

Office of the State Auditor

Audit Report

**Department of the Treasury
Bureau of Risk Management
Risk Management Interdepartmental Accounts**

July 1, 1993 to March 31, 1995

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The Honorable Christine Todd Whitman
Governor of New Jersey

The Honorable Donald T. DiFrancesco
President of the Senate

The Honorable Jack Collins
Speaker of the General Assembly

Mr. Albert Porroni
Executive Director
Office of Legislative Services

We have completed an audit of the **Risk Management Interdepartmental Accounts**, administered by the Department of the Treasury, Bureau of Risk Management, for the period July 1, 1993 through March 31, 1995.

We found that the financial transactions included in our testing were related to the agency's programs, were reasonable and were recorded properly in the accounting systems. However, we did note areas where improvement is needed. Our audit disclosed significant deficiencies, in the tort claim review process, which rendered the program ineffective. The programs backlog of more than 5000 cases had not been investigated or evaluated. Additionally, the bureau has been unable to document the level of state liability and as a result cannot purchase excess liability insurance coverage, leaving it at risk in the event of a catastrophic incident. We also noted numerous duplicate payments to vendors in several of the bureau's programs. Details of the findings and recommendations are included in our report.

This audit was conducted pursuant to the State Auditor's responsibilities as set forth in Article VII, Section 1.6 of the State Constitution and Title 52 of the New Jersey Statutes.

Richard L. Fair
State Auditor
June 28, 1996

**Department of the Treasury
Bureau of Risk Management
Risk Management Interdepartmental Accounts**

Scope

We have completed an audit of the Risk Management Interdepartmental Accounts, administered by the Department of the Treasury, Bureau of Risk Management, for the period July 1, 1993 to March 31, 1995. Our audit included financial activities accounted for in the state's General Fund.

Total expenditures of the accounts during the twenty-one month audit period were \$81.3 million. The prime responsibility of the risk management interdepartmental accounts is to provide insurance and other service payments for the state's various insurance premium and self-insurance policies to protect against loss from the result of accident or negligence where the state and/or its representative is involved. The largest program in this category is the state's self-insurance for workers compensation claims, amounting to approximately 75 percent of expenditures.

Objectives

The objectives of our audit were to determine whether financial transactions were related to the agency's programs, were reasonable and were recorded properly in the accounting system. We also tested for resolution of significant issues noted in our prior report.

This audit was conducted pursuant to the State Auditor's responsibilities as set forth in Article VII, Section 1.6 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, administrative code, circular letters promulgated by the State Comptroller, and policies of the agency. Provisions that we considered significant were documented and compliance with those requirements was verified by interview and observa-

tion and through our samples of financial transactions. We also read the budget message, reviewed financial trends, and interviewed agency personnel to obtain an understanding of the programs and the internal control structure.

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. Claims for each insurance category processed during our audit period were selected. Other transactions were selected using auditor's judgment.

To ascertain the status of findings included in our prior report, we identified corrective action, if any, taken by the agency and walked through the system to determine if the corrective action was effective.

Conclusions

We found that the financial transactions included in our testing were related to the agency's programs, were reasonable and were properly recorded in the accounting system. In making this determination, we noted certain significant internal control weaknesses and matters of compliance with laws and regulations meriting management's attention.

We also found that the agency has resolved the significant issues noted in our prior report.

Details of our findings and recommendations follow.

Tort Claim Review Process

A claim against the State of New Jersey relating to a death or for injury to a person or to property must be filed with the Bureau of Risk Management (BRM). The New Jersey Tort Claims Act (N.J.S.A. 59:8-8) prohibits the claimant from filing suit in court for a period of six months subsequent to submitting the claim. This delay is designed to give the state time to investigate the claim and make attempts to resolve it in the best interest of the state. BRM procedures require a thorough evaluation of each tort claim which might allow the state to settle a case without court proceedings. Once the six month period is complete, the claimant may file a Summons and Complaint. When this occurs, the case is forwarded to the Department of Law and Public Safety, Division of Law (DOL) for disposition. Once the case is adjudicated and a judgment awarded, payment is authorized by DOL and the payment to the claimant is processed by the Department of the Treasury, Division of Administration.

Our review noted the following weaknesses in the tort claim process:

- C BRM performs little or no investigative work in the six month period allotted for evaluation by law. Thus when a claimant files a Summons and Complaint the case is forwarded to DOL without an adequate preliminary investigation. At that time, it is difficult for DOL to perform an effective investigation due to the time delay and may result in the state going to court unprepared to properly defend itself. The primary reason for the lack of investigations by BRM was that the number of claim investigators had been reduced over the past several years to one employee. This individual's time was spent logging claims and handling phone complaints for the program. Little if any time was available to conduct investigations. As of the end of our fieldwork, the backlog of tort claims at risk management numbered more than 5000 cases.

The lack of an effective investigation may reduce the state's ability to settle the case out of court, result in an increased number of court cases which leads to increased court costs, and result in higher settlements or judgments.

- C Due to insufficient records, the monetary effect of not completing adequate investigations is unknown. It should be noted that in January 1995 a Risk Management Task Force expressed similar concern over the lack of investigations.

C The state has not established an adequate measure of its contingent liability for tort claims. A liability for these cases is estimated by arbitrarily assigning an initial amount of \$250 or \$500 when the claim is received. This amount is not adjusted upward unless further investigation is performed to document a higher level of liability. Since such investigations are seldom performed the state is unable to accurately measure proper tort liability amounts. The lack of adequate and accurate tort claim liability estimates is a contributing factor to the state's inability to reinstate its excess liability insurance policy as discussed in our next finding.

We recommend the bureau, in conjunction with the Division of Law, prioritize the investigative function and institute the necessary review procedures which would allow for timely investigation and evaluation of tort claims prior to the claimant filing suit against the state. In addition, the pending tort claims should be evaluated and measured.

The State Does Not Carry Catastrophic/Excess Liability Insurance Coverage

Our review of the insurance premiums program noted that the State of New Jersey did not purchase excess liability insurance. Without this insurance, the state is at financial risk in the event of a catastrophic incident. A study performed by the Governor's Task Force Steering Committee in 1995 indicated that most states purchase excess liability policies and/or have tort statutes that cap their liability. New Jersey has neither. In lieu of tort legislation to cap the state's liability the purchase of excess liability insurance would be prudent since it is management's responsibility to safeguard the state's assets.

Werecommend the bureau review and evaluate the risk reduction benefits available by purchasing excess liability insurance. As an alternative to insurance, legislation could be proposed to limit the state's tort liability for new claims. Should the decision be made to purchase insurance, then as noted in the preceding finding, an adequate tort claim amount must be calculated and provided to insurance companies in order to obtain excess liability coverage.

Duplicate Payments to Vendors

Our analysis and testing of agency expenditure transactions disclosed duplicate payments totaling \$472,000. Duplicates were noted in the following program areas:

- C The Workers' Compensation Payment System (WCPS) duplicated a portion of its September 2, 1994 payments. The bureau was unable to completely document the total amount duplicated. However, they had identified duplicate payments amounting to \$245,000 by the end of our fieldwork.
- C One claimant on the WCPS had been receiving duplicate compensation checks for a period of 21 months totaling \$23,953.
- C Our analysis and testing of tort claim payments disclosed duplicate payments totaling \$190,638.
- C Additional duplicate payments were noted in the areas of medical and auto liability claim payments.

The duplicate payments were caused by a variety of reasons. The duplication of workers' compensation payments resulted from a computer system problem, whereas the duplicate payment of medical and auto liability claim payments were caused by backlogs due to the high volume of invoices received versus limited resources available for processing. The tort liability payments process was complicated by procedures that require the Division of Law (DOL) to authorize tort payments which are then forwarded to Treasury, Division of Administration for final (third level) approval and issuance of the payment. Since the payment account was under the jurisdiction of Treasury, the DOL was not aware that they had access to the account to determine if a claim had been paid. Instead they used manual files which were not well organized due to human resource constraints.

Even though the potential for duplicate payments existed, none of the involved agencies (BRM, DOL, Treasury Administration) established procedures to detect duplicate payments. While many of these duplicate payments were either returned or were in the process of being recovered by BRM, the fact remains that the occurrence of such duplications allows for the possible loss of monetary resources to the state as well as the loss of valuable human resources wasted on the processing of payments twice and the subsequent recovery functions required to recoup the overpayment.

We recommend:

- C The Bureau of Risk Management address vendor invoice backlogs and institute procedures whereby periodic analysis of payments to vendors are completed and similar dollar amounts verified for propriety.
- C The Division of Law be given inquiry capability to the accounting system for tort liability transactions. By allowing the DOL access to the accounting system for the purpose of verifying if payments had been previously paid, duplicate payments could be avoided.
- C The Bureau attempt recovery of all duplicate payments.

Controls over the Processing of Refund of Disbursement Transactions

During our audit period the bureau received approximately \$4 million in refunds related to the workers' compensation program. Our testing disclosed inadequate controls over the processing of refund of disbursement transactions.

- C Checks were not posted to a mail log upon receipt, nor did the bureau subsequently reconcile refunds received with the New Jersey Comprehensive Financial System (NJCFS). The recording of receipts and periodic reconciliations are necessary to ensure that checks are properly deposited.

- C Checks were often deposited two to three weeks after receipt. Eleven of 16 transactions tested were not deposited timely. Treasury Circular Letter 94-24 requires agencies to deposit moneys the same day they are received.

- C There was a lack segregation of duties in the processing of duplicate payment refunds. One person was responsible for receiving the refunds, depositing them, preparing the cash receipt document, and applying the first two levels of approval for entry into NJCFS.

Management is responsible for providing an adequate level of internal control and compliance with procedures so that state financial resources are properly safeguarded. Limited segregation of duties, unreconciled records and noncompliance with Treasury procedures increases the state's risk of lost resources.

We recommend the bureau establish procedures to assure that refund of disbursement transactions are adequately controlled and recorded in the state accounting system. Procedures should include steps to adequately segregate receipt and recording functions, perform periodic reconciliations of bureau records with the accounting records, and compliance with Treasury circular letter requirements.