

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

Higher Education Student Assistance Authority

July 1, 2013 to April 30, 2015

**Stephen M. Eells
State Auditor**



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OFFICE OF THE STATE AUDITOR
(609) 847-3470
FAX (609) 633-0834

STEPHEN M. EELLS
State Auditor

GREGORY PICA
Assistant State Auditor

JOHN J. TERMYNA
Assistant State Auditor

New Jersey State Legislature

OFFICE OF LEGISLATIVE SERVICES

OFFICE OF THE STATE AUDITOR
125 SOUTH WARREN STREET
PO BOX 067
TRENTON NJ 08625-0067

DAVID J. ROSEN
Executive Director
(609) 847-3901

The Honorable Chris Christie
Governor of New Jersey

The Honorable Stephen M. Sweeney
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The Honorable Vincent Prieto
Speaker of the General Assembly

Mr. David J. Rosen
Executive Director
Office of Legislative Services

Enclosed is our report on the audit of the Higher Education Student Assistance Authority for the period of July 1, 2013 to April 30, 2015. If you would like a personal briefing, please call me at (609) 847-3470.

Stephen M. Eells
State Auditor
October 6, 2015

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Scope

We have completed an audit of the Higher Education Student Assistance Authority (HESAA) for the period July 1, 2013 to April 30, 2015. Our audit included financial activities accounted for in the state's General Fund and the authority's off-line accounts. The HESAA is a component unit of the state and is organizationally considered in, but not of, the Department of State. The HESAA functions independent of any supervision and control by the department as a non-profit, state-designated authority. The HESAA administers New Jersey's student grant and scholarship programs including the Tuition Aid Grant (TAG) and the New Jersey Student Tuition Assistance Reward Scholarship (NJSTARS) Programs. In addition, it administers the New Jersey College Loans to Assist State Students (NJCLASS) Program and the New Jersey Better Educational Savings Trust (NJBEST). HESAA expenditures for the audit period totaled \$822 million.

We also reviewed certain general controls over the HESAA's information systems including security management, physical security, contingency planning, change management, and logical access.

Objectives

The objectives of our audit were to determine whether financial transactions were in compliance with enabling legislation, were reasonable, and were recorded properly in the accounting systems. An additional objective was to determine whether the HESAA was meeting its administrative responsibilities for the grant, scholarship, and loan programs. We also determined the adequacy of select general controls over the HESAA's information systems including security management, physical security, contingency planning, change management, and logical access.

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

Methodology

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

In preparation for our testing, we studied legislation, the administrative code, circular letters promulgated by the Department of Treasury, and the policies of the HESAA. Provisions that we considered significant were documented and compliance with those requirements was verified by interview, observation, and through our testing of financial transactions and student records at the HESAA and at selected institutions. We also read budget messages, reviewed financial

trends, and interviewed HESAA and institution personnel to obtain an understanding of the programs and the internal controls.

A nonstatistical sampling approach was used. Our samples of financial transactions were judgmentally selected and were designed to provide conclusions about the validity of transactions, as well as internal control and compliance attributes. Our samples of grant, scholarship, and loan recipients were judgmentally selected and designed to determine eligibility and program compliance.

Conclusions

We found the financial transactions included in our testing were in compliance with enabling legislation, were reasonable, and were recorded properly in the accounting systems. We also found the HESAA was meeting its administrative responsibilities for the grant, scholarship, and loan programs. In making these determinations, we noted certain internal control and compliance weaknesses meriting management's attention concerning the re-employment of retirees, the NJCLASS Program, the Law Enforcement Officer Memorial Scholarships Program, and the NJBEST.

We further determined select general controls over the HESAA's information systems were adequate, however, we noted weaknesses in the areas of system access controls and risk assessment/security plan that merit management's attention.

We also made an observation concerning contracted temporary employees.

Former HESAA Employees Placed on Employment Agency Payroll

Practice appears to circumvent the Division of Pensions and Benefits post-retirement rules.

The HESAA augments its workforce through contracts with a number of employment agencies. Within certain contracts the HESAA established pass-through agreements, through which the HESAA recommends individuals to be hired by an employment agency and assigned to the HESAA. Nine former employees have returned to the HESAA through these agreements, including six former employees currently collecting a state pension. Although on the employment agencies' payrolls and charged under the contracts, the HESAA maintains complete control over the rate of pay, locations, assignments, and supervision of these employees. In addition, these individuals are performing job duties similar to their previous HESAA employment. For their general and administrative role, the employment agencies receive fees ranging from 22 percent to 30 percent above the employees' hourly rates, totaling over \$100,000 during the audit period.

New Jersey Statutes provide for post-retirement work restrictions that limit the amount of annual earnings and New Jersey Administrative Code requires "Bona fide severance from employment" before the re-employment of retired members from any of New Jersey's state-administered retirement systems. This is necessary to comply with Internal Revenue Code requirements. In addition, there is a form for all state agencies titled, "Notification of Employment after Retirement", which should be submitted within 15 calendar days of the date of hire for review by the Division of Pensions and Benefits. The circumstances surrounding the current retirees working under these contracts appear to be a circumvention of these post-retirement rules and there is sufficient evidence to refer the matter to the Division of Pensions and Benefits for further review.

HESAA also operates a summer internship program in a similar vein in which they select the individuals and establish the hourly rate of pay but use the employment agency as the conduit.

Recommendation

We recommend the HESAA refer this matter to the Division of Pension and Benefits. In addition, they should discontinue their practice of placing former employees or retirees on employment agencies' payrolls. If there is a continued, justifiable need for the services provided by these individuals, they should be brought back as employees on the authority's payroll, subject to the limitations and requirements set by the Division of Pensions and Benefits.

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New Jersey College Loans to Assist State Students (NJCLASS) Program

Program controls need to be strengthened.

The NJCLASS program established within the HESAA, “shall make loans available in such amounts necessary to ensure that student loans remain generally available to, or for the benefit of, eligible students who are not eligible for, or have additional financial need beyond, a federally insured student loan and who meet the established eligibility criteria”. Our audit of the loan program disclosed internal control and/or compliance deficiencies in the areas of maximum loan amounts, reporting and tracking of loan fraud, loan forgiveness, and Internal Revenue Service reporting.

Maximum Loan Amount

New Jersey Statutes state a maximum loan amount should be established based on such factors as the cost of attending a particular institution, family income, value of family assets, or other factors the HESAA may consider relevant. We found the HESAA has not established a maximum loan amount or any formulaic process to determine one on a case-by-case basis. This has resulted in 1,242 individuals that have had total loans disbursed over \$200,000; whether student, co-borrower, and/or cosigner. In one instance, a family of six with a combined parental yearly income of \$181,000, residing in a house valued at approximately \$163,000, received loans totaling \$832,395.

Reporting and Tracking of Fraud

New Jersey Statutes state that any person who having obtained an NJCLASS loan, solicits, applies for, or accepts such loan or any person who knowingly or willfully furnishes any false or misleading information for the purpose of obtaining a loan, or enabling another to obtain a loan, shall be guilty of a crime of the fourth degree. We found the HESAA determined 16 individuals in 2013 and 7 individuals in 2014 had allegedly obtained 39 individual loans totaling \$456,727 fraudulently and did not refer them to the New Jersey Office of the Attorney General for prosecution. We further found a HESAA policy that states when an individual declares they were put on a loan fraudulently, their information is completely removed from the NJCLASS system. This prevents the HESAA from performing edit checks on future applications to identify similarities with past fraudulent activity.

Forgiveness

The New Jersey Administrative Code establishes rules governing the discharge of NJCLASS loan balances for death or total and permanent disability of a borrower. These rules also state that other borrowers or co-signers of the loan would remain obligated to repay the loan. The HESAA executive staff created an internal policy, without seeking the HESAA Board’s approval, which allows the two individuals which currently comprise the executive staff to forgive loan obligations of other borrowers and co-signers. The NJCLASS trust is refunded

through the HESAA general revenue sources without board involvement. HESAA management has stated that the approval of the HESAA Board was not required for this policy. We found from July 2013 to August 2014, HESAA executive staff approved seven other borrowers or co-signers for loan forgiveness totaling \$211,595.

Internal Revenue Service Reporting

The Internal Revenue Service requires a Form 1099-C Cancellation of Debt for any student loan principal canceled of \$600 or more to be sent to the taxpayer and to the Internal Revenue Service. We found seven individuals that should have received a Form 1099-C for calendar year 2013 totaling \$211,554 but did not. Principal amounts canceled ranged from \$818 to \$76,487. In addition, we found one individual that received a Form 1099-C for \$39,166 representing four loans when the actual amount canceled totaled \$52,835 for five loans, a difference of \$13,669.

Recommendation

We recommend the HESAA improve their internal control and/or compliance deficiencies in the areas of maximum loan amounts, reporting and tracking of fraud, forgiveness, and Internal Revenue Service reporting. Specifically HESAA should:

- Comply with New Jersey Statutes by establishing a maximum loan amount.
- Refer all suspected fraud cases to the Attorney General's Office and maintain the names on the NJCLASS system.
- Obtain approval from the HESAA Board for the loan forgiveness policy. In addition, the Board should be included in the loan forgiveness process to ensure transparency.
- Comply with Internal Revenue Service requirements and issue Form 1099-C when applicable.

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Law Enforcement Officer Memorial Scholarships Program

Improvements should be made to the payment process.

The Law Enforcement Officer Memorial Scholarships Program provides scholarships for undergraduate study at eligible New Jersey institutions of higher education for the dependent children of New Jersey law enforcement officers killed in the line of duty. The amount of the recipient's scholarship is determined annually and is renewable for up to four years. Certifications are sent to the institutions to verify the dependent is currently registered for the semester and making satisfactory academic progress. In addition, the HESAA requests certification of the student's enrollment status (full or part-time) and the cost of attendance

depending upon whether the student commutes or boards at the institution. Eight individuals received at least one scholarship for the period Fall 2013 through Fall 2014 totaling \$194,438. Our review of those scholarships found four instances of improper payments and noncompliance with the New Jersey Administrative Code (NJAC) including the following.

- \$15,274 was sent to an institution even though the certification stated the student was not enrolled. The institution noted the error and subsequently returned the funds.
- \$21,465 was sent to an institution even though the certification stated the cost of attendance would be \$9,625 resulting in an overpayment of \$11,840.
- \$5,248 was sent to an institution even though the certification stated the student was part-time. The NJAC requires the student to be currently enrolled, or plan to be enrolled, as a full-time undergraduate student.
- \$12,648 was sent to an institution even though the certification stated the cost of attendance would be \$6,336. The amount paid was based on the cost of attendance shown on the institution's internet site.

In addition, the NJAC requires that students should receive notification specifying the amount of the scholarship based on their annual cost of undergraduate study and other available state financial assistance. No notifications were made to the students.

Recommendation

We recommend the HESAA strengthen the overall review process of the certifications received from the institutions. In addition, the HESAA should provide student notifications as required by the New Jersey Administrative Code.



New Jersey's 529 College Savings Plan (NJBEST)

Accurate and complete data should be maintained and utilized for scholarship awards.

A database used by the HESAA to administer the scholarship portion of the New Jersey Better Educational Savings Trust (NJBEST) was found to contain inaccurate and incomplete data for the issuance and tracking of scholarships. NJBEST is a qualified tuition savings program administered by the HESAA. An investment management firm is under contract to manage the college cost savings portion of the program and provide the HESAA with account information which they use to administer an associated scholarship program. On average, 548 one-time scholarships totaling \$592,000 are awarded annually to individuals within the NJBEST program. Scholarships are awarded to students who attend a New Jersey institution of higher education and meet eligibility requirements which include having a NJBEST account for at

least four years; making account contributions of \$1,200 or greater; and having made a qualified withdrawal from the account. We found the database of 15,000 records contained 25 individuals with two social security numbers, 143 individuals on the database twice, and 1,133 individuals who received scholarships totaling \$1.1 million with a blank disbursement date field, which would document the required withdrawal was made.

Six months after the initial review of the database, HESAA provided an updated database which also included inaccurate and incomplete data. Although improvements had been made, the database included 14 individuals that had two social security numbers, 4 individuals were on the database twice, and 1,104 individuals received scholarships totaling \$1.1 million with blank disbursement date field. In addition, we noted one individual, who appeared twice on the database, received two scholarships: one for \$1,250 in January 2014 and another for \$1,500 in November 2014.

Recommendation

We recommend the HESAA establish an accurate and complete database to include all of the eligibility requirement information to ensure the scholarships are only given when requirements are met by the student.



System Access Controls

Access control policies and procedures should be formally developed and properly implemented.

The HESAA utilizes three application systems to help meet its goals and objectives. We reviewed the general controls for the three systems (NJGRANTS, NJCLASS, and NJLOANS) that contain student application and institutional data for grants, scholarships, and loans. Our review found that HESAA does not have formal policies and procedures for granting and removing user access to the three systems. Attached to user access request forms there is a Summary of Security Awareness for HESAA Systems (summary). The summary outlines that inactive logon ID's will be suspended after 6 months and deleted after one year. In addition, logon passwords are required to be changed every 90 days. Access to the systems is granted to staff and contracted employees at the HESAA, in-state and out-of-state institutions, lenders, and attorneys. Our review of the 942 individuals with access to at least one of the HESAA systems disclosed the following.

- There were 80 logon IDs that had not accessed a system in greater than six months.
- There were 21 logon IDs that had not accessed a system in greater than one year.
- There were 305 logon IDs that had not updated passwords in greater than 90 days.

An additional review of system access found the following.

- Seven users had multiple logon IDs associated with their name, one of which had three separate logon IDs.
- Separated employees are not removed timely. Three of forty full-time employees separated between July 1, 2012 and December 31, 2014 did not have their access removed timely from the system, one of which had access removed 124 days after the date of separation. Six of forty-two separated temporary employees during that same time period did not have their access removed timely, one of which had access removed 60 days after the date of separation.

Federal Information System Controls Audit Manual (FISCAM) standards require application access control policies be formally developed, documented, and properly implemented. Effective application access controls provide reasonable assurance that only authorized personnel have access to the application and only for authorized purposes.

Recommendation

We recommend the HESAA formally develop and implement access control policies and procedures including the guidelines within the Summary of Security Awareness for HESAA Systems. In addition, separated individuals should be removed from the systems in a timely manner.

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Risk Assessment/Security Plan

A security plan should be formally developed to identify threats to each system.

Federal Information System Controls Audit Manual (FISCAM) standards require the development, documentation, and implementation of a security plan based on a risk assessment of each system or application. The lack of a comprehensive security plan increases the risk that existing controls may be ineffective or inadequate to protect the application and its data against unauthorized use, disclosure, modification, or loss. Our review found no evidence that risk assessments are performed or documented. In addition, no formal security plan has been developed, documented, and implemented for the NJGRANTS and NJCLASS systems. A formal security plan has been developed for the NJLOANS system, but it is outdated and does not include certain key information that should be included pursuant to the FISCAM standards.

Recommendation

We recommend HESAA formally perform risk assessments and develop, document, and implement security plans for each application or system pursuant to the FISCAM standards.

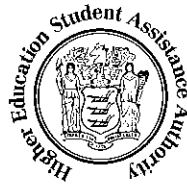
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Observation

Contracted Temporary Employees

The Fiscal Year 2015 HESAA's workforce as presented in the 2016 State Budget indicates that the authority operates with a workforce of 134 employees. However, the HESAA has an additional 110 individuals on staff through the use of temporary employment agencies. This distorts the actual workforce needed to operate the authority and it would appear to be a questionable business practice to have such a high percentage of employees with little or no "ownership" for the mission of the HESAA and having access to customer data. In addition, we noted a temporary employee holding an Assistant Director position and fifteen temporary employees that have been assigned to the HESAA for over four years.

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State of New Jersey

HIGHER EDUCATION STUDENT ASSISTANCE AUTHORITY

4 QUAKERBRIDGE PLAZA

PO Box 545

TRENTON, NJ 08625-0545

1-800-792-8670

www.hesaa.org

September 29, 2015

CHRIS CHRISTIE
Governor

KIM GUADAGNO
Lt. Governor

GABRIELLE CHARETTE, ESQ.
Executive Director

Mr. John J. Termyna, Assistant State Auditor
Office of the State Auditor
125 South Warren Street
P.O. Box 067
Trenton, NJ 08625-0067

Dear Mr. Termyna:

Thank you for the opportunity to review and respond to the draft audit report regarding the Higher Education Student Assistance Authority (HESAA) for the period July 1, 2013 to April 30, 2015.

I am pleased that the audit concluded that HESAA's financial transactions were in compliance with enabling legislation, were reasonable, were recorded properly in the accounting systems and that HESAA was meeting its administrative responsibility for the grant, scholarship and loan programs.

Notwithstanding the above, the audit noted some matters which merit management's attention. Below, HESAA offers information on the current status of these matters, as well as our corrective actions to address these matters and their corresponding recommendations.

Former HESAA Employees Placed on Employment Agency Payroll

Recommendation:

We recommend the HESAA refer this matter to the Division of Pension and Benefits. In addition, they should discontinue their practice of placing former employees or retirees on employment agencies' payrolls. If there is a continued, justifiable need for the services provided by these individuals, they should be brought back as employees on the authority's payroll, subject to the limitations and requirements set by the Division of Pensions and Benefits.

Response:

HESAA has contacted the New Jersey Division of Pensions and Benefits (Division) to confirm that its hiring practices comply with applicable rules governing the employment of retirees. HESAA will fully comply with the Division's guidance on this matter.

New Jersey College Loans to Assist State Students (NJCLASS) Program**Recommendation:**

We recommend the HESAA improve their internal control and/or compliance deficiencies in the areas of maximum loan amounts, reporting and tracking of fraud, forgiveness, and Internal Revenue Service reporting. Specifically HESAA should:

- * Comply with New Jersey Statutes by establishing a maximum loan amount.*
- * Refer all suspected fraud cases to the Attorney General's Office and maintain the names on the NJCLASS system.*
- * Obtain approval from the HESAA Board for the loan forgiveness policy. In addition, the Board should be included in the loan forgiveness process to ensure transparency.*
- * Comply with Internal Revenue Service requirements and issue Form 1099-C when applicable.*

Response:

With respect to the first bullet, HESAA believes its regulation at N.J.A.C. 9A:10-6.6 which states in pertinent part "the amount borrowed for an NJCLASS Loan Program loan shall not exceed a student's estimated cost of attendance at the eligible institution minus all other financial assistance for which the student is eligible for the academic period for which the loan is intended" does establish maximum loan amounts in compliance with the statute. It should be noted that before HESAA makes any NJCLASS loan, we require school certification to ensure that the amount of the loan is the cost of attendance less all other financial assistance. In cases where the loan is not certified, HESAA cancels the loan. If the loan is certified for an amount less than requested by the borrower, HESAA only approves the loan for the certified amount.

Notwithstanding the above, we understand that the State Auditor believes that a maximum loan amount should be a specific aggregate dollar amount, rather than the cost of attendance less other financial aid. Given the negative consequences of over-borrowing for both the borrowers and the Authority, HESAA has formed an internal Task Force to look at this issue and determine an appropriate aggregate dollar amount.

With respect to the second bullet, upon this issue being brought to our attention, we immediately began referring all fraud cases to the Attorney General's Office.

As to maintaining the names on the NJCLASS system, it is important to note that when a fraud or forgery is reported to HESAA, the alleged victim must submit documentation including a police report to HESAA to support his/her claim. HESAA then thoroughly investigates the claim and renders a determination in the matter. After the investigation is complete, and only when it is determined that a fraud or forgery actually occurred, will HESAA remove the victim's name from the loan record to prevent any further credit reporting of the victim in accordance with the federal Fair Credit Reporting Act. HESAA believes that not removing an individual who has successfully demonstrated that he/she is a victim of fraud or forgery could unfairly prejudice that individual in future loan applications. However, should a victim of fraud be released from a loan, co-sign a subsequent loan and then claim they were victimized a second time, HESAA in the second investigation will have the individual's history and will give the subsequent claim of fraud or forgery the additional scrutiny it merits. Finally, it should be noted that when one individual successfully demonstrates fraud or forgery, all other parties to the loan remain on the system so that in the event the perpetrator of the fraud or forgery attempts to apply for additional loans his/her application will be flagged and handled appropriately.

With respect to the third bullet, the agenda for the upcoming October 22, 2015 Board meeting will include approval of the loan forgiveness policy. In addition, the Board will be fully briefed on all loan forgiveness requests received, granted or denied during Fiscal Year 2015. Due to the Personally Identifiable Information (PII) in the loan forgiveness applications, this briefing will take place in closed session and will occur on an annual basis each October for the fiscal year just ended.

With respect to the fourth bullet, HESAA concurs with the State Auditor's finding and has implemented a reconciliation process between the Finance Department and the Servicing and Collections Unit to ensure that all cases of loan discharge and/or loan forgiveness are reported appropriately to the IRS on a Form 1099-C and in the timeframes mandated by the IRS.

Law Enforcement Officer Memorial Scholarships Program

Recommendation:

We recommend that the HESAA strengthen the overall review process of the certifications received from the institutions. In addition, the HESAA should provide student notifications as required by the New Jersey Administrative Code.

Response:

HESAA concurs that a strengthening of the overall review process was necessary and has taken steps to achieve same. For example, HESAA has reformatted the school and HESAA certification form to clearly indicate to the schools and HESAA staff the certification steps that must be followed and the eligibility criteria that must be met. In addition, HESAA has implemented a final review process that requires all approved applications be re-checked one last time prior to payment. HESAA concurs that students should be notified directly by the Authority and will do so on a going forward basis.

Finally, it should be noted that in the cases cited in the report where errors were made, all erroneous payments were refunded to the Authority.

New Jersey's 529 College Savings Plan

Recommendation:

We recommend the HESAA establish an accurate and complete database to include all of the eligibility requirement information to ensure the scholarships are only given when requirements are met by the student.

Response:

HESAA concurs with this recommendation; and since this matter was initially brought to our attention, we have been working with Franklin Templeton to refine the data file they provide to us. The file Franklin Templeton now sends HESAA contains the necessary eligibility criteria including disbursement dates.

With respect to duplicate individuals appearing on the report, each instance must be investigated on a case by case basis, to make sure that they are indeed duplicates and not individuals who have more than one NJBEST account. Both HESAA and Franklin Templeton have established procedures and processes to ensure that true duplicates are culled from the file.

Systems Access Controls

Recommendation:

We recommend the HESAA formally, develop and implement access control policies and procedures including the guidelines within the Summary of Security Awareness for HESAA Systems. In addition, separated individuals should be removed from the systems in a timely manner.

Response:

HESAA concurs with this recommendation and we are in the process of developing and implementing access control policies and procedures which will address, among other things, removing system access for separated individuals in a timely manner.

Risk Assessment/Security Plan

Recommendation:

We recommend HESAA formally perform risk assessments and develop, document, and implement security plans for each application or system.

Response:

HESAA concurs with this recommendation and will develop, document, and implement security plans for each application or system which will include key information pursuant to FISCAM standards. Development of the plans will include a risk assessment phase.

Contracted Temporary Employees

While pleased with the services rendered by our temporary employees, HESAA recognizes the benefits of hiring full-time employees and has made significant strides in this direction. To date, numerous job postings have been issued, search committees formed, interviews conducted and most importantly qualified candidates hired. Specifically, with respect to the Assistant Director position noted in the audit, HESAA has identified a qualified candidate, received the requisite approval to hire, and made an offer that was accepted with an anticipated start date of Monday, October 5, 2015.

In closing, I would like to thank your audit staff for their diligent work and the professionalism they exhibited throughout their time at HESAA. If you have any questions, please do not hesitate to contact me directly.

Sincerely,

A handwritten signature in black ink, appearing to read 'Gabrielle Charette', with a long horizontal flourish extending to the right.

Gabrielle Charette, Esq.
Executive Director