



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

**Department of the Treasury
State Legal Services**

July 1, 2010 to April 30, 2012

**Stephen M. Eells
State Auditor**

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The Honorable Stephen M. Sweeney
President of the Senate

The Honorable Sheila Y. Oliver
Speaker of the General Assembly

Mr. Albert Porroni
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Enclosed is our report on the audit of the Department of the Treasury, State Legal Services for the period of July 1, 2010 to April 30, 2012. If you would like a personal briefing, please call me at (609) 847-3470.

A handwritten signature in black ink, reading "Stephen M. Eells".

Stephen M. Eells
State Auditor
August 6, 2012

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Scope

We have completed an audit of the Department of the Treasury, State Legal Services for the period July 1, 2010 to April 30, 2012. Our audit included financial activities accounted for in the state's General Fund. Annual appropriations were \$20 million in fiscal year 2011 and \$15 million in fiscal year 2012. The State Legal Services program provides grants for free civil legal services to eligible individuals who cannot afford legal counsel. These services are provided through the non-profit organization, Legal Services of New Jersey and its regional offices.

Objectives

The objectives of our audit were to determine whether financial transactions were related to the agency's programs, were reasonable, and were recorded properly in the accounting systems.

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.

In preparation for our testing, we studied legislation, the administrative code, circular letters promulgated by the Department of the Treasury, and policies of the agency. 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 read the budget messages, reviewed financial trends, and interviewed agency personnel to obtain an understanding of the programs and the internal controls.

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

Conclusions

We found that the expenditure transactions included in our testing were recorded properly in the accounting systems, however, we were unable to determine reasonableness and whether the expenditures were related to the program because the Department of the Treasury is unable to independently verify financial eligibility of clients being served. In making these determinations we noted an internal control weakness requiring management's attention.

Program Monitoring

Program monitoring should be enhanced.

The Department of the Treasury cannot independently monitor the eligibility of clients receiving services under the program. This increases the risk that clients are receiving free legal services when they are not financially eligible. In fiscal year 2012, eligible recipients are those who are under 200 percent of the federal poverty level based on family size. The grant agreements between the department and Legal Services of New Jersey (LSNJ) and its affiliates are structured in a manner that protects the confidentiality of case information including the client's identity unless the client grants written consent. Without the client's identity, the department cannot verify their financial information. Although LSNJ procedurally asks for proof of a client's financial eligibility, it does not have the ability to independently verify the accuracy of the information. In order for a granting agency to be accountable to the public, it should have the ability to effectively monitor the program.

Recommendation

We recommend the Department of the Treasury seek legislation that would enable it to restructure the grant agreement with Legal Services of New Jersey and its affiliates in a manner that requires clients to consent to the release of their identifying information to Treasury for financial eligibility monitoring purposes only.

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Governor

KIM GUADAGNO
Lt. Governor

ANDREW P. SIDAMON - ERISTOFF
State Treasurer

July 26, 2012

Mr. John J. Termyna
Assistant State Auditor
Office of Legislative Services
Office of the State Auditor
P.O. Box 067
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RE: Departmental Audit Response - Department of Treasury
State Legal Services

Dear Mr. Termyna:

Thank you for the opportunity to respond to the audit report of the Department of the Treasury, State Legal Services program.

The audit report concludes that your office was unable to determine reasonableness and whether the expenditures were related to the Legal Services program, because the Department of Treasury is unable to independently verify financial eligibility of clients being served. Further, your office recommends the Department seek legislation that would enable it to restructure the grant agreement with Legal Services of New Jersey and its affiliates (collectively "LSNJ") in order to require LSNJ's clients to consent to the release of identifying information for financial eligibility monitoring purposes.

While the Department generally agrees that independent eligibility determination would be an additional tool for program monitoring, implementation is difficult and appears to be legally impermissible. First, the New Jersey State Legislature cannot require LSNJ's clients consent to disclosure of information that the New Jersey Supreme Court has deemed protected by the attorney-client privilege or otherwise confidential. That would be inconsistent with the separation of powers. And, the New Jersey Supreme Court has made clear that when a client is asked to consent to disclosure of protected information, the consent must be "totally voluntary" - meaning the "client can deny consent without any sense of guilt or embarrassment." In re Advisory Opinion No. 544 of N.J. Supreme Court Advisory Committee on Professional Ethics, 103 N.J. 399, 407 (1986) (citing *ABA Informal Opinion 1287* (1974)).

Second, you propose to require release of LSNJ's clients' "identifying information" but do not specify what information is sought. To the extent that information includes Social Security

numbers, your proposal would violate the federal Privacy Act, which prohibits the Department from *requiring* LSNJ's clients to disclose their Social Security numbers. See Privacy Act of 1974, Pub. L. No. 93-579, § 7(a)(2)(A) & (B), 88 Stat. 1896, 1909 (1974), *reprinted in* 5 *U.S.C.A.* § 552a (note). The Privacy Act allows the mandatory collection of Social Security numbers but only in very limited situations, none of which is applicable here. The Privacy Act also does allow voluntary disclosure of Social Security numbers, assuming that the governmental entity is authorized to collect them. Therefore, the State Legislature would need to adopt legislation to authorize the collection of such information. However, because of the Privacy Act restrictions, such collection could be voluntary only.

Third, while the exact nature of the legislation you propose is not entirely clear, it seems likely that it would be inconsistent with federal law applicable to LSNJ (and could potentially be preempted by federal law). The Legal Services Corporation was created by federal legislation. The Legal Services Corporation Act of 1974 explicitly provides that “attorneys providing legal assistance must have full freedom to protect the best interests of their clients in keeping with the Code of Professional Responsibility, the Canons of Ethics, and the high standards of the legal profession.” 42 *U.S.C.A.* § 2996(6). More specifically, the Act requires LSNJ’s attorneys to comply with State rules of professional responsibility and protects privileged/confidential client information from disclosure. See 42 *U.S.C.A.* §§ 2996e(b)(1)(A) & (b)(3) & 2996h(d). And, the New Jersey Supreme Court has specifically held that RPC 1.6(a) and the attorney-client privilege prohibit legal services providers from disclosing their clients’ names, addresses, etc. to state agencies that provide funding. See *In re Advisory Opinion No. 544*, *supra*, 103 *N.J.* at 409.

Moreover, even if legislation were adopted and the Grant Agreement were modified, those changes would not improve the Department’s ability to verify client eligibility. Under the existing Grant Agreement, LSNJ conducts extensive questioning of all applicants for limited or full representation. Applicants must disclose all sources of income, assets, household and living arrangements, and related factors. All applicants for such services must sign a certification attesting to the accuracy of the information. Where questions or doubts are presented, LSNJ requires further verification. This process is governed by detailed federal regulations. See, e.g., 45 *C.F.R.* part 1611. Those regulations make clear that a legal services client’s “financial eligibility [must be] determined in a manner conducive to development of an effective attorney-client relationship.” 45 *C.F.R.* § 1611.1.

The vast majority of LSNJ’s cases involve one of four main problem types where an individual’s income and any available assets are directly or indirectly at issue in the legal proceeding, and consequently become quickly known to both LSNJ and adjudicators. Income and assets in such matters are discoverable and often litigated, and are not subject to being concealed. These problem types are:

- (1) Consumer defense matters and bankruptcy; (2) family matters, especially divorce and child support; (3) housing, particularly tenancy and foreclosure; and (4) entitlements matters, where individuals are seeking to secure or retain one or more government benefits.

Moreover, the Department, in its role as the Grant Administrator to LSNJ, does perform certain routine reviews to assure that only those eligible for the program are receiving services. For

example, the Department reviews reports submitted by LSNJ and its affiliates and conducts on-site visits to their offices.

LSNJ's semi-annual reports to the Department outline how each service provider has provided the necessary legal services to its clients and the costs incurred in doing so. The reports are accompanied by the necessary expense documentation and audit submissions typically required by grant agreements. The latter always includes verification from the certified public accountant firm that conducted the audit, confirming the service provider's compliance with applicable laws, regulations, contracts and grant agreements.

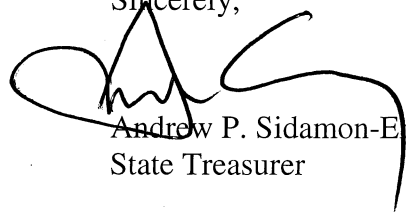
In addition, the Department conducts periodic on-site visits. To confirm that LSNJ is verifying client eligibility, during on-site visits:

1. The Department views client files of service providers and their case attorneys.
2. Case attorneys are asked to provide eligibility information on random client files.
3. Similar to an audit, the random files are then copied with client identifiers such as SSNs redacted. The Department representative is able to verify their existence before making the redacted copy. The files disclose the information provided by the client to obtain services. Such information may include:
 - a. Wage statement;
 - b. Verification that client is on Social Security or Assistance, and thus automatically eligible; and/or
 - c. Proof that the client was referred by another State or Federal Agency such as Medicaid, who has already verified eligibility.

To further ensure the eligibility of all LSNJ clients, the Department is presently reviewing and looking to strengthen these measures through increased sampling and more meaningful reporting.

While the Department does not independently verify the eligibility of all LSNJ clients, these measures provide reasonable means to verify client eligibility through typical sampling without violating attorney-client privilege, federal guidelines or any laws. The Department does not believe that the legislation you propose would significantly improve on existing or enhanced measures.

Sincerely,



Andrew P. Sidamon-Eristoff
State Treasurer

c: Dave Ridolfino, Associate Deputy State Treasurer, Department of Treasury
Daniel Povia, Chief Auditor, Internal Audit Unit, Department of Treasury