
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 2003. In conformance with our responsibilities to perform financial and compliance audits, all state agencies are audited periodically. During 2003, we issued 37 reports which identified \$46.6 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

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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 State Auditor also performs other similar or related duties as required of him by law.

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.

COST SAVINGS

During calendar year 2003 we identified \$46.6 million in new cost savings or revenue enhancements. The schedule of cost savings is presented on page 3.

**OFFICE OF LEGISLATIVE SERVICES
OFFICE OF THE STATE AUDITOR
SCHEDULE OF COST SAVINGS AND
REVENUE ENHANCEMENTS
REPORTS ISSUED DURING 2003**

<u>REPORT</u>	<u>COST SAVINGS/ REVENUE ENHANCEMENTS</u> (In Thousands)
Department of Community Affairs	
Housing Assistance and Inspection Programs	\$ 1,970
Department of Corrections	
Administration	1,400
Department of Education	
City of East Orange Board of Education	46
City of Paterson Board of Education	86
Early Childhood Education Program	360
Jersey City Public Schools	465
Pleasantville Board of Education	
Early Childhood Education Program	363
Trenton Board of Education	
Early Childhood Education Program	1,730
Newark Public Schools	289
Department of Human Services	
Division of Medical Assistance and Health Services, and Division of Disability Services Selected Programs	1,873
Division of Medical Assistance and Health Services Third Party Liability Process	13,500
Department of Law and Public Safety	
Attorney General's Law Enforcement Forfeiture Account	1,249
Division of Consumer Affairs	360
Department of Military and Veterans' Affairs	198
Department of the Treasury	
Division of Taxation	
Interest on Late Tax Refund Payments	14,500
Division of Taxation	
Transfer Inheritance Tax Revenues	500
Office of Administrative Law	600
Office of the Public Defender	9
Sick Leave Injury Program	2,500
State of New Jersey Alternative Fuel Program	<u>4,600</u>
Total Cost Savings and Revenue Enhancements	<u>46,598</u>

AUDIT REPORTS

TYPES OF AUDITS PERFORMED

Financial Audits

Financial audits are designed to provide reasonable assurance about whether the financial statements (or schedules) 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 195 funds and component units which had a total asset value of \$135 billion at June 30, 2003 based on full accrual accounting. Three other financial audits were issued in calendar year 2003.

Audits of Agencies

The objectives of this type 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 24 of these audits in calendar year 2003. These audits encompassed \$5.0 billion and \$2.9 billion of expenditures and revenues, respectively.

Information Technology Audits

The objectives of this type audit are to determine whether the financial data relating to a particular computer system are reliable, valid, safeguarded, and recorded properly. During calendar year 2003, we reported on the Department of the Treasury, Division of Revenue Information Systems.

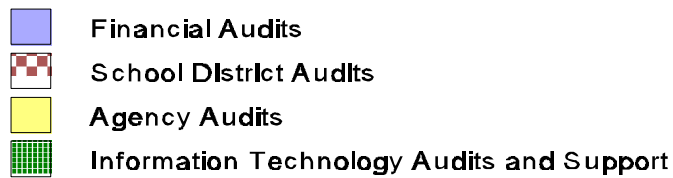
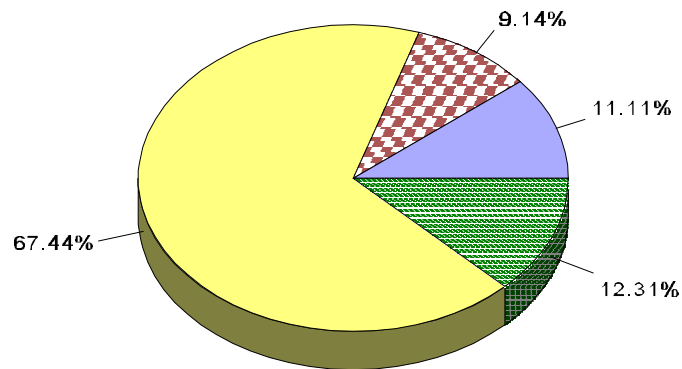
School District Audits

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 eight school districts in calendar year 2003. These audits encompassed \$1.3 billion and \$135 million of expenditures and revenues, respectively.

AUDIT REPORTS

DISTRIBUTION OF AUDIT HOURS

The distribution of audit hours used in performing audits during calendar year 2003 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 a result of an independent objective audit 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 the report are routinely sent to:

- the chairs of the pertinent Senate and 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 82 professionals and six support staff. All auditors must have a bachelors degree in accounting or a related field and a minimum of 24 credit hours in accounting. Forty-four staff members (54 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 of 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 audit communication, planning, information technology, office administration, personnel, policy, statistical 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 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.

ORGANIZATION

ADMINISTRATIVE STAFF

The administrative staff processes, files, and distributes all reports. This group is responsible for maintenance of 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, 2003**

STATE AUDITOR

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

ASSISTANT STATE AUDITOR

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ASSISTANT STATE AUDITOR

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Peter Wozniak
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Elizabeth H. Klingele

Camille E. Thomas-Day



ACCOMPLISHMENTS AND RESULTS

ACCOMPLISHMENTS AND RESULTS

Summary

This section highlights nine of the more significant audits issued during the past year which individually contained cost savings/revenue enhancements greater than \$1 million and collectively totaled \$43.3 million. The Office also issued 11 reports with individual cost savings less than \$1 million totaling \$3.3 million. Our reports also contain findings addressing areas of noncompliance with laws or regulations, weaknesses in internal controls, and economies and efficiencies to improve operations; four of the more significant audits are included in this section. All reports issued in calendar year 2003 are identified on a schedule on pages 33 to 34 and are available for review on our internet website.

We found multiple causes for refunds not being paid within six months: 1) inadequate monitoring over refund processing; 2) the failure to process refunds in a timely manner; and 3) a weakness in the Generic Tax System (GENTS) regarding the generation of a specific report. As a result, interest on Corporation Business Tax (CBT) and Gross Income Tax (GIT) refunds during our audit period total \$14.5 million.

Tax returns are received by the Division of Revenue (DOR) and posted to the taxpayer's account on GENTS. The Division of Taxation then applies various criteria to determine which refunds are held for manual review by its CBT and GIT Refund Units. Upon completion of this review a refund is issued. The state is required by law to pay interest at the prime rate on requested refunds not paid within six months. Interest is computed to the beginning of the six-month period.

There are various causes for refunds not being paid within six months. In some cases returns were not posted to GENTS in a timely manner, while in other instances returns were posted timely but were not processed by the division quickly enough to avoid paying interest. In addition, representatives of the CBT and GIT Refund Units informed us that the "Refunds/Credits to be Reviewed List" was not providing the units with all newly posted refunds pending review. To address this problem, ad-hoc reports were periodically produced to obtain all refunds to be reviewed. These ad-hoc reports disclosed some of the refunds that did not appear on the GENTS report. The refunds discovered were sometimes close to or past the six-month threshold.

Furthermore, the division has not requested the comprehensive aged file which separates all refunds pending review into six age categories. This file would be useful in identifying refunds approaching the six-month limit. We requested the file and found that as of July 2002 there were 27,846 CBT refund requests pending review totaling \$116.2 million for return years 1990 through 2001. Analysis of the report revealed that 26,892 of the refund requests pending review, totaling \$90 million, were more than 120 days old. We extracted all 28 CBT refunds pending review that were more than \$20,000 and greater than 120 days old. The 28 refunds totaled \$2 million. We requested the CBT Refund Unit review the refunds and they came to the following conclusion:

Seventeen of the 28 refund requests totaling \$1.6 million were for return years 1990 through 1992 and were an average of over 9 years old. They had not been reviewed because only refunds for the tax year 1993 and forward are entitled to receive interest. All 17 appear to be valid; however, locating the taxpayers may prove difficult due to the significant amount of time that has passed without working on the refund requests. One of the valid returns was for \$322,728 from return year 1992. However, since the company is no longer in business and has not filed a return since 1994, the overpayment will remain in the company's account and eventually revert to the state.

The requested file for GIT identified 320,912 refund requests pending review totaling \$74.4 million for return years 1999 through 2001. Analysis of the report revealed that 200,479 refund requests totaling \$22.4 million were more than 120 days old. We extracted the 35 GIT refunds pending review with potential refunds of more than \$10,000 and greater than 120 days old from the file. The 35 refund requests totaled \$1.4 million. We requested that the GIT Refund Unit review the refunds and as a result:

- eleven refunds totaling \$1.26 million were paid plus an additional \$38,915 in interest,
- fifteen refunds requesting \$173,713 were held pending further review,
- eight refunds requesting \$23,947 were denied, and
- one refund was approved for \$35,335 but was not paid due to previous amounts owed to the state.

It should be noted that the above refund requests were processed relatively quickly once they were brought to the division's attention. While all these refund requests may not be approved, the review of selected refund requests did reveal that the report did identify valid refunds.

Insurance Information Not Being Updated

The division uses a vendor to assist in identifying Third Party Liability (TPL) and to seek reimbursements from Medicare and other third-party sources. A recovery fee of approximately 10 percent is paid for this service which totals \$5 million annually. Once the division is notified of other insurance coverage through the vendor, the division should update the Medicaid Management Information System (MMIS) files. However, the division is not always updating the files. Thus the division is paying unnecessary recovery fees relating to previously identified recipients with insurance and is unable to cost avoid on subsequent claims.

We determined that during our audit period the division recovered \$32 million of TPL claims for recipients previously identified as having TPL by the vendor and paid the vendor approximately \$3 million in recovery fees. In addition, there is \$140 million in open claims for which the division is seeking recoveries through their vendor. If this occurs, the division would unnecessarily pay a recovery fee of approximately \$14 million to the vendor.

Unrecorded Medicare Coverage

Under a federal buy-in agreement, states may enroll individuals in the Medicare Part A and Medicare Part B programs and pay their premiums, currently \$316 and \$58.70 a month, respectively. The purpose is to provide Medicare health insurance, which reduces costs to the Medicaid program. The division pays Medicare approximately \$125 million annually. The Medicare buy-in system should automatically update the MMIS files. We performed a test which noted 60 Medicaid recipients for whom the division paid Medicare premiums, but whose files were not updated for this coverage on MMIS. Upon notification, the division identified an additional 1,600 Medicaid recipients with the same problem. By not updating its files, the division estimates that it paid unnecessary Medicaid claims of more than \$5 million annually. Although the division's TPL vendor may detect these errors and recover some of the payments, Medicaid would still pay up to \$500,000 annually in avoidable fees. This problem has been occurring for years and should be addressed in a future enhancement project by the division.

Medicaid Overpayments

The division, in most cases, reimburses hospital claims under the Diagnosis Related Groups (DRG) rate, which is a patient classification system in which cases are grouped by shared characteristics of principal diagnosis, secondary diagnosis, age, surgical procedure and other complications, and consumption of a similar amount of resources. In most cases, the division is paying less than the amount billed on the claim, because the DRG rate is less than the amount billed. However, we found \$5 million of claims, over a two-year period, where the DRG amount paid by the division was greater than the amount billed. Medicaid should pay the least amount possible between the DRG rate and the amount

DEPARTMENT OF HUMAN SERVICES
DIVISION OF MEDICAL ASSISTANCE AND HEALTH SERVICES
THIRD PARTY LIABILITY PROCESS

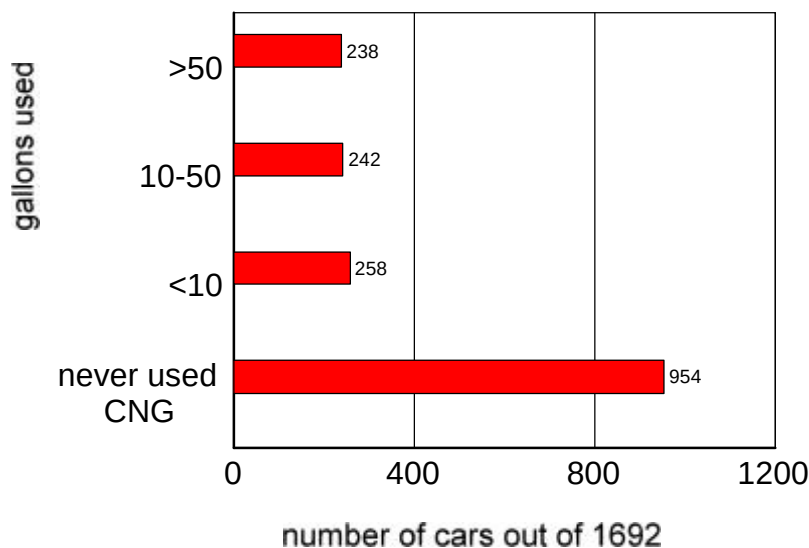
billed.

Fuel Use of CNG Vehicles

Goals of the program were to reduce petroleum usage and thereby improve the air quality through the use of compressed natural gas (CNG). We found that the state is not accomplishing this objective because alternate fuel vehicles (AFVs) are only using CNG four percent of the time over the vehicle's lifetime.

As of November 2002, 56 percent of the state's dual-fuel cars had never been filled with CNG and operate exclusively on unleaded gasoline. This represents a small improvement from July 2000 when it was 73 percent. However, 250 vehicles (15 percent) used less than 10 gallons of CNG throughout their lifetimes. As a result, the state incurred \$6 million in incremental costs for AFVs being operated on gasoline from which it received no environmental benefit. When New Jersey resumes the vehicle life cycle replacement program and purchases 700 AFVs annually, the projected non-beneficial incremental costs for those vehicles would be \$ 2.5 million yearly based on current usage rates.

Dual Fuel Vehicles Lifetime Usage through November 2002



The major contributing factor to the under-utilization of CNG continues to be the lack of fueling stations. As of the end of our field work, there were only three refueling stations for New Jersey's fleet of AFVs; one located at the Department of Transportation in the Trenton area, one in Wall Township, and the other in Hackensack. The Wall Township and Hackensack facilities have limited access and, combined, provided fuel for only 25 vehicles. In addition, the Trenton station can not meet current demand. According to the Advanced

Technology Vehicle Task Force, which was created by the Governor's executive order, the estimated cost to upgrade the Trenton facility to a larger capacity will range from \$600,000 to \$850,000.

Due to the cost, efforts were made by state officials to utilize existing federal, local, and private facilities. However, minimal success occurred as a result of those efforts. Since our last report, the state received \$1.1 million through federal sources to build fueling stations. The task force in August 2000 developed a priority list of refueling locations required to meet the state's immediate needs. The top three locations were Hamilton, Cherry Hill and an upgrade of the Trenton station. The station located in Hamilton is near completion with a cost in excess of \$600,000. The facility at Cherry Hill, which has cost the state in excess of \$300,000 to date, is currently in the construction bidding phase. There remains insufficient funding to upgrade the Trenton station.

Cost Savings Alternative

Federal regulations provide for temporary relief from the purchase of AFVs while continuing to meet its mandate. Relief is granted on a per year basis and takes the form of either exemptions or credits. New Jersey has taken minimal action to relieve the burden of purchasing vehicles while continuing to comply with the mandate since our last report. By increasing efforts to utilize credits and implementing additional alternatives, such as purchasing ethanol fueled vehicles, cost savings to the state could be realized and still comply with the program regulations. The following options were available to New Jersey.

Exemptions can be granted in areas where the alternative fuel is not available to the fleet as a result of one or more of the following reasons: 1) distance from the vehicle location, 2) lack of station accessibility, and 3) unreasonable amounts of time necessary to travel in order to refuel. In addition, exemptions can be granted in cases where the make and model of the vehicle has no similar AFV manufactured. New Jersey has not availed itself of this option.

AFV credits are accumulated when the minimum federal purchase requirements have been exceeded for any given model year. New Jersey has amassed these credits due to their commitment to exceed the minimum. Since our last report, the state applied 160 credits during their model year 2001 acquisitions. However, they continue to have a balance of 80 banked credits that can still be utilized.

The Energy Policy Act of 1992 (EPACT) allows for the buying and selling of AFV credits between qualifying fleets. Those credits can be used to offset future year purchase requirements. Our research indicates that the market price to purchase credits from others is significantly less than the incremental cost required to purchase an AFV. New Jersey has not availed itself of the option to purchase credits from others.

EPACT allows states to earn AFV credits for using biodiesel fuel (fuels derived from biological materials mixture) in medium and heavy duty vehicles. Those credits can then be used to offset current year purchase requirements up to 50 percent of the total. Consideration should be given to increasing biodiesel usage when New Jersey resumes the life cycle vehicle replacement program.

Based upon the estimated usage of 1.3 million gallons of diesel fuel annually, New Jersey could be eligible for over 575 AFV credits each model year by converting from diesel to biodiesel with a potential cost avoidance of \$2.1 million. Effective model year 2001, New Jersey began applying credits earned against AFV purchase requirements based upon biodiesel usage. However, the credits earned were minimal.

New Jersey selected CNG as its alternative fuel even though other types of AFVs are available, such as those that operate on ethanol. Vehicles which operate on ethanol have no incremental purchasing cost. Currently there are no ethanol fueling stations in New Jersey. Our research indicates that the cost to build such a facility ranges from \$40,000 to \$150,000, which is significantly less than a CNG refueling station.

Best Practices

The State of New Jersey is one of four states, along with the federal government, that has a continuation of pay program for injured employees to collect full wages. New Jersey's program is, by far, the most generous with a one year benefit time. The federal government has a 45 day benefit time and the other states follow with 22, 21, and 7 days. This continuation of pay program cost New Jersey \$6.8 million in fiscal year 2002. The state could have saved \$2 million and provided similar services and benefits if its Workers' Compensation (WC) Program was used. This savings represents the difference between the taxable Sick Leave Injury (SLI) benefit versus the non-taxable WC benefit. Additional savings of \$500,000 would be realized from the employer share of payroll taxes.

The matrix below shows the impact of weekly benefits at various salary levels. Those making \$50,000 or less would take home about the same amount since taxes and deductions would not be taken from the WC benefits. This change would most effect those making more than \$50,000 since there is a \$629 weekly cap on WC benefits. Historical data shows only 14 percent of state employees on SLI are in this category and the average benefit time is only 24 days.

Weekly Take Home Pay

Status	Married	Single	Married	Single	Married	Single	Married	Single
Salary	\$30,000	\$30,000	\$40,000	\$40,000	\$50,000	\$50,000	\$60,000	\$60,000
*SLI take home	\$461.17	\$419.43	\$595.61	\$535.46	\$672.45	\$635.15	\$800.47	\$740.08
WC take home	\$396.67	\$398.86	\$530.77	\$532.96	\$623.37	\$625.56	\$623.37	\$625.56

*The SLI take home amounts are not reduced by union dues, additional health benefit costs, deferred compensation etc.

Accounts Receivable

The department disbursed over \$140 million of federal Section 8 Tenant Based Assistance program funds and \$4.5 million of state Homelessness Prevention Program (HPP) funds during fiscal year 2002. As a result of incomplete accounts receivable record keeping there are \$1.9 million of receivables currently deemed uncollectible.

Treasury Circular Letter 03-06-OMB requires the agency to maintain an internal control system which is adequate to effectively collect the amounts due to the agency, track the age of accounts, and to flag delinquent accounts. The details of our audit of the accounts receivable for several programs are presented below.

Rental Assistance Program

The Department of Community Affairs (DCA) administers the Section 8 Tenant Based Assistance Program through a grant from the United States Department of Housing and Urban Development. The purpose of the program is to make housing available to low-income families in the private rental market. Households that meet eligibility requirements normally pay no more than 30 percent of their adjusted monthly income towards their rent and utility costs. The program pays the balance of the rent directly to the landlord of the property. During fiscal year 2002, DCA received and expended in excess of \$140 million in accomplishing this objective.

Monies are due from landlords who were overpaid due to tenants vacating apartments prior to the end of the lease, and from tenants under-reporting income and/or damaging rental units. Our review indicates certain receivables can not currently be collected due to insufficient record keeping practices. We identified 1,175 overpayments representing in excess of \$800,000 in landlord receivable accounts and another 302 tenant receivables approximating \$160,000 that are currently uncollectible due to missing or incomplete debtor information. The missing information on many of these receivables may reside on archived data tapes that can be retrieved with the help of the state's Office of Information Technology (OIT). We made this observation to DCA management and they have contacted OIT to determine the details and extent of the recovery process. The department has implemented a new software application that may correct the above noted deficiencies.

There is a program within the Section 8 grant known as Family Self Sufficiency (FSS). An FSS participant may, under certain circumstances, receive a monthly escrow account credit over a five-year period. Upon completion of a contract of participation the successful candidate receives in cash the value of the accumulated credits. Our review identified nine individuals who owed the program money due to previous damage claims that were not offset against the escrow payment. We also noted two FSS graduates who received in excess of \$10,000 more than they were entitled to because the monthly credits continued even though their contracts had been completed.

Homelessness Prevention Program Loans

The Prevention of Homelessness Act of 1984 appropriated to the Department of Community Affairs \$1.65 million for rental and mortgage assistance grants to municipalities, and loans and grants to qualified applicants who face imminent eviction or foreclosure. Repaid loans are to be deposited into the account to be used to assist future applicants. The program has continued to be funded through an annual appropriation of \$4.5 million. In fiscal year 2002 there were \$2.8 million in grants to individuals, \$1.3 million in grants to municipalities and non-profits, and \$400,000 in loans to individuals.

In 1986, the department initiated an undocumented change in policy reclassifying loans to grants for first time recipients of rental assistance payments. Mortgage assistance payments and those receiving rental assistance payments two or more times are considered as loans that must be repaid. In May 2002, \$430,000 in loans issued between 1984 and 1986 were converted to grants. The actual amount converted to grants can not be determined by management due to incomplete information.

Loans for rental assistance totaled \$2.3 million as of January 10, 2003. Mortgage assistance loans expected to be repaid as of this date also approximate \$2.3 million.

Our audit disclosed the department's record keeping practices have resulted in the inability to submit for collection \$1 million of loans due to insufficient or missing information. As in the case of the Rental Assistance loans, information recovery is attainable using OIT and by conducting a thorough review of existing files. Our audit has identified specific loans and has made that list available to the department. Accordingly, the department has been in contact with OIT regarding these loans and is in the preliminary stages of retrieving the missing information.

Personal Care Assistant Services

Medicaid recipients can receive personal care assistant (PCA) services if they need help performing personal care, health related tasks and household duties. A physician must determine an individual's need for these services which are provided by private vendors. The Division of Disability Services administers the PCA program which expends \$231 million a year. Vendors providing the care determine the level of service needed on a case-by-case basis. The division can better monitor the program to ensure vendors are not providing more hours of service than are needed.

The division implemented a pilot project in 1998 to monitor cases in five counties. Temporary nurses were hired to perform independent assessments of the level of service provided. Within a three-year period the nurses reduced the number of hours of care needed in 4,100 of 17,000 cases they reviewed. This resulted in a reduction in hours claimed by providers which potentially saves the program \$1 million a year. Due to staffing constraints, the division is unable to continue the pilot program or to expand it statewide. If providers are not adequately monitored, the savings achieved by the pilot project might decrease.

The division's internal policy Number 62: Volume 8 requires providers in the pilot project counties to complete a prior authorization form for all cases. We noted 37 percent of our test cases in one county did not have the required form. Without the prior authorization form, the division cannot properly monitor these claims.

The division does not require sufficient information to analyze claims for certain correlations or trends. For example, we noted the system did not identify the referring physician for 95 percent of total claims paid. We further noted the system identified the attending physician as the personal care provider in all cases. Complete and accurate physician information could be helpful in determining if relationships exist between certain physicians and PCA providers.

Transportation - Mobility Assistance Vehicle Services

The Division of Medical Assistance and Health Services (DMAHS) provides transportation services to Medicaid recipients who need medical services. Private vendors provide the transportation by ambulance, mobility assistance vehicle (MAV) and several lower modes. Medicaid transportation programs expend \$57 million a year, \$39.8 million of which is spent on MAV services, including \$11 million for mileage. Medicaid recipients who are not ambulatory can use MAV if they receive prior authorization from the division. Vendors are paid for providing transportation to and from a medical facility and for mileage. Our review of MAV claims noted internal control weaknesses that increase the risk of overpayment.

- The division is converting to electronically submitted claims which are not accompanied by the transportation certification form which contains the trip

destination and various signatures. This form is retained by the vendor. Without going to the vendor, there is no way to verify the claim destination matches the previously authorized destination, the service was actually received, or the mileage was reasonable.

- Vendors overbilled the division \$134,000 by erroneously entering an additional payment code on the claim. The system paid the vendors for three one way trips instead of one round trip.
- The system allowed vendors to be paid twice for the same service. During fiscal year 2002 there were \$250,000 in claims that were potential duplicates. We tested 99 multiple payments (\$4,950) with the same service date and noted 12 duplicates totaling \$600.

We also noted cost savings can be achieved by changing the rate structure for mileage paid to MAV and ambulance providers. Currently the rate is \$1.50 per mile for the first 15 miles and \$2.00 per mile from the first mile for trips of 16 miles or more. This adds \$7.50 to each claim over 15 miles. By changing the rates for longer trips to \$1.50 for the first 15 miles, the division would reduce MAV costs by \$738,000 a year.

Accounts Receivable

According to N.J.S.A. 2C:43-3.3, any person convicted of a crime on or after January 9, 1997 is to be assessed a mandatory \$30 penalty for each offense. This penalty is not discretionary and the standard language on every Judgement of Conviction (JOC) document makes the penalty applicable to every person convicted of an offense since 1997. These monies are to be deposited into the Law Enforcement Officers Training and Equipment Fund (LEOTEF). We noted the penalty is not recorded by the department unless the \$30 is specifically marked on the JOC by the Administrative Office of the Courts (AOC). From January 9, 1997 to July 29, 2003, approximately 26,000 inmates were convicted of more than 63,000 offenses. Only 28 percent of these offenses were assessed the mandatory \$30 penalty. We estimate the department has not recorded for recovery \$1.4 million in penalties on inmate records.

Forfeiture Program Financial Activity

Funds seized by state law enforcement agencies, where the state will be the prosecuting agency, are deposited into a series of cash management accounts where they accumulate interest awaiting disposition. These cash management accounts are administered by the Division of Criminal Justice's Property Management Office (PMO). Dispositions of the principal amounts seized, upon the case being closed, include returning it to the claimant, sharing it with other law enforcement agencies, releasing it for restitution in related criminal matters, and depositing it into the Attorney General's Law Enforcement Forfeiture Account (AGLEFA). Interest earnings are retained by the state and separately deposited into the Asset Maintenance Account (AMA). The AGLEFA and AMA accounts represent the aggregate available for the administration of the forfeiture program and provide a supplemental source of funding for various law enforcement programs, including witness protection, confidential investigations, and enhancing the computer-aided dispatching system. An additional program supported by the fund is the Hepatitis Inoculation Program administered by the Department of Health and Senior Services. Our review of these accounts as of June 30, 2002 revealed the following issues related to the finances of this program:

- a) Three accounts totaling \$896,000 as of June 30, 2002 included \$534,000 in interest which had accumulated over a number of years. In addition, the division could not identify balances of \$195,000 as to ownership of the funds. The interest and unidentified funds should have been transferred to the AMA and the state's unclaimed personal property fund, respectively. The transfer of the interest on a regular basis would have resulted in additional funds for the program or lapsed to the General Fund.
- b) Twenty-nine cash management accounts with cases ranging from 7 to 15 years old had balances totaling \$383,000. The division could not determine if the cases should be closed and transferred to either AGLEFA or the state's unclaimed personal property fund. These cases should have been processed in a more timely manner.
- c) Fringe benefits of employees working on the program were not reimbursed to the state as required by Treasury Circular Letter 96-16. In addition, we found no evidence that a waiver from this requirement had been obtained by the division. For the period July 1, 2000 to June 30, 2002 \$137,000 should have been reimbursed.

Abbott Preschool Program Budgeting and Funding Process

N.J.A.C. 6A:24-3.3 required full-day, full-year early childhood education be made available to three and four-year old children in Abbott districts by the 2001-2002 school year. The program is required to be adequately funded based on the demonstrated need of the community and the Department of Human Services (DHS) providers. Districts requested funding for the educational component of their preschool programs through the submission of an Operational Plan to the Department of Education (DOE). The line item budget requests contained within the Operational Plan are primarily based on the projected preschool enrollment.

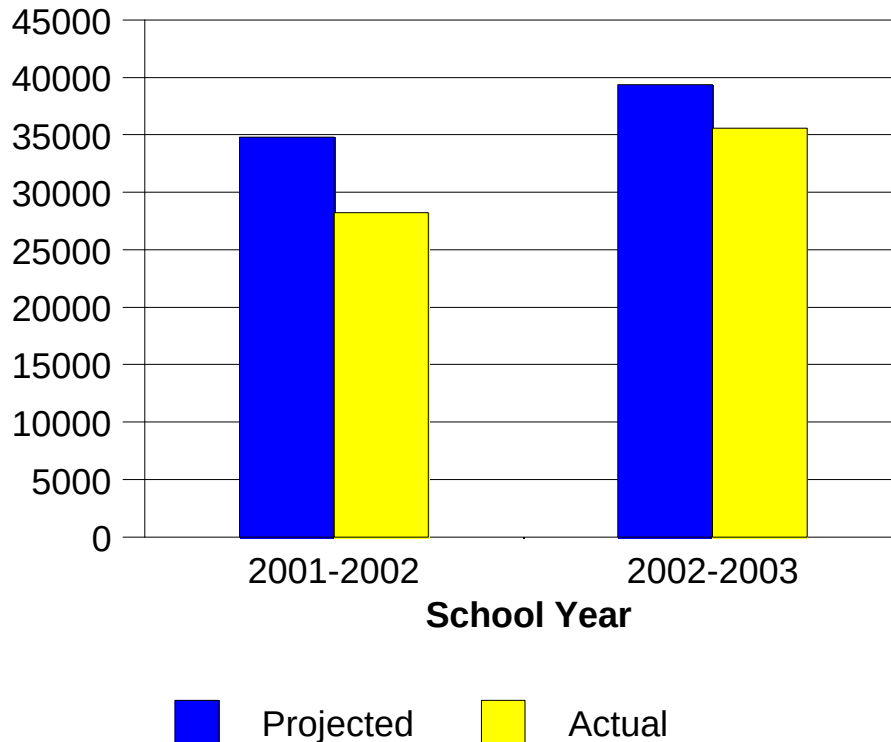
The actual cost of the preschool program must be determined and monitored to accurately project future funding needs and reduce the chance of misappropriation. Financial reporting for the early childhood programs consists primarily of the annual school district financial statement audits that are performed by independent accountants hired by the local school boards. The audit reports include a Statement of Early Childhood Program Aid which compares budgeted and actual expenditures in total. Individual program expenditures including the preschool program are not identified. The DOE does not require districts to report the actual cost of the programs and therefore cannot conclude on the effectiveness of the preschool program budgetary process. The DOE should have controls in place to determine if district budgets were reasonable. These controls should be able to detect deviations from the budget. Each district budget could be periodically compared to actual expenditures to help ensure that resources are not being misused. If expenditures are less than expected, it may indicate that program objectives are not being met. Budgetary control is important for ensuring that the DOE's resources are appropriately allocated.

In fiscal year 2003, the state made available an additional \$142 million in preschool expansion aid to the Abbott districts because the amount appropriated for Early Childhood Aid did not increase from fiscal year 2002. This appropriation funded the increase in the approved budgeted preschool costs from fiscal year 2002 to fiscal year 2003. The rationale of a funding methodology that is based on a comparison of budgeted amounts without considering actual expenses is questionable in this circumstance as the DOE has not implemented procedures to ensure the validity of their budgetary process. As previously mentioned, actual program expenditures are not compared with budgeted amounts.

Furthermore, the preschool budgets are based on projected enrollments which have proven to be overstated. The overall program enrollment was 19 percent less and 10 percent less than projected in school years 2001-2002 and 2002-2003, respectively.

ABBOTT DISTRICT PRESCHOOL PROGRAM

Actual vs. Projected Enrollments



Provider Budgets and Financial Records

In school year 2001-2002, the approved preschool budgets for the Abbott districts totaled \$237 million, of which approximately \$100 million was for contracts with community providers for the educational component of the program. Community provider budgeted costs increased by \$112 million in school year 2002-2003 to \$212 million.

As part of the contracting process, providers are required to submit zero-based budgets and accompanying schedules which reflect the actual cost of delivering the education program. The districts are responsible for ensuring that provider budgets are reasonable based upon a needs-based analysis. The budgets are submitted to the DOE as part of the districts' annual operational plans. Our review noted that the districts were requesting funding from the DOE through their operational plans without properly assessing the needs and circumstances of providers. We found that the provider budgets at two of the six districts reviewed were not the basis for the per pupil payments but in fact each district had negotiated per pupil rates. Because of this funding process, seven providers in one district were paid approximately \$215,000 more than the budgeted cost of delivering the service

in school year 2001-2002. Another district appeared to determine an amount to award each provider and then adjusted the budget rather than using the budget itself to determine the award.

The districts' abilities to determine a provider's actual costs and assess need is further hindered by inadequate record keeping and financial records. The Abbott preschool contracts require providers to maintain a financial management system that provides for accurate, current, and complete disclosure of all financial activity. These records are to be made available for inspection by the district, the state and/or their designee. However, formal procedures for the review of provider program costs have not been provided to the districts by the DOE. We reviewed the financial management systems of 26 providers in the six audited districts and found that the providers were unable to determine the actual cost of their early childhood programs. Specifically, we noted:

- Two of the providers had no financial management systems or financial statements. These providers accounted for both educational services and wraparound day care in one checking account. Evidence of revenue and expenditures for one provider could only be found through canceled checks and bank statements. No documentation to support program revenue and expenses was provided by the other provider but a review of their files indicated serious concerns relating to their viability. Federal and state payroll taxes were not paid for 2001 and portions of 2002. In addition, public utilities and telephone accounts contained past due amounts because of sporadic payments which also resulted in notices to shut off services.
- Provider financial systems that could be reviewed were not maintained in accordance with generally accepted accounting principles, as required. Expenses including staff salaries were not properly allocated between the 180 six-hour days of educational services and the 245 days of wraparound day care services. Financial reports and records at 24 of the 26 providers did not show direct expenses and the allocation of indirect expenses relating to educational services. Expenses were also not properly allocated between school district students and private students. Therefore, the amount and propriety of the costs associated with the program could not be determined.
- We tested program disbursements for proper support documentation and reasonableness and found problems at the majority of providers reviewed. Some payments were not supported by a bill or invoice. These included payments of cellular phone bills, contributions to a family member, credit card payments, payments made to "cash", reimbursements to owners and staff, and payments to individuals for services rendered when they were not on the payroll. There were also no written contracts. We also identified expenses that were not program related, which included payments for back taxes not associated with the program, gift certificates, personal expenses, and donations to churches, civic and miscellaneous organizations.

Program Funding Process

The district's school year 2002-2003 Operational Plan was approved by the state Department of Education (DOE) in the amount of \$19,944,194. The major component of this funding was for contracted services in the amount of \$14,390,695. The district subsequently contracted with providers for \$12,935,050 resulting in excess funds of \$1,455,645. This occurred because contracts with providers were finalized several months after the plan was required to be submitted. The amount was reviewed by DOE and the award was reduced by \$782,550 from \$19.9 million to \$19.1 million. We believe the entire \$1,455,645 to be excess funds.

Among the many itemized costs included in the Operational Plan was \$947,700 for wrap-around care. The district projected this cost in its budget because the services, typically funded by the state Department of Human Services (DHS), could not be guaranteed at the time the budget was submitted. Our audit disclosed DHS will fund this service; therefore, the \$947,700 awarded also represents excess funding. In summary, based upon our review of the district's approved operational plan versus projected costs, it appears the district has been overfunded by approximately \$2.4 million, of which \$782,550 has already been reclaimed by DOE.

Summary

We found the payments to Medical Day Care (MDC) providers were related to the department's programs and were recorded properly in the accounting system. However, we could not determine the reasonableness of the cost of the Medical Day Care Program due to program regulations not adequately defining the population to be served. Without explicit regulations defining the types of medical conditions which warrant MDC services, any medical condition diagnosed by a physician is sufficient to enroll an individual in the program. This program has apparently evolved from providing services as an alternative to nursing home care to providing services to any participant eligible for Medicaid and some providers are actively recruiting from senior housing to fill their allotted slots through the use of advertising circulars and open house visits. Although the department had enacted a moratorium on licensing new facilities, we found that providers who had filed their applications prior to the moratorium were still being processed for licensure. As of February 2003, 52 new facilities with a capacity of 5400 slots have been approved. This could increase the program's participants by approximately 70 percent and program expenditures by \$60 million. Existing regulations should be redefined to clearly state eligibility requirements for participation in MDC services. Participants not eligible for MDC services could be referred to programs requiring less intensive medical services.

In making this determination, we also found the department needs to implement controls over provider reimbursements to prevent improper payments from being processed. In addition, the department needs to improve its program oversight function.

Business Continuity and Disaster Recovery

The division processes revenue and the related documentation for many state agencies. The capability to process this revenue and data is important to state operations. Therefore, procedures must be in effect to safeguard information resources, minimize the risk of unplanned interruptions, and enable the recovery of critical operations in the event such interruptions occur. This comprehensive business continuity plan should address all potential disruptions to division operations. We found the division's disaster recovery plan and capabilities to be inadequate, and we have provided the department and division with further technical detail to allow them to address these issues.

Funds Kept in Hold Status

Child Support cases can be placed in hold status for a variety of reasons such as inability to find the absent or custodial parent, lack of court order for emancipating the child, or removal of the child from public assistance grants. Once a case has been placed in a hold status, funds collected will not be disbursed. During our audit period 6,600 cases with balances totaling \$3.4 million were maintained in this status. Balances from 700 cases totaling \$1 million have been in this status for a period exceeding one year. These funds belong to one of the principals involved in the case. Failure to restore these cases to active status deprives the rightful recipient use of their funds. Another 700 cases have been in a hold status for a period in excess of a year where no funds have been collected.

We reviewed the records for 74 of the cases over one year old where funds had been collected. In 21 cases, some dating back to 1993, there was no evidence of any enforcement activity. Cases maintained in a hold status require the same constant monitoring as active cases. This effects the probation unit's ability to effectively administer and enforce court issued support orders. It could also adversely affect performance indicators which could reduce federal incentive payments to each vicinage.

Administrative Office of the Courts (AOC) Directive 1-91 provides instruction to the vicinages on how to file a motion with the court to terminate its continuing supervision while a support order remains in effect. Filing such a motion allows any amount held to be disbursed to the rightful owner and removes the program's supervising responsibility. The rights and responsibilities of any party involved are not altered by this action. Only Mercer, of the nine counties tested, indicated they had implemented this directive.

Controls Over Cash

The postal service returns child support payment checks to the counties when the intended recipient no longer resides at the address on the payment envelope. Our test of 15 counties indicated procedures concerning these checks varied not only from vicinage to vicinage, but also among counties located within the same vicinage. Additionally, while some counties, such as Burlington, maintained adequate records and controls, others did not. Ten counties did not maintain a log listing returned checks and whether or not these checks were voided or remailed. Two counties kept returned and voided checks in an open box. One county did not stamp void or in any other way indicate on a check that it had been voided. This county was unable to locate 22 voided checks. None of the missing checks had been cashed at the date of our tests. The issue of missing void checks has been turned over to the AOC internal audit unit for investigation.

While the majority of child support payments are received at the central processing center, vicinages collect approximately \$5.6 million annually. Procedures concerning these collections varied not only from vicinage to vicinage but among counties located within the same vicinage. Additionally, while some counties maintained adequate records and

controls, others did not. Four counties did not maintain logs showing checks received. Two counties did not reconcile cash receipts to the register, nor send them to the central processing center on the day they were received. Two counties did not issue receipts when payment was made by check. Three counties did not identify the cashier accepting payments.

Strong internal controls are necessary to assure adequate safeguarding of assets reducing the chance of loss or use in an unauthorized manner. This is extremely important when dealing with fluid assets such as cash or checks.

**OFFICE OF LEGISLATIVE SERVICES
OFFICE OF THE STATE AUDITOR
SCHEDULE OF REPORTS ISSUED DURING 2003**

<u>REPORT</u>	<u>TYPE OF FINDINGS</u>			
	<u>COMPLIANCE</u>	<u>CONTROLS</u>	<u>ECONOMY/ EFFICIENCY</u>	<u>NONE</u>
Casino Control Fund		OPINION ONLY		
Department of Community Affairs				
Housing Assistance and Inspection Programs	X	X	X	
Department of Corrections				
Administration	X	X	X	
Department of Education				
City of Camden Board of Education				
Early Childhood Education Program	X	X		
City of East Orange Board of Education		X	X	
City of Passaic Board of Education		X		
City of Paterson Board of Education	X	X		
Early Childhood Education Program	X	X	X	
Jersey City Public Schools	X	X	X	
Newark Public Schools		X	X	
Pleasantville Board of Education				
Early Childhood Education Program	X	X	X	
Trenton Board of Education				
Early Childhood Education Program	X	X	X	
Department of Health and Senior Services				
Division of Consumer Support				
Medical Assistance to the Aged				
Medical Day Care Program	X	X	X	
Department of Human Services				
Division of Medical Assistance and Health Services, and Division of Disability Services Selected Programs	X	X	X	
Division of Medical Assistance and Health Services Third Party Liability Process	X	X	X	
Department of Law and Public Safety				
Attorney General's Law Enforcement Forfeiture Account	X	X	X	
Division of Consumer Affairs	X	X	X	
Department of Military and Veterans Affairs		X	X	

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SCHEDULE OF REPORTS ISSUED DURING 2003**

REPORT	TYPE OF FINDINGS			
	COMPLIANCE	CONTROLS	ECONOMY/ EFFICIENCY	NONE
Department of the Treasury				
Division of Revenue				
Information Systems		X		
Division of Taxation				
Interest on Late Tax Refund Payments			X	
Rebate Programs				X
Transfer Inheritance Tax Revenues	X	X	X	
Higher Education Services				X
Office of Administrative Law	X	X	X	
Office of the Public Defender		X	X	
Judiciary				
Administrative Office of the Courts		X		
Child Support Enforcement Program	X	X		
Superior Court of New Jersey				
Atlantic and Cape May Vicinage	X	X	X	
Bergen Vicinage				X
Gloucester, Cumberland and Salem Vicinage	X	X	X	
Mercer Vicinage	X	X	X	
Somerset, Hunterdon and Warren Vicinage	X	X	X	
New Jersey Comprehensive Annual Financial Report				
	OPINION ONLY			
Pinelands Commission				
	SINGLE AUDIT REPORT			
Sick Leave Injury Program		X	X	
State of New Jersey				
Alternative Fuel Program			X	
Report on Compliance and Internal Control Related to Our Audit of the State's Comprehensive Annual Financial Report				X