Office of the State Auditor

Audit Report

Department of Environmental Protection

Hazardous Discharge Fund
Hazardous Discharge Site Cleanup Fund

July 1, 1994 to June 30, 1995
# Department of Environmental Protection

### Hazardous Discharge Fund
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## Audit Report

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We have completed an audit of the Hazardous Discharge Fund and the Hazardous Discharge Site Cleanup Fund administered by the Department of Environmental Protection for the period July 1, 1994 to June 30, 1995.

We found that there was compliance with the significant terms of the funds' enabling legislation, with the exception of the requirement for an annual OMB program analysis. In addition, the agency had developed methods to measure site remediation activity. Procedures for the direct billing of oversight costs were operating effectively, except for the timeliness of billings. However, the indirect cost rate was found to be inaccurate because of the use of incorrect expenditures in the calculation. We determined that the agency had complied with their established procedures to ensure that payments were made for the services contracted. 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
Department of Environmental Protection  
Hazardous Discharge Fund  
Hazardous Discharge Site Cleanup Fund

Scope

We have completed an audit of the Hazardous Discharge Fund and the Hazardous Discharge Site Cleanup Fund administered by the Department of Environmental Protection for the period July 1, 1994 to June 30, 1995.

Total expenditures of the funds during the 12 month audit period were $7.5 million. The prime responsibility of the funds is the identification, cleanup, and removal of hazardous discharges and the remediation of contaminated groundwater supplies. Revenues of the funds totaled $9.4 million during our audit period and the major component of revenue was recoveries of current and prior years’ program oversight costs.

Objectives

The objectives of our audit were to determine whether the state is complying with the terms of the funds’ enabling legislation; determine the establishment and utilization of criteria to measure site remediation activity; test procedures for the direct billing of oversight costs to responsible parties, including the calculation of the indirect cost rate used in direct billings; and determine compliance with procedures for payments to contractors.

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 observation 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.

We determined whether the site remediation program had established goals for its cleanup activities and how it measured its progress in achieving those goals through interview and reviews of agency documentation. We reviewed a sample of billings to responsible parties for accuracy and timeliness; we also reviewed the components of the indirect cost rate used in the direct billing process for reasonableness and proper support. Finally, we tested a sample of payments to contractors for compliance with established procedures.

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. Some sample populations were stratified and large dollar transactions were examined. Other transactions were selected on a systematic basis or by auditor judgment.

Conclusions

We found that there was compliance with the significant terms of the funds’ enabling legislation, with the exception of the requirement for an annual OMB program analysis. In addition, the agency had developed methods to measure site remediation activity. Procedures for the direct billing of oversight costs were operating effectively, except for the timeliness of billings. However, the indirect cost rate was found to be inaccurate because of the use of incorrect expenditures in the calculation. We determined that the agency had complied with their established procedures to ensure that payments were made for the services contracted.

Details of our findings and recommendations follow.
Direct Billing Backlog

The Department of Environmental Protection (DEP) requires the payment of oversight costs from those parties which are responsible for contamination of sites and who are conducting the remedial action. These oversight costs represent the costs incurred by the department for providing guidance and approval for privately conducted and funded remedial activities. The direct billing function is designed to recoup all of the costs of the program of oversight of responsible party remediation activities. The billings are based on an oversight cost formula established by N.J.A.C. 7:26C.

The current direct billing system maintained by DEP’s Division of Responsible Party Site Remediation does not ensure that there will be a sufficient number of billings to recoup oversight costs in a timely manner. It is a goal of the division to bill every oversight project twice a year. The division estimates that there are 7,000 billable cases (no formal records of billable cases are maintained). Thus there should be approximately 14,000 bills issued annually. During fiscal year 1995 the division issued only 2,260 bills totaling $19.7 million. As a result of the insufficient number of billings, funds that are expended by the site remediation program for the oversight of responsible parties cannot be recovered in a timely manner.

There were a number of causes of this direct billing backlog. The division did not have in place a system that would ensure that all oversight cases were billed on a regular basis. Billings were dependent on billing requests from case managers. Once a billing request was prepared, there were delays in data entry of the requests and in preparing the bills. Although most expenditures were analyzed automatically, there were some categories of expenditures that had to be reviewed manually in order to complete the bill.

The direct billing process is scheduled to be automated in the near future. A contract has been signed with Pinkerton and they will begin implementing their system in 1996.

Recommendation

The department should institute an oversight billing system that will allow it to do the following:

C determine the total number of billable cases under its jurisdiction;

C initiate regular billing requests;
prioritize billings so that cases with the highest expenditures can be billed first and most frequently; and

accumulate all recoverable costs in its database from which it can generate an analysis of expenditures and an allocation of charges between funds.

Indirect Costs

Indirect costs are one component of the oversight cost formula that is used to calculate the costs incurred by DEP in its oversight of responsible party remediations. Indirect costs are those costs which are not readily assignable to individual cases, but which provide general support for the oversight activities of the site remediation program and should therefore be reimbursed by the responsible parties. The indirect cost rate is calculated by dividing total indirect costs of the site remediation program by total direct salaries and fringe benefits of the program.

Our review of the fiscal year 1995 Site Remediation Indirect Cost Calculation revealed that the indirect cost rate of 81.8 percent was inaccurate because of the use of incorrect expenditures. Salary costs were misstated because the source reports did not include all salary expenditures. The source reports included payroll expenditures that were made by payroll transactions but did not include charges to salary accounts that were made via debits and credits. In addition, nonsalary indirect costs were misstated because of the improper inclusion of direct expenditures and because of improperly coded indirect costs.

We recalculated fiscal year 1995 indirect cost rate to be 79.2 percent which could result in reduced billings.

The maximum exposure would be no greater than $750,000 were DEP to bill for all billable costs.

Our comparison of the fiscal year 1995 indirect cost rate to the rates of prior years disclosed that DEP adopted a different methodology to calculate the rates for fiscal year 1995. The prior methodology, formally adopted and published, included total department management costs as opposed to pro-rated department costs. The DEP has now changed to allocating department management costs so that only those costs related to the Site Remediation Program will be included in the indirect cost calculation. This redefining of cost factors resulted in a lower indirect cost rate for fiscal year 1995. Based on the current methodology, we recalculated the 1993 rate to be 116 percent, rather than 134 percent, which could have resulted in reduced recoverable costs of $4.5 million.
Recommendation

To ensure that costs on future indirect cost calculations are accurate, we recommend that the following steps be taken:

C nonpayroll charges to salary accounts should be reviewed by site remediation personnel to determine whether they should be included;

C expenditures from direct program activities should be excluded from site remediation indirect costs, and

C care should be exercised by all DEP personnel when entering and reviewing project activity codes on invoices, and

C revised rates should be applied to all subsequent billings.

OMB Program Analysis

The Director of the Office of Management and Budget (OMB) of the Department of the Treasury is required by N.J.S.A. 13:1E-55.1 to conduct an annual analysis of DEP’s hazardous discharge cleanup program and to submit it to the Commissioner of DEP and to the State Auditor. OMB has not conducted such a program analysis since 1991 due to confusion raised by a legislative funding decision and a Deputy Attorney General’s opinion.

The statute that required the OMB program analysis also called for the Hazardous Waste Advisory Council to review, analyze and evaluate this analysis. After the legislature decided not to provide funding for the council in its fiscal year 1993 appropriations, the Attorney General’s office ruled that the council was relieved from performing its duties. OMB personnel interpreted this decision to mean that its program analysis was also no longer required to be performed. We requested a clarification of this ruling from the Attorney General’s office and were informed that OMB is still required to conduct its annual program analysis.

Recommendation

We recommend that OMB carry out its statutory duty to perform a program analysis of the hazardous discharge cleanup program at DEP.