

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

**New Jersey Transportation Trust Fund
Authority Appropriations
and
Department of Transportation
Contract Administration**

July 1, 2002 to November 23, 2005

**Richard L. Fair
State Auditor**

2004-2005

LEGISLATIVE SERVICES COMMISSION

ASSEMBLYMAN
JOSEPH J. ROBERTS, JR.
Chairman

SENATOR
BERNARD F. KENNY, JR.
Vice-Chairman

SENATE

ANTHONY R. BUCCO
RICHARD J. CODEY
NIA H. GILL
LEONARD LANCE
ROBERT E. LITTELL
ROBERT W. SINGER

GENERAL ASSEMBLY

CHRISTOPHER "KIP" BATEMAN
FRANCIS J. BLEE
JOHN J. BURZICHELLI
ALEX DECROCE
GUY R. GREGG
JOSEPH J. ROBERTS, JR.



New Jersey State Legislature

OFFICE OF LEGISLATIVE SERVICES

OFFICE OF THE STATE AUDITOR

125 SOUTH WARREN STREET

PO BOX 067

TRENTON NJ 08625-0067

ALBERT PORRONI

Executive Director

(609) 292-4625

RICHARD L. FAIR

State Auditor

(609) 292-3700

FAX (609) 633-0834

The Honorable Jon S. Corzine
Governor of New Jersey

The Honorable Richard J. Codey
President of the Senate

The Honorable Joseph J. Roberts, Jr.
Speaker of the General Assembly

Mr. Albert Porroni
Executive Director
Office of Legislative Services

Enclosed is our report on the audit of the New Jersey Transportation Trust Fund Authority Appropriations and Department of Transportation, Contract Administration for the period of July 1, 2002 to November 23, 2005. If you would like a personal briefing, please call me at (609) 292-3700.

A handwritten signature in black ink, appearing to read "Richard L. Fair".

Richard L. Fair

State Auditor

April 27, 2006

Table of Contents

	Page
Scope.....	1
Objectives	1
Methodology	2
Conclusions	2
Findings and Recommendations	
Bureau of Auditing.....	4
Construction Order Tracking System	5
Settlement Collections.....	7
Supplementary Data - Unaudited.....	9
Bonds Issued and Status of Bonds	10
Investment Status.....	10
Projects Financed by Proceeds.....	10
Future Bonds Issues	10
Schedule of Bonds Issued and Status of Bonds as of June 30, 2005.....	11
Schedule of Obligated and Unobligated Balances as of June 30, 2005	12
Auditee Response.....	13

New Jersey Transportation Trust Fund Authority Appropriations and Department of Transportation Contract Administration

Scope

We have completed an audit of expenditures made by the Department of Transportation for the period July 1, 2002 to June 30, 2005 for transportation projects funded from revenues of the New Jersey Transportation Trust Fund Authority (TTFA). Our scope did not include the project expenditures for New Jersey Transit Corporation since this entity and its financial activities are audited by an independent certified public accounting firm. Total expenditures of the projects during the audit period were \$1.6 billion. The prime responsibility of the New Jersey Transportation Trust Fund Authority is to provide the payment for and financing of all, or a portion of, the costs incurred by the Department of Transportation for the planning, acquisition, engineering, construction, reconstruction, repair and rehabilitation of the state's transportation system. These activities are accounted for in the Special Transportation Fund. We also audited the department's contract administration function for the period July 1, 2003 to November 23, 2005. This function is accounted for in the state's General Fund and the Special Transportation Fund and is financed through general state appropriations, TTFA appropriations, and Federal Highway Authority funding.

Objectives

The objectives of the Transportation Trust Fund Authority audit were to determine the extent to which funds are expended for costs directly related to the projects, including but not limited to salaries and other administrative expenses. In addition, statutes require that we report on the status of bonds, the investment status of unexpended bond proceeds, to identify projects financed from the proceeds of the bonds, and to provide a description of any anticipated bond issues.

We also audited contract administration to determine whether financial transactions were

related to the department's programs, were reasonable, and were recorded properly in the accounting system. The audit was conducted pursuant to the State Auditor's responsibilities as set forth in N.J.S.A. 27:1B-21.1e and N.J.S.A. 27:1B-21.1f and Article VII, Section 1, 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, administrative code, circular letters promulgated by the State Comptroller, and policies of the department. Provisions that we considered significant were documented and compliance with those requirements was verified by interview, observation, and through our samples of expenditure transactions. We also read the budget message, reviewed financial trends, and interviewed department personnel to obtain an understanding of the projects and programs, internal controls, status of bonds, projects financed by the proceeds, and the investment status of the bond proceeds.

A nonstatistical sampling approach was used. Our samples of expenditure transactions were designed to provide conclusions about the validity of transactions as well as internal control and compliance attributes. Transactions were sorted and judgmentally selected.

Conclusions

We found that the financial transactions included in our testing were related to the TTFA projects. In addition, contract administration financial transactions were related to the department's programs, were reasonable, and were recorded properly in the accounting system. In making these determinations, we noted certain internal control weaknesses meriting management's attention.

Information on the status of the bonds, investment status of unexpended bond proceeds, projects financed from bond proceeds, and anticipated bond issues is included as supplementary data in our report. This information has been compiled from Department of Transportation and Department of the Treasury records and is presented for informational purposes. This information has not been audited by us and we do not express an opinion on the information.

Bureau of Auditing

Overall controls need to be strengthened for Professional Contract audits.

The Division of Accounting and Auditing, Bureau of Auditing is responsible for auditing professional service contracts. The bureau established a two-year audit cycle for major consulting engineering firms and a three-year audit cycle for major utility and rail consultant firms. Since substantial portions of the department's contracts are federally funded, the bureau has incorporated the federal cost principles in the audit process.

In order to comply with state and federal requirements, the department has contracted with three certified public accounting (CPA) firms to audit consultant contracts to determine if costs were incurred, billed, and paid under the terms of the contract. The bureau has criteria to audit all consultants with expenditures totaling \$500,000. As of October 1, 2005 there were 1200 contracts with cumulative unaudited expenditures totaling \$950 million. Some of these contracts date back to 1993. Approximately 100 consultant firms require contract cost auditing on an ongoing basis. To maintain a two-year cycle, 50 firms should be audited annually. In addition, we noted no audits have been performed on the major utility and rail consultant firms.

The department's approach is to include all outstanding contracts in the scope of the CPA's review to assist in the elimination of the backlog. However, the bureau's audit plan is an ever changing document which may push planned audits to a future date. In addition, since the consulting contract terms only requires them to retain their supporting documentation for a minimum of three years, the department needs to decide if older contracts should be included in the scope of the audits. An alternative approach may be to audit current period contracts and if problems exist, expand the scope to prior periods.

The bureau only finalized 23 audits during fiscal years 2004 and 2005. As of October 2005 an additional 44 CPA audits were outstanding; 26 had been received by the bureau in draft form, while 18 had not yet been submitted. At this rate the backlog will continue to grow. Additional efforts must be made to eliminate the backlog and to finalize ongoing audits.

In addition to the audit contract processing issues, we identified a lack of follow up on audit results. The audits may identify questionable costs when the consulting firm is unable to support amounts billed to the department. If the bureau concurs with the results, a receivable is established for consulting firm overpayments. Department records indicate outstanding receivables of \$6.5 million dating back to 1965. No collection efforts were being undertaken. However, the department initiated collection efforts as of July 2005, but only for currently completed audits.

Recommendation

We recommend that the department determine how many years of consultant firm contract costs should be included in the CPA firms audit scope. Additional efforts should be made to finalize audits and to initiate collection efforts of all outstanding receivables.

»»»<<<

Construction Order Tracking System

Management should use the Construction Order Tracking System as a monitoring tool.

As part of the Capital Program Management's Strategic Goal to improve the quality of design and reduce the financial impact of construction change orders on capital program funds, the department developed a computerized Construction Order Tracking System (COTS). This system has the ability to produce exception and status reports relating to all construction orders statewide. These reports can identify potential problem areas with contract plans, systemic procedural problems, and/or the

magnitude of changes being made which can impact the program's cash flow position. The changes being made on the projects are categorized into nineteen distinct types. These different types would allow management to pinpoint potential problem areas for which work improvements and/or procedural changes could be implemented to reduce the number of changes required on future projects or improve quality while reducing costs. The system can also identify potential problems and/or systemic issues common to a particular contractor, designer, resident engineer, field manager and/or region.

Management is not fully utilizing the COTS as required by the Construction Procedures Handbook. In addition, we noted that the South Jersey region office had not entered information into the COTS for over a year and had a backlog of 110 change orders. The untimely entering of information weakens management's ability to utilize the system for its intended purpose. Management is also unable to fully monitor the changes by their type, cause, and related costs.

The department is currently in the process of replacing some of the outdated construction IT systems with new modules which will include a replacement for the COTS. The initial implementation is expected in July 2006, with full implementation by December 2007.

Recommendation

We recommend that the department place more emphasis on evaluating causes for changes to construction contracts, and use this information to minimize future construction change orders. In addition, we recommend that the department management enforce the timely entry of information into the COTS.

»»»<<<

Settlement Collections

Controls need to be strengthened and procedures established for settlement collections.

The purpose of a system of internal control is to provide adequate checks and balances that ensure financial transactions are properly authorized and recorded, and to provide a means to safeguard the assets of the entity. In order to accomplish these objectives, management generally provides a means to verify that all receipts are recorded and deposited, and that more than one person is involved in the process. A strong system of internal control will deter errors or detect errors early if they do occur.

The department's consultant agreement states, "The Consultant shall be liable to the State for all damages to the State caused by Consultant's negligent errors and omissions. The Consultant shall reimburse the state for the full costs it has incurred as a result of such negligent errors and omissions, including interest and other expenses."

Once an error or omission is identified, a notification letter is sent to the consultant informing them there may be recoverable costs in accordance with contract terms. Negotiations between the department project manager and the consultant are conducted, and if an amount is negotiated and agreed upon, a second letter is sent by the project manager requesting payment. The project manager receives checks from the consultants.

Records were not maintained by the division to record the amount billed and received. The department should revise their Policy and Procedure No. 236 Cash Receipts - Invoicing to include the negotiated settlement collections. Compliance with Treasury Circular Letter 94-24 OMB could not be determined due to the lack of records. This circular requires agencies to ensure that all monies are deposited on the same day as received.

Recommendations

We recommend that the department establish a procedure to segregate the negotiation, billing, collection and deposit functions. In addition, the departmental policy for cash receipts should be updated to include the settlement collections by the Division of Project Management.

»»><<<

**SUPPLEMENTARY DATA
UNAUDITED**

Bonds Issued and Status of Bonds

On January 15, 1985 the Transportation Trust Fund Authority issued bonds for the purpose of financing the cost of planning, engineering, construction, repair and rehabilitation of the state transportation system. The 1985 Series A bond was the initial series of bonds issued by the authority under the bond resolution. The authority has issued bonds totaling \$14,001,275,000 as of June 30, 2005 with total principal and interest outstanding of \$9,440,330,307. See Schedule I for the status of each bond issue.

Investment Status

Cash and cash equivalents consist of State of New Jersey Cash Management Fund deposits and short term investments acquired under forward delivery agreements. The fair market value at June 30, 2005 was \$136 million.

Projects Financed by Proceeds

The projects financed by the proceeds of each bond issue are not determinable. The bond proceeds are commingled with other revenue sources: motor fuel taxes, commercial vehicle fees and taxes, and toll road authority contributions. A schedule of obligated and unobligated balances by budget fiscal year is provided on Schedule II.

Future Bond Issues

As of the close of our field work, no date had been established for the sale of additional bonds.

»»<<<

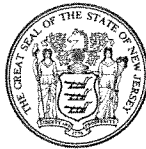
TRANSPORTATION TRUST FUND AUTHORITY
BONDS PAYABLE
SCHEDULE OF BONDS ISSUED AND STATUS OF BONDS
AS OF JUNE 30, 2005
(UNAUDITED)

Schedule I

Bond Series	Principal	Interest	Total
1985 Series A	\$61,270,000	\$0	\$0
1986 Series A	200,000,000	0	0
1988 Series A	125,000,000	0	0
1992 Series A	275,000,000	0	0
1993 Series A	500,000,000	0	0
1993 Series B	61,470,000	0	0
1994 Series A	400,000,000	0	0
1995 Series A	804,475,000	17,840,000	892,000
1995 Series B	788,225,000	93,960,000	38,066,350
1996 Series A	334,065,000	30,435,000	1,853,550
1996 Series B	714,340,000	31,070,000	1,864,200
1997 Series A	703,940,000	29,080,000	1,599,400
1998 Series A	700,000,000	129,430,000	63,850,075
1999 Series A	450,000,000	373,175,000	191,381,419
2000 Series A	450,000,000	17,995,000	899,750
2001 Series A	325,000,000	157,335,000	40,259,375
2001 Series B	690,000,000	0	0
2001 Series C	1,191,450,000	1,184,850,000	399,742,026
2003 Series A	331,100,000	324,135,000	168,073,925
2003 Series B	345,000,000	345,000,000	98,404,593
2003 Series C	924,810,000	279,865,000	80,027,463
2004 Series A	471,655,000	253,820,000	159,713,750
2004 Series B	849,800,000	849,800,000	380,822,706
2005 Series A	566,785,000	566,785,000	175,516,138
2005 Series B	1,213,140,000	1,213,140,000	928,484,601
2005 Series C	524,750,000	524,750,000	286,413,988
Total	\$14,001,275,000	\$6,422,465,000	\$3,017,865,307
			\$9,440,330,307

**NEW JERSEY TRANSPORTATION TRUST FUND AUTHORITY
SUMMARY OF OBLIGATED AND UNOBLIGATED BALANCES
AS OF JUNE 30, 2005
(UNAUDITED)**

<u>Budget Fiscal Year</u>	<u>Obligated</u>	<u>Schedule II Uncommitted Amount</u>
1993	\$2,643,914	\$517,088
1994	17,890,826	4,808,169
1995	6,637,696	2,208,497
1996	6,702,547	4,845,182
1997	7,996,578	5,920,821
1998	10,206,273	2,616,459
1999	14,357,121	1,901,909
2000	18,314,074	1,387,246
2001	31,085,567	1,932,404
2002	55,199,506	2,288,052
2003	79,582,377	7,964,322
2004	140,037,971	15,731,931
2005	<u>302,387,644</u>	<u>30,756,842</u>
Total	<u>\$693,042,093</u>	<u>\$82,878,922</u>



State of New Jersey

DEPARTMENT OF TRANSPORTATION
P.O. Box 600
Trenton, New Jersey 08625-0600

JON S. CORZINE
Governor

KRIS KOLLURI, Esq.
Commissioner

By Hand

April 19, 2006

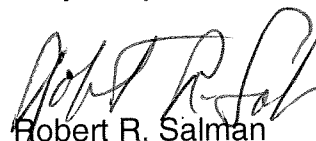
James B. Patterson
Assistant State Auditor
Office of Legislative Services
Office of the State Auditor
125 South Warren Street
P.O. Box 067
Trenton, N.J. 08625-0067

Re: Comments on March 31, 2006 Audit Report

Dear Mr. Patterson:

In response to your March 31, 2006 letter to me, enclosed are written comments concerning the March 31, 2006 audit report of the New Jersey Transportation Trust Fund Authority Appropriations and Department of Transportation Contract Administration.

Very Truly Yours,


Robert R. Salman
Inspector General

c: Steven B. Hanson, Chief Financial Officer
Department of Transportation

CHIEF FINANCIAL OFFICER COMMENTS
OLS CONFIDENTIAL DRAFT AUDIT REPORT
7/1/02 - 11/23/05

BUREAU OF AUDITING

Contract audits are reaching an average of five to six year cycle due to the loss of staff associated with current budget constraints. The Department does not anticipate any change to this staffing situation through the remainder of FY 2006 and FY 2007. Accordingly, we will attempt to decrease our audit cycle by limiting the scope of our audits, subject to Federal Highway Administration concurrence, in the following manner:

- Require our CPA firms to conduct "set-up work" for contract audits. This work is currently performed by in-house staff.
- Limit the numbers of years of consultant firm contract costs to be included in the CPA audit scope.
- Minimize the number of consultant firms to be audited within a specific cycle by increasing the audit expenditure minimum from \$500,000 to \$750,000.
- Statistically sample consultant firms that over the years have demonstrated adequate internal controls over their billing process and have consistently complied with Federal and State regulations.

CAPITAL PROGRAM MANAGERMENTS COMMENTS
OLS CONFIDENTIAL DRAFT AUDIT REPORT
7/1/02 - 11/23/05

CONSTRUCTION ORDER TRACKING SYSTEM (COTS)

We fully agree that it is important to evaluate the causes of changes made to construction contracts as a means to improve our contract documents and to minimize the number of construction change orders in the future. However, it is important to note that the majority of Construction Change Orders (CO's) are unique to their own project and not a systemic problem that would require a Baseline Document Change.

The Construction Order Tracking System (COTS) is just one tool utilized to track for trends or systematic problems. Unfortunately, COTS is outdated and the entry fields that define a problem are subjective and too loosely defined. COTS will be replaced in the fall of 2007 when the Site Manager portion of Trns*port goes online. This will eliminate double work on the part of Construction staff, and provide for better defined reasons relative to why a change order is needed. The new system will also allow us to disseminate reasons for CO's in a more efficient and timely manner. Data from COTS and analyses of said data will continue to be issued by QMS until Site Manager/Trns*port becomes available in 2007.

CPM also recognizes that COTS is only as good as the information that is entered into the system. A program to bring the system up to date has been put into place and the backlog of change orders not entered will be eliminated by July 1, 2006.

Currently CO's are tracked by the staff in the Division of Construction Services (Regional Construction Engineers, Resident Engineers), the Division of Project Management (Project Managers and Program Managers) as well as by the Bureau of Program support Services in Division of Quality Management Services (QMS). When a construction project reaches the 70-90% complete milestone, Lessons Learned are captured through input from the Resident Engineer, Project Manager and Subject Matter Experts (SME's). The Lessons Learned are entered into the Lessons Learned Data Base managed by the Project Management Office in conjunction with QMS. If a common problem arises, Baseline Document Changes (BDC's) will be issued to ensure the problem doesn't continue.

SETTLEMENT COLLECTIONS

Capital Program Management (CPM) recognizes and agrees with the State Auditor's Findings and Recommendations as they relate to CPM's present system of "Settlement Collections" recoverable from Design Consultants. In response, CPM's on-going efforts to improve this system include the following, as part of our Action Plan:

- A December 2005 Departmental Memorandum was issued that included a "Renewed Emphasis" of the Department's Policy on notifying a Consultant of "Errors & Omissions" and their responsibility to reimburse the State. The Division of Project Management's Project Management Office (PMO) is initiating an update of all Policies and Procedures (P & P) under a Process Improvement Program. This Memorandum will be incorporated into the final P & P.
- CPM is presently reviewing agenda items for forming a future CPM Task Force, to review the P & P for assessing "Design Consultant Liability" and "Design Consultant Accountability". Some specific subjects include "Negotiations and Cost Sharing Agreements".
- CPM, in the short-term, will recommend implementation of a Department Corrective Action Notice (CAN) to address the "Negotiation, Billing, Collection, and Deposit Functions" by CPM. The CAN will be prepared by the PMO and will incorporate the best components of existing P & P.
- CPM, in the long-term, will be only one of many Department-wide "Sponsors" that are required to change existing P & P. The Department has recently (4/3/06) approved "Policy and Procedure No. 300", which is for "Guidelines for Revision of Policies and Procedures". Again, the PMO will take the lead on coordinating with other Department "Sponsors" on "Policy and Procedure No. 236- Cash Receipts" and possibly "Policy and Procedure No. 345- Cost Sharing Agreements".