



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

**Department of Education
Marie H. Katzenbach School for the Deaf**

July 1, 2010 to August 31, 2012

**Stephen M. Eells
State Auditor**

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Enclosed is our report on the audit of the Department of Education, Marie H. Katzenbach School for the Deaf for the period of July 1, 2010 to August 31, 2012. If you would like a personal briefing, please call me at (609) 847-3470.

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

Stephen M. Eells
State Auditor
January 9, 2013

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Scope

We have completed an audit of the Department of Education, Marie H. Katzenbach School for the Deaf for the period July 1, 2010 to August 31, 2012. Our audit included financial activities accounted for in the state's General Fund and the school's Student Activity Fund.

Expenditures totaled \$16.6 million in fiscal year 2012. Marie H. Katzenbach School for the Deaf is under the direction of the Department of Education. The primary responsibility of the school is to provide academic, career, and technical educational services to deaf and multiply disabled deaf children from birth through twelfth grade. The school served 168 students in school year 2011-2012 which includes 74 students who participated in the residential program. Revenues were \$11.5 million in fiscal year 2012 of which the major component is tuition paid by local school districts from which the student resides. An additional \$0.8 million of Department of Education federal revenue funds programs at the school. The annual appropriation from the state is \$3.6 million. Prior year unexpended funds totaling \$5.2 million were carried forward into fiscal year 2012 and appropriated for school operating expenses.

Objectives

The objectives of our audit were to determine whether financial transactions were related to the school's programs, were reasonable, and were recorded properly in the accounting systems. We also tested for resolution of the significant conditions noted in our prior report dated March 23, 2006.

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 school. Provisions that we considered significant were documented and compliance with those requirements was verified by interview, observation, and through our samples of financial transactions. We also read the budget messages, reviewed financial trends, and interviewed department and school personnel to obtain an understanding of the programs and 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. Transactions were judgmentally selected for testing.

To ascertain the status of findings included in our prior report, we identified corrective action taken by the school and performed tests to determine if the corrective action was effective.

Conclusions

We found that the financial transactions included in our testing were related to the school's programs, were reasonable, and were recorded properly in the accounting systems. In making these determinations, we noted certain internal control weaknesses and matters of compliance meriting management's attention. We also found that the school has resolved the significant issues noted in our prior report with the exception of a payroll internal control issue which has been updated and restated in the current report.

During the audit, we observed that the campus is too large and inefficient for a student population that has been steadily declining over the years. The department is performing a study to determine a more cost effective manner to meet the students' facility needs. We recommend the department implement a plan that is both cost effective and provides the flexibility to meet the future needs of the declining population.

Internal Controls - Payroll/Personnel

Strengthening internal controls of the payroll/personnel functions may reduce the risk of errors and irregularities.

Payroll expenditures totaled \$12.6 million during fiscal year 2012. The Department of Education, Office of Human Resources processes the school's payroll and maintains leave records for the school's employees. Management is responsible for establishing and enforcing internal controls that safeguard assets from loss or unauthorized use. Maintenance of accurate and current records is necessary to ensure the proper use of resources. We noted the following weaknesses.

Terminated/Inactive Employees on the Payroll

Our review noted that terminated employees were not removed from the active payroll records in a timely manner increasing the risk that inappropriate or erroneous payroll transactions could be processed. We examined the payroll records for all 49 employees who had been removed from the payroll during the audit period and found that 35 had remained on the active payroll records from 2 to 33 pay periods after their separation date or final pay. Additionally, we noted seven employees with temporary positions that had been inactive from 10 to 28 pay periods and a full-time employee inactive for 56 pay periods still on the active payroll records as of June 29, 2012. A full-time employee received a payment of \$1,400 while on a leave of absence without pay. Prior to this erroneous payment, this individual had not been paid for 17 pay periods. Fraudulent or unearned payroll checks may be produced and not detected when inactive or terminated employees remain on the active payroll records. This condition was also noted in our prior report dated March 23, 2006.

Leave Records

Employee leave records were maintained manually by timekeepers through the pay period ending October 7, 2011. Subsequently, all employee leave time is maintained on the electronic Cost Accounting and Timesheet System (eCATS). We noted numerous errors with the employee manual leave balances that were posted to eCATS. Our review of 25 sampled employees disclosed that 21 had one or more incorrect leave balances posted as a result of mathematical errors and improperly prorated leave time allotments. The errors ranged between 0.5 and 21 hours and were not detected because there was no supervisory review of the timekeepers' work.

Recommendation

We recommend that the department's Office of Human Resources establish written policies for the removal of terminated and inactive employees from the active payroll records. In addition, we recommend that the unit perform a review of all employee leave balances that were posted to eCATS and correct any discrepancies.



Repairs and Maintenance of Leased Facilities

Oversight over tenant repairs should be improved.

The school generates additional income from the rental of vacant space. The standard lease is made "by and between the State of New Jersey Department of Education ("Landlord") acting by and through the Department of the Treasury, Division of Property Management & Construction" (DPMC) and the tenant. The lease states that the tenant may deduct the cost of repairs from their monthly rent if the landlord is unable to carry out the repairs in a timely fashion. The lease also states that any repairs performed by the tenant should be approved by the landlord and be in compliance with all federal, state, or local statutes, codes, decisions, regulations, ordinances, rules, or other requirements.

We reviewed rental payments received from one tenant for the period July 2010 to January 2012 and noted they were reduced by \$100,000 for repair costs. We could not verify that the repairs were approved by the department or DPMC in advance because the tenant was only required to obtain verbal approval from the school's management. In addition, we found that \$56,000 of these repairs did not have evidence of price competition as required by Circular Letter 11-10 DPP "Delegated Purchasing Authority". Enforcing compliance with procurement regulations may reduce costs and enhance rental income.

Recommendation

We recommend that the department develop a formal written policy for the approval of facility repairs and maintenance that are performed by a tenant. The policy should require the tenant to obtain written authorization from the department in advance of any work being completed and if applicable, obtain price competition as required by Circular Letter 11-10 DPP "Delegated Purchasing Authority". The policy should further require the DPMC to review all transactions over an established dollar threshold.



Temporary Appointments

Established regulations should be followed when using temporary appointments.

Pursuant to New Jersey Administrative Code (N.J.A.C.) 4A:4-1.7, temporary appointments may be approved for positions in which the job assignment is for an aggregate period of not more than six months in a 12-month period. In accordance with the Civil Service Commission, hours worked within the 12-month period may not exceed 944, unless an exemption is provided for the position.

The school employed approximately 50 temporary employees in fiscal years 2011 and 2012. We calculated the total hours worked for each employee and found that 21 employees exceeded the 944 hour limit in fiscal year 2011 and 19 employees exceeded the 944 hour limit in 2012. At least eight employees exceeded 1,400 hours worked in both fiscal years including one employee who worked over 2,200 hours in each year. The Civil Service Commission has provided an exemption for those positions that provide specialized aid and one-on-one services to the children. However, our review of fiscal year 2012 disclosed five temporary employees working in non-exempt positions that exceeded 1,200 hours worked.

Pursuant to N.J.A.C. 4A:3-5.5, temporary employees shall be entitled to overtime compensation at the rate of one and one-half times their regular rate for time worked in excess of 40 hours per week. Our review of five temporary employees who worked over 1,900 hours in fiscal year 2012 disclosed that they were not compensated at overtime rates for time worked in excess of 40 hours in a week.

Recommendation

When using temporary employment services, applicable guidelines concerning time worked and compensation should be followed. Employees who were entitled to overtime compensation should be retroactively compensated. In addition, the department should attempt to establish permanent positions where deemed appropriate.



Storeroom Inventory

Training in supply inventory record keeping is needed.

In February 2012, the school began using a new inventory system for clerical, janitorial and school supplies. The supplies are located in a centralized storeroom from which electronic orders are received from various locations across the campus. We performed a physical count of the supplies and found numerous discrepancies between amounts on hand and the amounts recorded in the system. Overall, the physical count of \$121,000 exceeded the system records by \$25,000. Inaccurate inventory records could cause purchasing inefficiencies, supply shortages,

spoilage, and an increased risk of items being stolen without detection. Because the system is relatively new, responsible staff was unfamiliar with the proper procedures that would have created accurate inventory records.

Recommendation

We recommend that the staff responsible for maintaining the inventory system receive additional training on proper inventory procedures. In addition, physical counts should be performed periodically and any variances properly resolved.



Student Activity Fund

Student Activity Fund internal control procedures need to be strengthened.

The school has established a student activity fund for various extracurricular activities that benefit and serve the student population. Funding is primarily received through donations and fundraising events. During fiscal years 2011 and 2012, fund disbursements totaled \$34,600 and \$42,900 respectively. The fund's standard operating procedures state that "All disbursements must be supported by a receipt, claim or company invoice." Our review found that these procedures were often not followed so payments could be processed expeditiously. Specifically, our test of 57 fund disbursements found a lack of supporting documentation for 15 transactions totaling \$10,900. These payments included a total of \$4,800 to eight employees for services rendered that should have been processed through payroll to allow for applicable payroll taxes. Additionally, we noted a segregation of duties weakness as the same individual who prepares the monthly reconciliations for the account also maintains possession of the checkbook. The lack of compliance to procedures and inadequate internal controls could lead to the misuse or misappropriation of funds.

Recommendation

We recommend that all fund disbursements be properly supported by the required documentation. We further recommend that payments to employees for services rendered be made from the appropriate payroll account, with reimbursement from the student activity fund processed afterward. Additionally, we recommend that the checkbook be maintained by someone other than the individual who prepares the reconciliation.



Observation

Campus

Marie H. Katzenbach School for the Deaf was founded in 1883 and is currently located on approximately 110 acres of land. Until 1952, the facility was situated on approximately 70 acres of land when the school acquired an additional 40 acres to meet the needs of a student population that had grown to nearly 600. School enrollment, however, has declined steadily over the years, resulting in a facility that is too large and inefficient for its current population.

The school's enrollment has declined from 203 students in school year 2008-2009 to 168 in school year 2011-2012. The declining enrollment is partially attributable to higher functioning students as a result of medical advancements and earlier diagnosis. With the aide of cochlear implants and other medical innovations, many students can now be taught in their home school district. As a result of the declining enrollment, the school's facilities and grounds are vastly underutilized. The school offers a four night a week residential program and has eight dormitory buildings that can accommodate approximately 369 students. During school year 2011-2012, the residential student enrollment of 74 students represented only 20 percent of capacity. In addition, the campus has several buildings that are only partially used or not used at all. Also, although enrollments have decreased 17 percent over the last three years, the school's expenditures have increased 9.2 percent over the same period.

The Department of Education, in conjunction with the school's administration, is currently performing a study to determine a more cost-effective manner to meet the students' facility needs.

We recommend the department implement a plan that is both cost-effective and provides the flexibility to efficiently meet the future needs of the school's declining population. A change in location should be considered.



State of New Jersey

DEPARTMENT OF EDUCATION

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CHRIS CHRISTIE
Governor

KIM GUADAGNO
Lt. Governor

CHRISTOPHER D. CERF
Commissioner

January 8, 2013

Mr. Stephen Eells, State Auditor
Office of Legislative Services
Office of the State Auditor
125 South Warren Street
P.O. Box 067
Trenton, NJ 08625-0067

Dear Mr. Eells:

Subject: Response to OLS Audit Report of the Department of Education, Marie H. Katzenbach School for the Deaf

The New Jersey Department of Education (DOE) has received and reviewed the findings and recommendations contained in the Office of Legislative Services (OLS) Audit Report of the Department of Education, Marie H. Katzenbach School for the Deaf for the period July 1, 2010 to August 31, 2012. The findings, recommendations and observation at pages 3 through 7, along with our responses are as follows:

Summary of Finding, Page 3

Internal controls – Payroll/Personnel. Terminated/Inactive employees were not removed from the active payroll records in a timely manner increasing the risk that inappropriate or erroneous payroll transactions could be processed.

Leave records. The auditors noted numerous errors with the employee manual leave balances that were posted to the e-CATS.

Recommendation

We recommend that the department's Office of Human Resources establish written policies for the removal of terminated and inactive employees from the active payroll records. In addition, we recommend that the unit perform a review of all employee leave balances that were posted to eCATS and correct any discrepancies.

Department Response

We agree during Marie H. Katzenbach School for the Deaf's migration to the electronic timekeeping system eCATS, inactive employees were removed from the payroll. To continue this practice, management at the school must complete and forward a Personnel Action Request

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form prior to the resignation or termination of employees. Following these established guidelines will remove the employees from the payroll in a timely manner. This will alleviate the risk for inappropriate or erroneous payroll actions.

Additionally, the Office of Human Resources has begun an audit of all Marie H. Katzenbach School for the Deaf employee leave balances with specific emphasis to leave balances that were posted to eCATS. This process will determine any discrepancies and corrections will be made.

Summary of Finding, Page 4

Repairs and Maintenance of Leased Facilities – Oversight over tenant repairs should be improved.

Recommendation

We recommend that the department develop a formal written policy for the approval of facility repairs and maintenance that are performed by a tenant. The policy should require the tenant to obtain written authorization from the department in advance of any work being completed and if applicable, obtain price competition as required by Circular Letter 11-10 DPP “Delegated Purchasing Authority”. The policy should further require the DPMC to review all transactions over an established dollar threshold.

Department Response

We agree and will develop a formal written policy with the approval of DOE.

Summary of Finding, Page 5

Temporary Appointments – Established regulations should be followed when using temporary appointments. Five temporary employees who worked over 1,900 hours in FY2012 were not compensated at overtime rates for time worked in excess of 40 hours in a week.

Recommendation

When using temporary employment services, applicable guidelines concerning time worked and compensation should be followed. Employees who were entitled to overtime compensation should be retroactively compensated. In addition, the department should attempt to establish permanent positions where deemed appropriate.

Department Response

We agree the Office of Human Resources reviewed the payroll and converted all appropriate per diem employees to hourly positions. This will enable proper compensation of all overtime hours worked. The Office of Human Resources has begun an audit of payroll records to determine

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which hourly employees are entitled to overtime payments. Once the hourly employees that are entitled to overtime are identified, the Office of Human Resources will begin to issue payments.

We disagree with adding additional permanent positions due to the fiscal constraints placed on the Katzenbach budget with regard to full-time equivalents.

Summary of Finding, Page 5

Storeroom Inventory – Training in supply inventory record keeping is needed. A physical count of supplies revealed discrepancies between amounts on hand and the amounts recorded in the system.

Recommendation

We recommend that the staff responsible for maintaining the inventory system receive additional training on proper inventory procedures. In addition, physical counts should be performed periodically and any variances properly resolved.

Department Response

We agree, and we will arrange for training on proper inventory procedures. Additionally, we will establish policy for regular inventory counts.

Summary of Finding, Page 6

Student Activity Fund – Student Activity Fund internal control procedures need to be strengthened. Several disbursements were not supported with a receipt, claim or company invoice, which caused delays in processing payments.

Recommendation

We recommend that all fund disbursements be properly supported by the required documentation. We further recommend that payments to employees for services rendered are made from the appropriate payroll account, with reimbursement from the student activity fund processed afterward. Additionally, we recommend that the checkbook be maintained by someone other than the individual who prepares the reconciliation.

Department Response

We agree and have taken steps to insure that all fund disbursements are properly supported by the required documentation and future employee payments for services rendered are made from the appropriate payroll account.

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OLS Observation, Page 7

The observation addresses the use of the campus facility. It notes the school's declining enrollment and that the DOE, in conjunction with the school's administration, is currently performing a study to determine a more cost-effective manner to meet the students' facility needs.

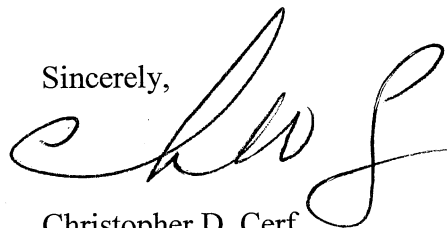
The auditors recommend the department implement a plan that is both cost-effective and provides the flexibility to efficiently meet the future needs of the school's declining population. A change of location should be considered.

Department Response

We agree with the recommendation including examining all alternatives to ensure that the educational needs of the school's population are met.

We trust that our responses satisfy the concerns raised in the audit report. Should you have any questions or need further information, please contact Angel Ramos at 609-530-3112.

Sincerely,



Christopher D. Cerf
Commissioner

CDC/DC/BG/AR/Revised Final DOE Response to OLS Audit of Katzenbach School 2012.doc

c: David Corso
Barbara Gantwerk
Angel Ramos
David Joye
Dodi Price
Allwyn Baskin
Charles Peffall