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Department of Labor
Employer Accounts System

July 1, 1999 to February 28, 2001

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Enclosed is our report on the audit of the Department of Labor, Employer Accounts System for the period July 1, 1999 to February 28, 2001.

If you would like a personal briefing, please call me at (609) 292-3700.

July 24, 2001
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Department of Labor  
Employer Accounts System

Scope

We have completed an audit of the Department of Labor, Employer Accounts System (EAS) for the period July 1, 1999 to February 28, 2001. Our audit included revenue transactions accounted for in the Unemployment Compensation Fund, the State Disability Benefit Fund, the New Jersey Workforce Development Fund, the Health Care Subsidy Fund, the Catastrophic Illness in Children Relief Fund, the Worker and Community Right To Know Fund, the Pollution Prevention Fund, and the Unemployment Compensation Auxiliary Fund. In addition, we evaluated selected application and general controls involved in the processing of employers’ quarterly contribution reports and payments, and the administration and maintenance of the EAS. Our tests of application and general controls included those in place over file processing data integrity, data security, and application change management.

The major functions of the EAS include processing of employers’ quarterly contribution reports and payments, maintaining employer accounts, assessing employers, and calculating employer experience rates.

Starting in 1997, the EAS was redesigned to address concerns related to the year 2000 and the exhaustion of employer registration numbers. Effective July 1, 1998, the governor’s reorganization plan transferred certain responsibilities for reports, receipts and correspondence processing from the Department of Labor (DOL) to the Division of Revenue (DOR) within the Department of the Treasury. Forms and payments received by the DOR are processed. A data file is then produced and transmitted to the DOL for processing through the EAS.

Total annual revenues processed through the EAS are in excess of $2 billion.
**Objectives**

The objectives of our audit were to determine whether revenue transactions were related to the agency's programs, were reasonable, and were recorded properly in the Employer Accounts System. An additional objective was whether adequate general and application controls were in place to ensure computer processed data was relevant and reliable. This audit was conducted pursuant to the State Auditor's responsibilities as set forth in 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. Additional guidance for the evaluation of computer controls was provided by *Assessing the Reliability of Computer-Processed Data* and *Federal Information System Controls Audit Manual* issued by the United States General Accounting Office and *Control Objectives for Information and Related Technology* issued by the Information System Audit and Control Foundation. In preparation for our testing, we studied legislation, administrative code, circular letters promulgated by the State Comptroller, and policies of the agency. We also studied computer user, operation, and facility documentation. Provisions that we considered significant were documented and compliance with those requirements were verified by interview, observation, and through our samples of financial transactions. We also reviewed financial trends and interviewed agency personnel to obtain an understanding of the programs and the 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. Our tests of application and general controls were designed to provide conclusions about the adequacy
of those controls in place over file processing data integrity, data security, and application management. Sample transactions were randomly selected.

Conclusions

We found that the revenue transactions were related to the agency's programs and were reasonable. We noted a significant number of errors where data was not properly recorded in the EAS, some of which impact rate calculations. While adequate general and application computer controls were in place to process data, the absence of certain management controls and policies hinder the EAS properly recording data.
System controls and processes need to be improved to ensure that employer experience rates are correct.

Certain employer penalty rates need to be reassessed.

Employer Experience Rates

The unemployment, workforce development, healthcare subsidy and disability insurance tax rates are assigned on a fiscal year basis. The Department of Labor (DOL) uses the “reserve ratio method” in determining tax rates for employers. This method requires a record be maintained for each employer identifying the contributions paid, unemployment and disability benefits charged to their account, and taxable wages. The cumulative contributions less cumulative benefits results in the employer’s reserve balance. This reserve balance is then divided by either the three or five year average annual taxable wages, whichever is higher, to arrive at the employer’s reserve ratio. The reserve ratio is used to determine the employer’s contribution rates based on current rate tables.

A review of 47 of the state’s 250,000 employers’ experience rate calculations for fiscal year 2000 disclosed 12 (26 percent) employers with incorrect calculations, resulting in the wrong assigned rate for four (8 percent) employers. In addition, where problems were noted, we expanded our testing to include a review of rate calculations for fiscal year 2001. Details of our review are as follows:

Employers are assigned a new employer (basic) rate until they have established three consecutive full or partial years of contribution payment experience. Effective July 1 of the fourth year of subjectivity, rates are assigned based on the employer’s unemployment experience history. Specially assigned or penalty rates apply to employers who previously had sufficient experience to receive an experience rate but subsequently paid no contributions on wages for employment with respect to at least one of the last three calendar years used in the rate calculation.
Our testing identified two employers with basic rates in fiscal year 2000 who were assigned the penalty rate in fiscal year 2001 when the EAS failed to recognize contributions paid for the first quarter of operations. Since both employers had filed and paid contributions on time, they should have received a calculated rate. One employer’s unemployment rate increased from 2.8 percent (basic rate) to 5.4 percent (penalty rate). The employer’s unemployment calculated rate should have been 1.4 percent. Additionally, the employer’s assigned disability rate of 0.5 percent should have been reduced to 0.2 percent.

When notified, department management investigated this matter further and identified 9600 employers who had basic rates in fiscal year 2000 and penalty rates in fiscal year 2001. They examined 114 of these employers and found that 50 percent were improperly assigned penalty rates and would have to be manually adjusted. Based on this error rate, a potential 4800 employers could be affected.

System edits do not adequately preclude contributions from being credited to the wrong employer.

One employer had contributions for three quarters posted to another employer’s account even though the returns (NJ-927) properly reflected the employer’s identification number, name control and quarter referenced in the encoded data line. This error occurred when DOR registered the employer under their corporation number. This number happened to be consistent with numbers previously used by the DOL for registration numbers. Although DOR subsequently assigned a proper employer identification number, this information was not updated timely in the EAS. When the returns were transmitted to DOL they were matched and were posted to another employer’s account under the old registration number. As a result, both employers were assigned incorrect experience rates.

These errors could have been detected if:
• The DOL had an edit check for reasonableness. The returns incorrectly posted included taxable wages between $3 million and $16 million. The employer whose account they were posted to generally had $20,000 or less in taxable wages.

• The DOL’s edit check for name control had not been turned off.

• The EAS was updated in a timely manner.

• The DOL had periodically sent out delinquency notices.

Department management estimates that between 3,000 and 4,000 employers are affected by this type of error and will have to be manually adjusted. The department has changed the EAS programming to eliminate the option to post transactions using either the employer identification number or the old registration number.

Manual adjustments to employer accounts are required following a retroactive rate adjustment. These adjustments are often due to employers making voluntary contributions to increase their reserve ratio and thus reduce their unemployment contribution rate. In one instance, an employer’s taxable wages were overstated by $653,000 and cumulative contributions were overstated by $17,000 resulting in the employer receiving a lower rate. This occurred when the employer’s contributions were not properly adjusted and reallocated after making a voluntary contribution.
The Employer Accounts System is not properly identifying contributions to be included in the rate calculations.

The EAS currently excludes late transactions from subsequent rate calculations. We noted one employer whose fourth quarter of 1998 payment was received late and was properly excluded in the fiscal year 2000 rate calculation. However, this payment should have been included in the fiscal year 2001 rate calculation, but was excluded.

The fiscal year 2001 calculation should only include account activity attributable to quarters ending December 31, 1999 and prior. Employer contributions overpaid are not included in rate calculations since there are no associated taxable wages to include in the calculation. In one case, an overpayment ($99,000) received prior to December 31, 1999 was reallocated and applied to the second quarter of 2000 and mistakenly included in the employer’s rate determination.

Predecessor’s accounts are not always included in the successor’s experience rate.

When an entire organization, trade or business or substantially all the assets of an employer subject to the law are acquired by another entity, the unemployment tax rate of the acquired entity is transferred to the new employer. Thus the predecessor’s contributions paid, benefits paid and taxable wages paid are included in the successor’s experience rate calculation. The same is basically true for disability unless the employer had a private plan.

In one case, the successor’s experience rate calculation for fiscal year 2001 did not include three quarters of contributions and associated taxable wages paid by the predecessor. As a result, the successor was improperly assigned a lower experience rate. Department management was unable to explain how this condition occurred.
**Recommendation**

We recommend the department:

- continue their efforts to identify and correct employers who have been improperly assigned penalty rates,

- implement additional edit checks to ensure that contributions are posted to the proper employer’s account,

- develop a program to automatically update employer accounts following retroactive adjustments,

- reprogram the EAS to properly identify and include contributions in the proper quarter when making experience rate determinations, and

- modify procedures for successor employer accounts to determine why the EAS is not properly capturing and including all predecessor employer(s) account activity.

**Auditee’s Response**

The department is identifying and correcting employer accounts that had been improperly assigned a penalty rate. The department had identified and documented this problem in various systems incident reports prior to the audit. The department’s Project Maintenance and Support Team is addressing the issue and resolution is expected prior to the issuance of FY 2001-2002 experience rating notices.

The department believes some additional edits may help to credit contributions from employers to the proper employer account. However, such edits may be costly to implement and operate. As noted in the audit, the department does have a name control edit check in the Employer Accounts System. Because of procedural differences that existed between the Department of Labor (DOL) and the Division of Revenue’s (DOR) registration processes prior to consolidation with DOR, the potential exists for NJDOL and DOR to be using different name controls
for accounts established prior to July of 1998. Therefore, in order to expedite the processing of files from DOR with large numbers of transactions, the DOL control was turned off. DOL will work closely with DOR to further consider the design and implementation of additional edits to reduce the number of incorrect postings to employer accounts.

While this was not accomplished as part of the original design of the Employer Accounts System, the department will design and implement programming changes.

The majority of items are properly identified and included in the correct quarter. For those items that were identified as problems, the department will make programming changes, with resolution expected prior to issuance of the FY 2001-2002 experience rating notices.

The department had identified and documented this problem in a systems incident report prior to the audit. Systems changes will be made to correct the problem.

**Data Integrity**

Each quarter, employers are required to file a NJ-927 (Employer's Quarterly Report) indicating gross and taxable wages paid and the amount of contributions due, and a WR-30 (Employer Report of Wages Paid) showing gross wages paid in total and by employee. These reports are received and processed by the Department of the Treasury, Division of Revenue (DOR). After the documents are processed, a data file is generated and transmitted to the Department of Labor (DOL) for entry into the EAS. The inaccurate reporting or recording of wages and employee data could result in overpayment or underpayment of contributions and the improper or incorrect payment.
of unemployment benefits. Furthermore, assessments and employer experience rates could be affected.

Data entered into the EAS is often inaccurate. Our review disclosed that there are insufficient verification and edit checks to ensure the integrity of processed data. We randomly selected 98 employers and compared their NJ-927 gross wages entered in the EAS, 658 quarterly reports for fiscal years 1999 and 2000, to the WR-30 gross wages entered and calculated in the EAS. We identified 57 instances where the amounts did not agree.

We attempted to verify the accuracy of data by tracing to the images of the original documents. In 24 instances the images were not available. In five instances errors were caused by the employer. In 28 other instances differences were caused by processing errors at the DOR.

Between July 1, 1999 and June 30, 2000 there were over 36,000 instances where the calculated gross wages from the WR-30 exceeded gross wages on the NJ-927 by $322 billion. Additionally, the NJ-927 gross wages exceeded the WR-30 calculated gross wages in 51,000 instances by $5 billion.

A batch of WR-30s with identified errors was selected and the original documents were compared with the data file transmitted to the DOL by the DOR. Wages entered into the EAS exceeded actual wages reported on the original documents by $73 billion. The number of employees actually reported by employers totaled 282 while the number entered totaled 352. It appears that in a number of cases, incorrect data was created during the process at DOR. Errors noted included invalid social security numbers (less than nine digits), quarterly base weeks in excess of 13, unreasonable employee quarterly wages (over $1 billion) and non existent employees (jumbled letters and characters for names in the name fields).
**Recommendation**

We recommend that DOL establish proper verification and edit checks in the EAS to identify and reject erroneous data. We further recommend that the DOL periodically cross match NJ-927 with WR-30 to identify any large, unusual variances of reported wages warranting additional review.

**Auditee’s Response**

We concur in part. The department agrees that additional verification and edits would produce more accurate records. The department will work closely with the Division of Revenue (DOR) to determine the most cost effective means of establishing an improved system of verification and edits.

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**Delinquent Returns**

Employers are required to file a NJ-927 (Employer's Quarterly Report) and a WR-30 (Employer Report of Wages Paid) quarterly. These reports are due within 30 days after the end of the quarter. Reported information on these reports serve as a basis for experience rate calculations and for seven different assessments levied on employers based on gross wages and number of employees. Additionally, reported employee wages are used to determine eligibility and benefits payable to unemployed workers. Penalties are assessed for incorrect filing or late filing.

Our review of 98 randomly selected employers disclosed that 22 were delinquent in filing their NJ-927 for at least one quarter between the third quarter of 1998 and the second quarter of 2000. Thirty-six were delinquent in filing their WR-30 reports for at least one quarter during the same period. To ensure compliance with established laws and regulations, notices should be sent out to employers within a reasonable period of time to encourage them to submit required reports and to remit any taxes due. The DOL has not sent out notices on all delinquencies for over two years. Department
management informed us that they had been reluctant to mail out delinquency notices due to concerns regarding processing backlogs at the DOR which currently have been addressed by DOR.

**Recommendation**

We recommend that the DOL send out delinquency notices.

**Auditee’s Response**

We concur. The department has started to send out notices on a limited basis so that results can be monitored and necessary changes made to the Employer Accounts System based on feedback from employers.

## Security Administration

The department does not maintain appropriate formal information technology security policies and procedures for the current client/server processing environment. The absence of an adequate framework of policies and procedures designed to safeguard information against unauthorized use or loss weakens the internal control environment of the associated business processes. The impact of this deficiency is disclosed in the following additional suggested areas for improvements.

The assignment of roles and responsibilities to individuals should be implemented in a manner that would reduce the possibility for a single individual to undermine a critical business process. Management should also make sure that the access afforded to individuals throughout the information technology processing environment provides only that which is necessary to perform assigned roles and responsibilities.

The department has not established an adequate segregation of duties between individuals responsible for system support, administration, and information entry and use. The current privileges afforded to database administrators and programmers provide
them the ability to enter transactions in addition to
their respective responsibility for data administration
and program modification. The excessive privileges
granted to the security administrator provide the
unnecessary ability to enter and approve transactions
in most functional areas. The assignment of two
identifiers to the system administrator allows this
individual to enter and approve transactions in most
functional areas in addition to performing the
position’s required system administration functions.
A limited review of transaction audit tables did not
disclose any inappropriate use of availed access.
However, a reduction in the level of access provided
to these individuals should be evaluated, or
compensating controls to monitor their access should
be established.

Management should monitor the effectiveness of
security controls in the normal course of operations
through management and supervisory activities and
other routine operations. The Employer Accounts
System application uses a custom developed security
administration program package for controlling and
maintaining the assignment of all users’ access. This
package defines the user’s application role and form
access level using custom developed views based on
functional area positions. The assignment of form
access level is a manual process following the
guidance afforded by the positional views. Once
established, these assignments are not periodically
evaluated for current use or need. As a result, some
employees have inappropriate access.

The department does not conduct periodic reviews to
ensure that inappropriate user rights do not exist. A
sample of 46 application users identified ten whose
assigned access rights were inappropriate:

- five users were assigned access rights that were
different than that established for the individual’s
related position;
two users were granted multiple access rights to the same form;

two identifiers were established for sharing by a group of users; and

one user whose three assigned identifiers were not removed upon their separation from the department.

Inquiry regarding these items disclosed that no formal procedures exist to review the propriety of and need for granted user access. Management should establish a control process to review and confirm access rights periodically.

**Recommendation**

We recommend that the department develop and implement appropriate security policies and procedures and monitor the effectiveness of these procedures.

**Auditee’s Response**

We concur in part. There are policies and procedures in place, however, we recognize the need to improve and strengthen them. The Employer Accounts System is a new and complex system and controls will evolve as personnel become more familiar with it. The department has already begun to take corrective action.

The roles and responsibilities of all individuals assigned to the Data Center including database administrators, system administrators and programmers have been reviewed. As a result of this review, access levels have been redetermined so individuals have access to do only those tasks, which are necessary to perform assigned roles and responsibilities. The role of the security administrator will allow for only system administrator functions (the ability to add new users, modifying existing security of users, and delete users and removal of access rights).
The security logs will be reviewed so all-multiple login IDs are eliminated for all users and administrators.

A procedure will be put into place where the custom developed security administration package will be reviewed on a monthly basis to determine whether appropriate access is in place for all users. A procedure will be formalized whereby the ability to add, change and delete access rights or users is in place in the case of employee separation from the department or an employee’s job duties are modified.

Software Security Implementation

The Employer Accounts System application operates in a client/server processing environment. The major components of this platform are the operating system, network operating system, and database management software. Each of these components contains separate authentication mechanisms and logging features. The department has not implemented the following basic component security features.

Passwords are not required to be periodically changed.

Under the employed security scheme, the operating system, network operating system, and data base management application passwords are not required to be changed at regular intervals. Passwords should be changed periodically to prevent guessing and to maintain confidentiality. Currently, operating system password aging, and network security password management have not been implemented. The current version of data base management software does not support user password management; however, this capability could have been developed or remedied through acquisition of third party software. A sample of 46 users identified 25 whose identifiers and passwords were the same. The absence of password management impacts the
Attempts at an unsuccessful login are not limited or monitored.

Security violations and activity are not logged.

The department does not maintain controls to limit the number of unsuccessful application login attempts nor do they monitor for such attempts. To help ensure that passwords cannot be guessed, login attempts with invalid passwords should be limited. This can be accomplished by locking or disabling the applicable user identifier after an excessive number of failed login attempts have occurred. The current version of database management software does not support user password policy enforcement; however, this capability should have been addressed through acquisition of third party software.

The department does not monitor successful and unsuccessful connections to and disconnections from the database. Violation and security activity should be logged, reported, and reviewed on a regular basis to identify incidents involving unauthorized activity. The lack of monitoring could allow security incidents to occur unnoticed and cause damage to the entity’s computer resources and data. The current version of database management software supports the auditing of connections to and disconnections from the database. This option should be enabled to provide timely detection of unauthorized access attempts and to detect suspicious activity.

Recommendation

Logical access controls should be maintained to enable an entity to properly identify and monitor users authorized to access their computer resources. We recommend the department evaluate the appropriate options available and implement the necessary functionality to ensure effective authentication and access mechanisms.

Auditee’s Response

We concur in part. To the extent where it is practical and cost efficient to do so, we will improve controls in this area. Due to the newness of our system and its interfaces with systems controlled by another
State agency, some actions may not be practical or will require cooperation of the other agencies.

An Employer Accounts Password committee has been formed and has already met to develop new procedures involving password aging and network security password management. A procedure will be developed requiring users to change their password every forty-five days. The system will also be upgraded to establish controls to limit unsuccessful application login attempts and to produce reports of excessive unsuccessful attempts to login. The listener log has been turned on to log all connections to the database including the workstation accessing the system and the time of access.

An instance of Oracle 8i has been added to the TAX Servers to begin the process of upgrading the Tax system to Oracle 8i which will allow for the use of the password protection features of this version of Oracle. The Department of Labor is also in contact with FileNet and the Department of Revenue to upgrade the version of FileNet and provide for the ability to automate the synchronization of the passwords between Oracle and FileNet.