and moving quickly. The Corporation continued the practice of advancing projects on a first-come, first-serve basis. Aside from the previously existing health and safety projects, no statewide priority was placed on which projects to advance and in what order. When the DOE authorized the Corporation to proceed with a project, an in-depth analysis was not performed prior to the project moving forward to determine where the project might fit into a master plan.

In addition, a comprehensive budget and project cost system was not developed, which would permit budget versus actual cost comparisons. The system should identify all cost components associated with the project. Furthermore, the system should be updated timely to reflect known increases in cost. Project budgets should be approved by the board and funds encumbered. This is currently not occurring. However, the board did approve some components of a project as it moved forward, such as land acquisition, design contracts, and construction contracts. Periodic status reports on all ongoing projects should also be prepared and presented to the board. The lack of such a system made it inherently difficult for the Corporation to control individual project costs, and prevented the board from properly monitoring the impact of all project costs, in their totality, on the financial position of the Corporation.

The current project control system is unable to record and track requests for change orders as they become known. The process can take months depending on the approval requirements. In the interim, there is no record of the change orders with their added costs, other than possibly in the project officer's files. This may result in an unrecorded obligation or liability and hamper the fiscal monitoring of the project.

These conditions resulted in the Corporation committing to projects that could not be completed within the current funding level. The Corporation's estimate of cost to complete the 134 current projects had been understated by at least \$380 million. In addition, 100 projects have been halted due to a lack of funding with \$144 million having already been expended.

Fastrack Methodology

In 2003, the Corporation instituted a Fastrack Approach for its construction projects. The Fastrack methodology initiated the design phase of a construction project simultaneously with the site development/land acquisition phase and subsequently commenced the

construction bidding sequence prior to the completion of the permit and construction document phases. The overlapping of these various activities was designed to reduce the overall duration of a project by 20 months. Although the Fastrack Approach may have its theoretical benefits, its implementation on the Corporation's projects was not successful because there were too many uncontrollable variables associated with the initial phases of the project which resulted in additional costs to the project. Problems encountered in the site development or acquisition phases, or changes to the facility plan at times resulted in the need for design changes, and thus, additional design costs. In addition, design consultants (architects) were allowed to proceed through contractual milestones, such as schematic designs, without the required DOE review and approval. This contributed to design change orders totaling more than \$67 million, which represented a 16 percent increase to original contract amounts.

For some projects construction costs were also affected since contracts were awarded prior to bid and construction documents being completed and approved. It has been estimated by the Corporation staff that correcting errors and omissions in bid documents and construction contracts were increasing project costs by five percent. We reviewed the reasonableness of this estimate by testing five projects totaling \$55 million that were more than 70 percent complete and found that due to errors and omissions costs increased by eight percent on these projects. Although management halted this practice in mid 2005, over \$1.3 billion in construction contracts had been awarded under the Fastrack Approach. If these five to eight percent rates of increase are valid for all contracts, projects costs will be \$65 to \$105 million higher.

Another repercussion of Fastrack was the increased magnitude of the number of unfinished projects that entered the design phase and had to be suspended when it was discovered that funding to complete the projects was not available. Approximately 100 projects with design contracts totaling \$191 million were suspended at various stages of design with approximately \$90 million in costs having been incurred to date. If the design contracts are suspended for more than 90 days, the Corporation will have to further compensate the design consultants for costs incurred because of the suspension. If the contracts need to be terminated, it may be necessary to reprocur the project designs, and the Corporation may have to pay for all of these completed services again.

Land Acquisition

As of October 2005, the Corporation acquired, by agreement or condemnation, 359 properties at a total cost of \$225 million. The acquisition process takes much longer than the Corporation's timeline which was up to nine months. According to the Corporation's Land Acquisition division, it generally takes 9 to 12 months to complete the predevelopment phase, and an additional 6 to 12 months to acquire the property. Our testing indicated that it takes at least this amount of time for each phase.

NEW JERSEY SCHOOLS CONSTRUCTION CORPORATION

Before attempting to acquire a property, the Corporation must complete a Land Acquisition 20 Point Checklist to obtain approval from the DOE. In order to complete many of the checklist requirements, the Corporation must rely on other entities such as local planning boards, the Department of Environmental Protection, and local or county water or sewage agencies. The Corporation does not have control over the time it takes these other entities or agencies to perform their work.

The Corporation also engages in negotiations that exceed the requirements of the Eminent Domain Act of 1971. This act requires that an offer be no less than the appraised amount, and rejection or failure to accept the offer within the period specified is proof that negotiations have failed and condemnation proceedings can begin. Since the Corporation uses offers/counteroffers which prolongs negotiations, the value of the property is allowed to appreciate in value, at times substantially. These factors contributed to the amount spent for these properties being \$31 million or 16 percent above the original appraised value.

We further noted that the estimated cost of remediation is deducted from the settlement or condemnation award amount. However, for reasons often outside the Corporation's control, these estimates are often based on very limited information. Consequently, the actual costs often greatly exceed the initial estimates. For the 25 school sites which have, or are expected to have, the highest remediation costs, this amount is expected to exceed the estimates by \$32 million. Even though the Corporation has recourse in recovering these additional remediation costs after the fact or requesting that the court hold any award amount in escrow, it has not used these methods.

Project Management Firm Costs

When EDA was assigned the responsibility for the school construction program it lacked the professional staffing to adequately control the program. In December 2001 there were only 50 EDA school construction employees with 13 of them assigned directly to the design and construction of Abbott school projects. Considering the enormity and urgency of the pending school projects, it was determined that the use of project management firms (PMF) was a necessity. These firms managed all of the functions necessary for the advancement and completion of all construction projects. Their responsibilities included managing tasks related to site feasibility and acquisition, design, demolition, and construction management services. They were initially directed to complete \$650 million in health and safety projects at 400 schools in the Abbott districts. Subsequently, over 250 construction projects with initial Construction Cost Estimates (CCE) of \$4 billion were awarded to PMFs to manage.

Our review noted that the average PMF fee of 11 percent of initial CCE seems high when compared to the average three percent Construction Manager (CM) rate paid by non-Abbott school districts. PMF services, however, are more comprehensive than CM services. PMFs also manage the pre-design and design phases, in addition to the services performed by a CM. However, when factoring in the three and one-half percent rate used

NEW JERSEY SCHOOLS CONSTRUCTION CORPORATION

for Design Only projects the total rate should be between six and seven percent. We have identified the following factors which contributed to the current PMF rate.

The procurement of PMF services followed procedures for professional service contracts which do not require awarding the contact to the lowest price qualified bidder. However, we found that fees were not considered in the competitive portion of the procurement process. Qualified vendors were ranked by EDA based on the PMFs' technical proposals and interviews. It was not until after these rankings were determined that the fee proposals were opened. Although the process allowed for the negotiation of the fees, we found the results of these negotiations to be ineffective in controlling costs. The negotiated savings were primarily the result of reducing the scope of work not the rate. Any savings were negated when the PMFs were awarded change orders for additional hours of work.

Although PMFs are paid on lump sum fixed fee contracts, the fees are based on budgeted hours and hourly rates of PMF personnel. Our analysis of PMF hourly rates indicated that direct salaries were marked up by 94 to 192 percent for the cost of employee benefits, indirect costs, and profit. Although salaries paid by PMFs and the Corporation are comparable, the \$182 million staffing costs for the 14 PMF contracts reviewed exceeded the comparable costs of the Corporation's staff (including benefits) by \$59 million or 48 percent. Although there were 276 Corporation employees, of which 88 were assigned to the Design and Construction division as of November 2005, they continue to assign all projects to PMFs rather than manage them in-house.

As of January 2006 PMFs have been contracted to perform \$540 million in professional services and have been paid \$283 million of that amount. There have been 24 contracts with 12 different PMFs. To limit the size of PMF contracts, in addition to a three-year duration restriction, a maximum construction cost cap was established. However, in order to continue to award projects to PMFs who were approaching their cap, additional assignments were designated as Design Only projects. It was interpreted that since the scope of work of Design Only projects stopped after the design stage, they did not violate the construction cost estimate cap. Three PMFs were awarded \$23 million in fees to manage such Design Only projects.

We further noted that the review criteria used by the project officers for determining the accuracy of the PMF invoices were not always adequate or consistently applied. As a result, invoice payments were made prior to the completion of services or were not justified by the contractual terms. The following are examples of advance payments.

A PMF was paid \$1.9 million, or 89 percent of a project's construction phase fee, even though the construction phase was only 62 percent complete per the construction contractor's billing. This indicates an advance payment of \$580,000.

NEW JERSEY SCHOOLS CONSTRUCTION CORPORATION

For two other projects the PMF was paid \$2.1 million, or about 40 percent of their construction phase fees, even though the primary construction contracts for these two projects have not yet been awarded.

In each of these examples, the erroneous billings were a product of predetermined project payment schedules rather than the actual status of the project. When the project was delayed, the billings were not properly adjusted, and so the services for which payment was sought may not have been completed and should not have been paid.

Project Management Firms - Change Order Fees

As of January 2006, 343 change orders totaling \$296 million were awarded to PMFs. Change orders were used in all instances when the PMF fee was adjusted. Many change orders, such as assigning additional school projects to the PMF, were appropriate under the contractual terms. Others, however, were the result of inconsistent application or interpretation of the original contract terms by the PMF and the Corporation's Design and Construction staff who recommended and authorized the fee increase. This can be partially attributed to a lack of written guidance on the eligibility of the various PMF change orders. In addition, no formal training has been given to the project officers on this subject. Furthermore, there has not been an adequate process to independently review PMF change orders outside of the Design and Construction division.

We reviewed the contract and change order activity of ten PMF contracts which contained 181 change orders totaling \$185 million. Sixty change orders totaling \$45 million were the result of contract term and scope interpretations which were questionable. We further noted that such interpretations varied depending on the regional office, PMF, or the Corporation's project officer involved.

We found that 27 change orders totaling \$15 million erroneously cited an additional assignment or an increase in scope of work as the cause for additional fees. These change orders cited additional construction cost estimate (CCE) for such things as land purchases, demolition costs, and upgrades in parking facilities even though they either have nothing to do with the CCE, such as land purchases, or they were already included in the original CCE, such as demolition and parking facility costs. The use of the PMF fee schedule was unwarranted in these cases. If it was determined that services rendered by the PMF were outside of the original scope of the project, the contract allows for amendments for additional services beyond those provided for in the lump sum fee. These additional services should be compensated in accordance with the PMF's table of hourly rates by title and supported by detailed documentation of the time spent by PMF staff. There was no such supporting documentation for any of these questionable change orders. However, even though the contract does not allow for additional services to be added to the CCE of an already assigned school facilities project, this method of determining compensation for additional work was the most expedient.

NEW JERSEY SCHOOLS CONSTRUCTION CORPORATION

In addition, three change orders requested by one PMF totaling \$5.7 million cited delays in the project beyond their control. Additional compensation is allowable, but only for those costs the PMF actually incurred as a direct result of such delays. Our review found the supporting documentation for the added compensation was not in compliance with the contract because the determination of the amount was based on budgeted hours rather than actual hours or costs incurred. In addition, the approval of these change orders is questionable because most regional directors deny this type of change order request since the PMFs should be in complete control of the project and their staff scheduling.

In another example, a PMF in the final year of a three-year contract, through the change order process, received an additional one and one-half percentage points to the CCE rate on all past and future additional assignments. This added \$3.4 million in PMF fees for the additional assignments. The justification for this change was that the originally contracted CCE rate did not include funding for other direct costs incurred by the PMF, such as a regional office and equipment leases. There was not adequate documentation to support this increase. Furthermore, this change order, which actually modified the terms of the contract, was not presented to the board for approval.

Additionally, change orders were also approved increasing the CCE values of four previously assigned projects to new square footage rates, even though the contract stipulates that the CCE value at the time of the award was to be used in determining the PMF fee. The resulting fee increase for these projects totaled \$725,000. This was not the regular practice and resulted in unnecessary additional costs.

**DEPARTMENT OF LABOR AND WORKFORCE DEVELOPMENT
UNEMPLOYMENT INSURANCE SERVICES**

Base Weeks Reporting Errors

New Jersey's unemployment insurance (UI) benefits are calculated using a formula based on a claimant's earnings divided by the number of weeks they worked during the qualifying period (base weeks). The Department of Labor and Workforce Development (department) relies on information regarding wages and the number of base weeks as reported by employers on their quarterly Employer Report of Wages Paid (WR-30). These forms are processed by the Department of the Treasury, Division of Revenue and an electronic file is sent to the department where it is uploaded to the systems used to process UI claims.

The WR-30 forms often contain incorrect information regarding base weeks, and as a result inaccurate benefit payments occur. One type of error occurs when employers report that their employees worked 12 weeks during a quarter when they actually worked 13 weeks. This commonly occurs in quarters that have six biweekly pay periods. We also found some employers reporting wages correctly, but entering zero base weeks on the WR-30. This results in overpayments when claims are processed because the denominator of the UI formula is understated.

The department detects some overpayments and underpayments during its federally mandated testing of claims. These results are reported to the U.S. Department of Labor on the Benefit Accuracy Measurement (BAM) report. This document details the types of errors occurring and whether the department, the employer, or the claimant is responsible. For calendar year 2005, the department reported an overpayment rate of 12.6 percent. Approximately 19 percent of these overpayments resulted from base weeks errors made by employers. The BAM report also shows an underpayment rate of 1.7 percent with 76 percent resulting from employer base weeks errors. If these statistically valid error rates are applied to total claims, we estimate base weeks errors caused the department to make overpayments of \$44 million and underpayments of \$24 million during 2005. Although the department pursues collection of all overpayments it detects, we were unable to determine how much of this related to base weeks errors.

Additional Benefits while in Training

N.J.S.A. 43:21-3 entitles claimants to collect total benefits of no more than 26 times their weekly benefit rate. This amount can be increased by an additional 26 times if claimants enroll in a qualified training program approved by the department. Once these additional benefits while in training (ABT) are exhausted, claimants must reestablish eligibility by working at least 20 weeks or by earning more than 12 times the statewide average weekly remuneration (wages) paid to employees.

**DEPARTMENT OF LABOR AND WORKFORCE DEVELOPMENT
UNEMPLOYMENT INSURANCE SERVICES**

We noted overpayments totaling \$67,000 to four claimants enrolled in these training programs. Payments were made after new claims were processed even though the claimants had not reestablished eligibility. The processors did not recognize the claimants had not reestablished eligibility since the system does not contain adequate edits to alert them to these types of claims. The billing and collection of overpayments places an additional administrative burden on the department.

**DEPARTMENT OF ENVIRONMENTAL PROTECTION
SITE REMEDIATION AND WASTE MANAGEMENT FUNDS**

Oversight Cost Recovery

The Department of Environmental Protection (DEP) utilizes an automated system entitled the Direct Billing System (DBS) to accumulate the costs incurred by the department when overseeing environmental clean ups. These costs are billable to the responsible parties. During our audit period these recoveries totaled \$30 million and were used to reimburse the Hazardous Discharge Site Cleanup Fund and the New Jersey Spill Compensation Fund. DEP employees code their timesheets for time spent on specific projects through the Electronic Cost Accounting and Time Sheet System (ECATS). Through an interface with the state's centralized payroll system, actual salary costs are derived. Salary costs applicable to projects that are billable to responsible parties are then uploaded to the DBS. The DBS applies a salary additive rate for employee leave time, a fringe benefit rate, and an indirect cost rate to the direct salary costs. Since 2002 homeowners and developers have been exempt from the indirect cost rate. On occasion other direct costs may be added manually to the DBS. These costs are then forwarded to the Department of the Treasury's Bureau of Revenue for billing and collection. Our audit found that since January 1998 approximately \$10 million in oversight costs was never billed to responsible parties because DEP management failed to ensure that project managers submitted the necessary documentation that would initiate the creation of a proper project number on the DBS for the accumulation of billable costs.

**NEW JERSEY TRANSPORTATION TRUST FUND AUTHORITY APPROPRIATIONS
AND DEPARTMENT OF TRANSPORTATION CONTRACT ADMINISTRATION**

Bureau of Auditing

The Department of Transportation, Division of Accounting and Auditing, Bureau of Auditing is responsible for auditing professional service contracts. The bureau established a two-year audit cycle for major consulting engineering firms and a three-year audit cycle for major utility and rail consultant firms. Since substantial portions of the department's contracts are federally funded, the bureau has incorporated the federal cost principles in the audit process.

In order to comply with state and federal requirements, the department has contracted with three certified public accounting (CPA) firms to audit consultant contracts to determine if costs were incurred, billed, and paid under the terms of the contract. The bureau has criteria to audit all consultants with expenditures totaling \$500,000. As of October 1, 2005 there were 1200 contracts with cumulative unaudited expenditures totaling \$950 million. Some of these contracts date back to 1993. Approximately 100 consultant firms require contract cost auditing on an ongoing basis. To maintain a two-year cycle, 50 firms should be audited annually. In addition, we noted no audits have been performed on the major utility and rail consultant firms.

The department's approach is to include all outstanding contracts in the scope of the CPA's review to assist in the elimination of the backlog. However, the bureau's audit plan is an ever changing document which may push planned audits to a future date. In addition, since the consulting contract terms only requires them to retain their supporting documentation for a minimum of three years, the department needs to decide if older contracts should be included in the scope of the audits. An alternative approach may be to audit current period contracts and if problems exist, expand the scope to prior periods.

The bureau only finalized 23 audits during fiscal years 2004 and 2005. As of October 2005 an additional 44 CPA audits were outstanding; 26 had been received by the bureau in draft form, while 18 had not yet been submitted. At this rate the backlog will continue to grow. Additional efforts must be made to eliminate the backlog and to finalize ongoing audits.

In addition to the audit contract processing issues, we identified a lack of follow up on audit results. The audits may identify questionable costs when the consulting firm is unable to support amounts billed to the department. If the bureau concurs with the results, a receivable is established for consulting firm overpayments. Department records indicate outstanding receivables of \$6.5 million dating back to 1965. No collection efforts were being undertaken. However, the department initiated collection efforts as of July 2005, but only for currently completed audits.

**DEPARTMENT OF HUMAN SERVICES
DIVISION OF DEVELOPMENTAL DISABILITIES
WOODBIDGE DEVELOPMENTAL CENTER**

Alleviating Excess Overtime

As a part of our audit, we analyzed overtime paid for nursing coverage at the Woodbridge Developmental Center (center) which totaled \$1.5 million during calendar year 2004. We found that 49 of 110 nurses earned overtime in excess of 25 percent of their annual salary. To determine the cause of this overtime, we reviewed the methods employed to schedule nursing coverage at the facility. We found the center does not schedule standard nursing coverage for three shifts, seven days per week. Many unfilled nurse positions exist on Fridays through Mondays. We examined the nurse coverage scheduled for May 2004 and May 2005 and found that 71 and 65 percent of the overtime paid in those respective months was earned because weekend shifts were not fully staffed. We analyzed the staffing levels required throughout the year and found that hiring six additional nurses at a cost of approximately \$379,000 would allow the center to provide the required seven-day, three-shift coverage and could reduce the overtime paid by approximately \$1 million.

Revenues

Woodbridge Developmental Center is a facility charged to care for and train developmentally disadvantaged persons. The center has been certified as an Intermediate Care Facility / Mental Retardation (ICF/MR) for many years and as such receives funding based on an approved per diem rate under the federal Medicaid program. The fiscal year 2005 daily rate for the center is \$502. Current billing practices are based upon a daily population movement report which tracks clients in the facility. The center receives monthly ICF/MR program reimbursements based upon the number of days a client resides in the facility. The center does not bill for clients temporarily residing in the center's "acute care unit". We were not able to obtain a reasonable explanation as to why the center deems clients ineligible for program benefits while in that unit. We noted that 3,800 acute care patient days were not billed from March 2004 through February 2005. If the same number of acute care days occurs in 2005, \$1.9 million could be billed to Medicaid.

While the center does not bill the ICF/MR program it records doctor visits and procedures performed for individual clients. This information should be coded by the doctors with all pertinent client information, entered by the center in a computer system, and recorded within the Division of Developmental Disabilities. Claim forms are then submitted electronically for reimbursement under the Medicare Part B program. This program pays on average \$35 per claim. We noted during August 2004 that doctors provided 900 cases of medical attention resulting in 700 reimbursable services under the Medicare program. When reviewing payments on these cases, we were unable to identify whether 480 eligible services were claimed, which potentially results in a loss of Medicare reimbursement amounting to \$16,800. Among the reasons we identified for this condition were doctors not filling out the proper forms timely, doctors miscoding the procedures, incomplete forms, and items thought eligible being disallowed.

**DEPARTMENT OF EDUCATION
ADMINISTRATION**

Revolving Funds

The annual appropriation act specifies that funds are available during the current fiscal year and for one month thereafter for expenditures applicable to said fiscal year. Unless otherwise provided all unexpended balances lapse into the State Treasury. Revolving fund account balances are carried forward into the next fiscal year. A revolving fund is defined as a fund established to finance (1) state activities of a business or commercial nature or (2) the operation of an intergovernmental service agency or enterprise, which generates receipts (income) from the sale of commodities or service. Such receipts are available for the continuing operation of the activity or enterprise.

The Department of Education (department) maintains various revolving funds. One revolving fund is used for the print shop and office supplies. The department also utilizes this fund to pay for interdepartmental postage and telephone charges which are subsequently recovered from other organizational units within the department. Since fiscal year 1993, the unexpended balance in this fund has increased from \$58,000 to \$1.4 million. Our review disclosed the following:

- At the fiscal year ending June 30, 2005 approximately \$743,000 in unexpended state balances which should have lapsed to the State Treasury were improperly credited to the fund.
- An additional \$764,000 was credited from four special purpose accounts to cover potential lawsuits. Settlements would normally be funded through the Department of the Treasury's interdepartmental tort claims account. A reserve was placed on this fund by the state's budget bureau to prevent the department from spending these funds without prior approval.
- Approximately \$1.1 million was expended out of the revolving fund for items such as a department vehicle, travel expenses, official receptions, furniture and computers. These costs, while reasonable and necessary, should have been paid out of the department's direct state services appropriations. Furthermore, the department allocated \$568,000 of these costs to various federal programs. Our review of selected transactions disclosed that these costs are administrative in nature and would have been recovered through the department's indirect cost rate. Administrative costs are a factor of the department's indirect cost rate calculation.

Another revolving fund is used as a clearing account for certain employee salaries which are allocable to federal programs. At the end of the fiscal year 2005, federal programs were assessed \$1.4 million for salaries, fringe benefits, and an additional 20 percent of salaries for operating expenses. Since only \$1.3 million was actually expended out of the account,

**DEPARTMENT OF EDUCATION
ADMINISTRATION**

the department was able to increase available funds by \$100,000. As of July 31, 2005 this revolving fund had an unexpended balance of \$356,000.

**DEPARTMENT OF THE TREASURY
DIVISION OF THE STATE LOTTERY**

Debt Recovery

The Division of the State Lottery (division) processes payments for prizes exceeding \$600. Before checks are processed, the division is required to match the payment file with other state records to determine if any prize winners have defaulted on student loans or child support obligations. Amounts owed to these agencies are deducted from the prize and forwarded to the respective agency before payment is made. The division could also recover amounts for other state agencies by matching the prize winners file to the Division of Taxation's Set-off of Individual Liability (SOIL) database which contains detailed records of debt owed to the state. We noted the division paid \$900,000 to prize winners during 2005 that could have been recovered.

DEPARTMENT OF CORRECTIONS
LIFE SKILLS ACADEMY

Contract Administration

The Department of Corrections (DOC) is responsible for administering a \$1.5 million appropriation to Life Skills Academy (LSA). The no-bid contract requires LSA to train inmates to better manage their lives while still incarcerated and in preparation for their eventual parole.

The terms of the agreement with DOC requires the vendor to employ instructors to visit various DOC institutions on a scheduled basis for two hours a day, five days per week, for eight weeks. Upon completion of the 80 hours of training, a certificate of graduation is given to each successful inmate. The contract allows for flexibility in the scheduling of classes to accommodate for missed and cancelled classes. Vendor payments are based and scheduled upon the contemplated graduation of 1,250 inmates each fiscal year.

The DOC has the responsibility to monitor the terms and conditions of the contract and the vendor's performance to ensure the value of services received is commensurate with the dollars disbursed. Our audit disclosed that DOC has not effectively monitored this contract and has allowed LSA to self monitor and report upon critical terms and conditions of the contract, such as attendance, eligibility of graduates, and curriculum hours completed.

Our review indicates that DOC did not require independent attendance data from the institutions where services were rendered prior to remitting payment to LSA. We requested that all participating institutions provide us with information about whether the institution kept attendance records. Of the eight institutions that responded, one acknowledged taking attendance and seven stated they did not take attendance. In addition, we reviewed the records at one facility and noted that the average graduate completed approximately 60 hours of training rather than the 80 hours required by the contract. At this same institution we also noted the company supplied graduation list included inmates serving as facilitators at the classes who had already graduated from the program.

Administration of a contract should include obtaining independent information about the effectiveness of the program. We were unable to obtain any information about the effectiveness of the program from DOC. However, it was the opinion of certain DOC management that the department may be in the position to provide similar or equal services with existing resources.

DEPARTMENT OF EDUCATION
MARIE H. KATZENBACH SCHOOL FOR THE DEAF

Business Office Operations

The Marie H. Katzenbach School for the Deaf (school) expends \$300,000 in business office salaries to process \$2.8 million in purchases and \$10.5 million in revenue annually. Employee turnover, vacancies, leave of absences, and the lack of cross-training have adversely impacted the operations of the business office. In April 2005, the school hired a new business manager who had limited experience using the state accounting system. In addition, the business office has operated without a permanent accountant since March 2004. As a result, we noted internal control weaknesses over purchasing, off-line accounts, segregation of duties, system security, and cross-training.

During fiscal years 2004 and 2005, the school expended \$950,000 for the purchase of goods and services which were not approved or recorded by the business office prior to their receipt. Confirming purchase orders were prepared after delivery. During this two-year period, 60 percent of all purchases were confirming orders. As a result, management did not know what the obligations of the school were and the various units had the ability to overspend their budgets. Most of the confirming purchase orders were for the maintenance and food service departments.

The business manager is not able to properly monitor accounting transactions involving tuition, receivables, and the Student Activity and Petty Cash Funds because the accounting software used by his staff is not on the school's computer network.

We noted that the school does not properly segregate duties. The Student Activity Fund and Petty Cash Fund are not independently reconciled. Instead, the bookkeeper processed, recorded, and reconciled all transactions on the accounting system for these funds. Bank reconciliations should be prepared by an employee who does not process accounting transactions. Another employee receives the cash receipts and posts them to the tuition receivable records. These responsibilities should be performed by different individuals to help safeguard assets.

We found a bookkeeper, while on extended leave of absence, provided her user id and confidential password to another business office employee. In addition, the former and current business managers also provided their user id to the same employee which allowed payments to be processed through the system without supervisory approvals. The state's summer 2005 accounting system newsletter reminded agencies that user ids and passwords are confidential information and are not to be shared. We also noted that one individual had system access even though the individual was no longer employed by the school.

Two temporary employees were hired to fulfill the duties of the permanent accountant. When the last temporary employee terminated their employment in August 2005, cash receipts activity they were responsible for were no longer performed. As of November 10, 2005 there were 28 checks totaling \$169,000 from September 29, 2005 through November 9, 2005, which had not been deposited or recorded in the accounting system.

**DEPARTMENT OF EDUCATION
MARIE H. KATZENBACH SCHOOL FOR THE DEAF**

State regulations require cash receipts be deposited on the day of receipt. Furthermore, monthly bank reconciliations for the Student Activity Fund and Petty Cash Fund had not been prepared since June 2005. No other employees were cross-trained to perform these duties.

**DEPARTMENT OF LAW AND PUBLIC SAFETY
JUVENILE JUSTICE COMMISSION
NEW JERSEY TRAINING SCHOOL FOR BOYS**

Optical Lens Program

The optical lens program at New Jersey Training School for Boys (NJTSB) provides residents the opportunity to obtain a vocational education and develop skills which could be utilized upon their release. In addition, the program provides eyeglasses to the Department of Corrections for inmates and provides safety glasses to the Department of Environmental Protection at a reasonable cost. Cost savings to the state could be increased by offering this service to other state departments and programs.

Our contact with the Department of Human Services revealed the following:

- Ancora Psychiatric Hospital informed us that the Medicare program will cover the cost of one pair of eyeglasses every two years for their residents while the state must fund any additional purchases. The average cost of their eyeglasses is \$92.
- New Lisbon Developmental Center has a vendor contract in which the average cost of eyeglasses is \$120 and repairs are made to damaged eyeglasses for \$65.

We found that eyeglasses are produced by NJTSB at an average cost of \$25 and there is no charge for subsequent repairs. Based on this information, other entities could attain 75 percent reductions in eyeglass costs and 100 percent savings in repairs.

In addition to substantial savings to those who participate, the utilization of NJTSB by other departments and programs would provide more opportunities for NJTSB residents to develop skills that may enhance their future.

**DEPARTMENT OF THE TREASURY
DIVISION OF PROPERTY MANAGEMENT AND CONSTRUCTION**

Timeliness of Lease Procurement

Acquisition of new leased space for state operations is broken into three phases. In the initial planning phase, the Property Management unit receives a Space Planning Request which is reviewed and forwarded to the Office of Management and Budget for budgetary approval. The negotiation phase begins when a scope of work is forwarded to the Contract Administration section whose functions include procurement through an advertised bid process and negotiation with prospective landlords. The final phase involves submission to the State Leasing and Space Utilization Committee for approval. The Division of Property Management and Construction (division) estimates that acquiring lease space using these three phases should take from nine to ten months. In the event that there is an immediate space need there is an emergency procedure that permits division personnel to bypass the bid process and contact prospective landlords directly.

Our review of the advertised bid process revealed that the actual amount of time from initial assessment of space needs to final approval exceeded two years. This extended time frame could adversely impact property availability, undermine the competitive bidding process, and affect final negotiated lease rates. In addition, protracted lease negotiations may force the division to seek property as an “emergency” procurement where the bidding process is bypassed. A review of 43 advertised leases revealed that the planning phase averaged over one year. The division’s timeline estimates that this portion of the process should take less than two months, which is comparable with the state of Maryland which was recognized by the federal government’s General Services Administration for best practices in real property management.

MOTOR VEHICLE COMMISSION CENTRAL OFFICE

Revenue

Types of revenue collected by the Motor Vehicle Commission include licenses, registrations, titles, program fees, fines, surcharges, and taxes relating to the operation of motor vehicles and affiliated businesses. There are 30 units throughout the central office which collect and record revenue. The Financial Management section is responsible for the collection of all the units' deposits, the preparation of the daily deposit package for the armored car service, and the recording of all revenue collected within the central office. State Treasury Circular Letter 94-24-OMB, Deposits by State Agencies, states that revenue should be deposited on the same day as received. Total revenue collected by the central office was \$167 million in fiscal year 2004 and \$165 million in fiscal year 2005.

We tested the commission's revenue collection procedures by sampling deposits from eight of the central office units which receive revenue. Our tests revealed untimely deposits, improper document preparation, posting errors, and inadequate cash reconciliation procedures.

Untimely Deposits

We tested 48 deposits totaling \$8,013,000 and found that 29 were deposited from 2 to 30 days after they had been received. These late deposits occurred in seven of the eight units tested and totaled \$4,694,000. We also found that two of the sample units did not restrictively endorse checks upon receipt nor did they keep the checks in a secure location prior to deposit. The delays in depositing and lack of endorsements in two units were due to the fact that checks are kept with the submitted documents while the processing cycle is completed. In addition, two of the units did not prepare daily deposits and three units that prepared daily deposit packages neglected to deliver them on a daily basis to the Financial Management section. The presence of undeposited cash and checks in so many locations increases the possibility of lost or misappropriated funds.

Cash Reconciliations

Three of the central office units sampled issue licenses, registrations, and titles, as do the 45 motor vehicle agencies located throughout the state. These transactions are recorded on various computer systems which provide daily summaries of all transactions. At the end of the day, unit personnel compare daily collections to these summaries, which indicate what should have been collected if all transactions were posted accurately to the system and proper collections were received. If the differences between actual collections and system totals exceed a preestablished amount, reconciliations should be performed and documented by the units. We found that the reconciliation procedures of all three units were unsatisfactory. These units did not prepare the required documentation or adequately explain the differences for 12 of the 15 sample items where daily collections did not agree with the business totals from the system reports. Proper reconciliations were not

**MOTOR VEHICLE COMMISSION
CENTRAL OFFICE**

performed because of inadequate oversight by unit supervisors. Such reconciliations should identify the reasons for differences, which could be theft, failure to collect payment, incorrect recording, or errors in the preparation of deposits. When reconciliations are not performed, commission management cannot take the appropriate steps to rectify the problems.

**MOTOR VEHICLE COMMISSION
INFORMATION TECHNOLOGY MANAGEMENT**

Driver History Database

The Motor Vehicle Commission (MVC) has not performed an analysis of their driver history database. Database integrity is important as the information supports the validity of the state's new secure digital drivers' licenses.

We analyzed the MVC driver history database to determine the integrity of driver license data. As part of this analysis, we compared the driver history database with the Department of Health, Division of Vital Statistics' deceased in-state and out-of-state resident files. We also reviewed what appear to be excessive issuances of duplicate licenses recorded in the database.

Results from our analyses revealed 15.5 million licenses recorded as issued since the system's inception. Social Security Numbers (SSN) were reviewed and we found over 6 million licenses had SSNs that contained all zeros (000-00-0000) or all nines (999-99-9999), which are no longer accepted when applying for a license.

The 6 million licenses with SSNs containing all zeros and nines were analyzed for propriety and the following results were disclosed:

- 95 percent of the licenses have expired but are not designated as expired in the non-comm field.
- 220,500 of the licenses remain active.

The remaining 9.5 million driver's licenses with SSNs that were not all zeroes or nines were analyzed for propriety and we found in the non-comm field that 2.9 million licenses have expired but are not designated as expired.

When we compared the driver history database with the Department of Health, Division of Vital Statistics' deceased resident files we found 75,000 deceased persons listed as having a NJ driver's license that have not been designated as deceased in the MVC driver history database. We also found 3,400 licenses of deceased persons recorded as issued after the deceased's date of death, of which over 500 were designated as deceased in the driver history database, but were issued anyway.

The duplicate license field was also reviewed for propriety. Any person who was issued five or more duplicates and whose license has not expired was included. Our results disclosed that 11,600 individuals are recorded as receiving a duplicate license more than four times. The highest number of duplicates for a license that has not expired is 26.

NEW BRUNSWICK SCHOOL DISTRICT

Management Compensation

The New Brunswick Board of Education (board) is responsible for approving the expenditure of district funds, including the compensation of its employees. Contracts governing the terms of employment for management should clearly delineate the salaries and benefits payable. Any modification of such contracts that change the amount of compensation and/or the nature and amount of benefits should have the explicit approval of the board. Although salaries for all 2,000 full-time and part-time district employees are approved annually by the board, modifications to the former Superintendent's compensation were not formalized in a revised contract and approved by the board as a whole. Our review of compensation for management indicated the following deficiencies.

The compensation for the former Superintendent in his final year amounted to \$226,662 in regular salary, \$16,000 in extraordinary earnings, \$45,364 for the cashing out of sick and vacation leave at the beginning of fiscal year 2004 and \$261,135 for his remaining sick and vacation leave upon his retirement at the end of the fiscal year. There was no formal contract, contract modification, or resolution adopted by the board to set the terms of the former Superintendent's compensation during his last year, including how he would be paid for unused leave time. In fact, the former Superintendent's last formal contract with the board was dated March 1990.

Our review of various memoranda provided to us by the district's management to support compensation amounts shows the former Superintendent's salary rising from \$145,371 in fiscal year 1998 to \$226,662 in fiscal year 2004.

Although these memoranda were on the board's letterhead and included the signature of the Board President or a board member, there was no board resolution. Instead, they appeared to be negotiation requests, proposals, or internal instructions to payroll. These documents often contained handwritten notes and/or alterations. None of these increases, which included such benefits as a car allowance, reimbursement of his pension contributions and contributions to his annuity fund, were evidenced by any documentation other than these memoranda. Similarly, extraordinary items including a yearly bonus of \$10,000 and a monthly stipend of \$500 also were not recorded in a board resolution.

In the March 1990 formal contract, the former Superintendent was allowed 30 vacation days per year, with a maximum carry forward of 30 days. It also included 87.5 days from prior service. This contract did not provide for the cashing out of either vacation or sick leave prior to retirement. It allowed for payment of unused vacation days upon termination and half of any unused sick days up to \$15,000 maximum upon retirement. Additional memoranda dated June 13, 2000 and May 8, 2003 increased his annual vacation days from 30 to 60 days with no indication on how many days could be carried forward. He cashed out 38 unused vacation days at full salary and 40 sick days at half salary during fiscal

NEW BRUNSWICK SCHOOL DISTRICT

year 2004 prior to his retirement. A memorandum dated July 28, 1998, signed by the Board President, eliminated the \$15,000 maximum and he was paid \$81,693 at retirement representing 50 percent of his accumulated sick leave balance.

Our review of the compensation for the Assistant Business Administrator/Board Secretary showed that she received over \$14,000 in overtime payments during fiscal year 2004. However, her contract for that year, while providing for overtime compensation, capped the allowable amount at \$5,000.

NEW JERSEY COMMERCE, ECONOMIC GROWTH,
AND TOURISM COMMISSION
URBAN ENTERPRISE ZONE PROGRAM

Loan Projects and Second Generation Funds

Loan projects fall into two categories: loans to specific businesses within a zone or funds to establish revolving loan programs. Initially, these loans are made as "first generation" loans directly from the Zone Assistance Fund. They are provided to individuals or business entities within the zone. The installment payments on "first generation" loans, along with the proceeds received from the sale of properties/equipment acquired through the Urban Enterprise Zone (UEZ) program, become the funding source of the zones' "second generation" accounts. These accounts are maintained and controlled at the local level. Per the UEZ policies, the use of second generation funds by the zones must comply with the UEZ legislation, although it is not subject to authority approval. Zones are required to submit quarterly reports only identifying second generation fund balances. However, this information is not adequately reviewed, compiled, or monitored by the authority. The zones have a reported bank balance of \$11.9 million in second generation funds as of December 31, 2005.

The state UEZ program does not have an adequate database to record loan projects, thus making it difficult to monitor these projects. We found that loan defaults or changes in loan terms and agreements are not communicated to the state program as noted in the following projects.

One zone provided a \$525,000 loan to a business entity in November 2002 to purchase eight acres of property for the purpose of constructing a car dealership. The car dealership filed for bankruptcy and the loan was discharged on January 14, 2005. On this same day, the remaining loan balance of \$477,000 was satisfied and the payment was deposited into the zone's second generation fund. Neither the New Jersey Commerce, Economic Growth, and Tourism Commission (commission) nor the Urban Enterprise Zone Authority (UEZA) were notified of the bankruptcy or the closing of the business.

Our review of another zone's \$150,000 loan program revealed that a loan applicant declined a \$30,000 loan. The UEZ coordinator elected to distribute these funds to another applicant increasing their previously approved loan amount. This information was never disclosed to the state UEZ program. In addition, the zone failed to comply with the project's matching requirement of a two to one ratio of private to state funds as indicated in the project proposal.

The commission's internal report referred to loan projects within one zone in which three businesses defaulted on their loans within months of receiving the funds. We reviewed the project files and found the defaults totaled \$28,000. There are no procedures requiring the zone to report the defaults nor is this information required to be communicated to the UEZA.

**NEW JERSEY COMMERCE, ECONOMIC GROWTH,
AND TOURISM COMMISSION
URBAN ENTERPRISE ZONE PROGRAM**

In 2001, a municipality received approval for advance funding of \$1.35 million for a loan to construct an ice arena. Closing on the loan was originally scheduled for October 2001. Closing was delayed and did not occur until January 2002. During our field visit to the zone, we learned that the city actually owned the mortgage for only one day, before selling it off to the lender of the primary mortgage. Neither the change in the terms of the deal nor the delays in the closing were disclosed to the state UEZ program. The funds were subsequently deposited in the zone's second generation fund.

During our review we noted that the same municipality came before the UEZA in July 2005 and requested advanced funding in the amount of \$5 million for an economic development loan to a local business. The proposal stated that the zone would also provide a \$3 million loan from their second generation fund, which we interpreted as a zone match. The business received a total of \$8 million in state and zone funding. Zone officials closed on the loan and disbursed \$8 million prior to seeking UEZA approval for this project. In February 2006 the zone returned to the authority with a project proposal requesting first generation funding of \$3 million for the "Retirement of an Outstanding Balance on a Revolving Line of Credit". It appears that the zone had not used their second generation funds as their match but rather borrowed the funds and then requested UEZ funds to satisfy the loan.

**OFFICE OF LEGISLATIVE SERVICES
OFFICE OF THE STATE AUDITOR
SCHEDULE OF REPORTS ISSUED DURING 2006**

<u>REPORT</u>	<u>TYPES OF FINDINGS</u>			
	<u>COMPLIANCE</u>	<u>CONTROLS</u>	<u>ECONOMY/ EFFICIENCY</u>	<u>NONE</u>
Casino Control Fund		OPINION ONLY		
The College of New Jersey	X	X		
Information Technology		X		
Department of Corrections				
Garden State Youth Correctional Facility		X		
Life Skills Academy		X		
Mid-State Correctional Facility	X	X		
Riverfront State Prison		X		
Department of Education				
Administration		X		
Early Childhood Education Program		X		
Marie H. Katzenbach School for the Deaf	X	X		
New Jersey After 3 Program	X	X		
Department of Environmental Protection				
Green Acres Funds				X
Site Remediation and Waste Management Funds	X	X	X	
Department of Health and Senior Services				
Division of Aging and Community Services			X	
Department of Human Services				
Ancora Psychiatric Hospital		X		
Division of Developmental Disabilities				
New Lisbon Developmental Center	X	X		
Woodbridge Developmental Center			X	
Division of Mental Health Services				
Administration and Support Services				X
Department of Labor and Workforce Development				
Tax Revenue Systems		X		
Unemployment Insurance Services	X	X		

**OFFICE OF LEGISLATIVE SERVICES
OFFICE OF THE STATE AUDITOR
SCHEDULE OF REPORTS ISSUED DURING 2006**

TYPES OF FINDINGS

<u>REPORT</u>	<u>COMPLIANCE</u>	<u>CONTROLS</u>	<u>ECONOMY/ EFFICIENCY</u>	<u>NONE</u>
Department of Law and Public Safety				
Division of Gaming Enforcement and Casino Control Commission				X
Juvenile Justice Commission				
New Jersey Training School for Boys	X	X	X	
Department of Personnel	X	X		
Department of the Treasury				
Division of Property Management and Construction		X	X	
Division of the Ratepayer Advocate		X		
Division of the State Lottery		X	X	
Motor Vehicle Commission				
Central Office	X	X		
Information Technology Management		X		
New Brunswick School District		X		
New Jersey Commerce, Economic Growth, and Tourism Commission				
Urban Enterprise Zone Program		X		
New Jersey Schools Construction Corporation		X	X	
New Jersey Transportation Trust Fund Authority Appropriations and Department of Transportation Contract Administration		X		
Pinelands Commission		SINGLE AUDIT REPORT		
Administration				X
State of New Jersey				
Report on Internal Control and on Compliance and Other Matters Related to Our Audit of the State's Comprehensive Annual Financial Report				X