

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

**Department of Environmental Protection
Environmental Regulation and Selected Programs of
Compliance and Enforcement**

July 1, 2009 to December 31, 2011

**Stephen M. Eells
State Auditor**

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Enclosed is our report on the audit of the Department of Environmental Protection, Environmental Regulation and Selected Programs of Compliance and Enforcement for the period of July 1, 2009 to December 31, 2011. If you would like a personal briefing, please call me at (609) 847-3470.

A handwritten signature in black ink that reads "Stephen M. Eells".

Stephen M. Eells
State Auditor
July 2, 2012

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Scope

We have completed an audit of the Department of Environmental Protection, Environmental Regulation and selected compliance and enforcement programs related to Environmental Regulation for the period July 1, 2009 to December 31, 2011. The audit included financial activities for air quality, environmental safety and health, pesticide control, and solid and hazardous waste management, as well as their related compliance and enforcement programs. These activities are accounted for in the state's General Fund. Revenues for the audit period were \$185.5 million for these programs. Included in our scope were the Diesel Retrofit Program funded by \$49.8 million from a 4% dedication of the Corporate Business Tax (CBT) receipts, and \$1.7 million federal American Recovery and Reinvestment Act (ARRA) and \$644,000 for Diesel Emission Reduction Act (DERA) grant for the State Clean Diesel Grant Program. We also reviewed the New Jersey Environmental Management System (NJEMS) used by the department for the collection and review of permit applications, facility emission statements, testing documents, monitoring reports, and enforcement actions. Our expenditure tests were limited to the diesel programs.

Objectives

The objectives of our audit were to determine whether the financial transactions were related to the Environmental Regulation programs, were reasonable, and were recorded properly in the accounting systems. We also determined whether the diesel retrofit program utilized approved state contracted installers to perform the installations, the recommended devices were used and were meeting the updated emission standards, and the required one-time inspection forms were submitted timely. In addition, we determined whether compliance with ARRA requirements was achieved. We also determined whether the federal DERA funding was used to reimburse the approved vendors for retrofitted devices and whether the department submitted the required quarterly reports timely. Lastly, we also determined the adequacy of access controls over the processing of data relating to the department's billing and revenue collection cycle which were processed through the NJEMS.

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 Statues.

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, the administrative code, circular letters promulgated by the Department of the Treasury, and policies and procedures 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 financial transactions. We read the budget messages, reviewed financial trends, and interviewed

department personnel to obtain an understanding of the programs and internal controls. We also reviewed ARRA and Diesel Emissions Reduction Act grant agreements applicable to the Diesel Risk Reduction program.

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. Transactions were judgmentally selected for testing.

Conclusions

We found that the financial transactions included in our testing were related to the programs, were reasonable, were properly recorded in the accounting systems, and were in compliance with the ARRA and DERA diesel grant requirements, where applicable. We also found the diesel retrofit program is utilizing the recommended devices installed by state approved contractors and were meeting the updated emissions standard; however, the one-time inspection forms were not submitted timely. We also determined the NJEMS access controls over the processing of data related to the department's billing and revenue collection cycle to be inadequate. In making these determinations, we have identified areas where improvements can be made to the verification of the retrofitted off-road equipment, the capturing of data in NJEMS, the receivables and collections included in the audit scope, and pesticide's cash receipts process that should be considered by management.

Diesel Retrofit Program

Off-road equipment should have a one-time verification of the installation.

The Diesel Retrofit Law of 2005 requires that the following classes of diesel vehicles be retrofitted.

- School buses
- Solid waste vehicles that are publicly-owned or used to perform solid waste services under a public contract
- Commercial buses
- Publicly-owned on-road vehicles and off-road equipment

The costs of the retrofits are reimbursed by the state. The benefits of this law are intended to be the reduction of harmful diesel emissions.

During our audit period, the department received \$49.8 million from the Corporate Business Tax (CBT) and expended \$26.4 million to retrofit these designated vehicles. Owners are required to get the retrofitted device installed by an approved state contracted installer. The vehicle owner is responsible for submitting a compliance form entitled *One-time Compliance Inspection* (OTCI) to the department on two separate occasions. Upon completion of the installation, the vehicle owner signs and submits the compliance form certifying completion of the installation to the diesel retrofit program unit in order for the contract vendor to be paid. The vehicle owner is also responsible for submitting the form after their next regularly scheduled vehicle inspection at which time the installation is verified and the form is signed by the inspector. A licensed Diesel Emission Inspection Center (DEIC) certifies the installation for the solid waste and publicly owned vehicles, and the Motor Vehicle Commission (MVC) Inspection Unit certifies for school and commercial buses. Our review of the documentation received by the department's diesel inspection unit found that these vehicles are meeting the new retrofit standards. However, the owners of the off-road equipment are exempt from the OTCI verification and are not required to have an emission test performed. The department estimates there are 500 off-road pieces of equipment and one has been retrofitted as of December 2011. Although there are no standards in place to measure the reduction in emissions, the department should visually verify the installations.

One-Time Compliance Inspection forms should be submitted timely.

We tested 105 vehicles and found 52 cases where the OTCI form was not submitted to the department. A December 2011 report indicated the OTCI form with an inspector's signature had not been submitted to the department for 4,456 of the 9,997 vehicles retrofitted. The vehicle owner has one year from the date of installation to submit this form. We found that, because of limited staffing, the unit responsible for monitoring the submission of the OTCI has not been following up with the vehicle owners who have not submitted their forms, nor has the unit been forwarding the non-reporting vehicle owners to the department's compliance and enforcement

unit for further follow up. As a result of our audit, the diesel retrofit program unit is now notifying the compliance and enforcement unit of delinquent form submissions. Although the diesel retrofit program is not required by law to ensure the devices are functioning as intended, periodic inspection result reports prepared by DEIC or MVC can be used by the department to assist in determining whether the retrofit standards are being met.

Recommendation

We recommend the department have at least a one time visual inspection performed for retrofitted off-road equipment to verify the installation. We also recommend the diesel retrofit program unit continue to refer those non-reporting vehicle owners to the compliance and enforcement unit for further follow-up to ensure the OTCI form signed by a DEIC or MVC inspector is submitted. Furthermore, the department's diesel inspection unit could share the inspection reports from DEIC and MVC with the diesel retrofit program unit to assist in determining whether the devices have been installed.

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New Jersey Environmental Management System (NJEMS)

The NJEMS was originally designed as a database management system for air permit activities in the late 1990s. The department gradually enhanced the usage to other programs and linked additional databases. Most inspection, assessment, billing, and revenue collection transactions are now processed through NJEMS. The department also built an internet portal to allow the public to input license and registration data that is uploaded to NJEMS, along with e-check and credit card payment information.

NJEMS programming support is performed by a contract vendor. The department personnel work together with the vendor in the design phase of NJEMS applications and specify the needs and controls that should be in place. The vendor writes the programming language for the department and finalizes the applications. However, the department personnel are responsible for the administrative and database management functions for NJEMS.

Our audit focused on the NJEMS Assessments module, which is the primary departmental billing and revenue collection system. We have noted the following system issues.

Segregation of Duties

NJEMS access controls should be improved.

Employees with update access for the Assessments module have the ability to adjust billable amounts, and to create and cancel bills. As of September 12, 2011, 81 employees have this capability for the programs within our audit scope. These functions should be segregated and/or closely monitored by a supervisor to ensure transactions are handled appropriately. When an employee adjusts a billable amount to \$0, the NJEMS automatically changes the bill status to

“Closed Paid in Full”. This makes it appear as though the regulated entities have satisfied their debt and are in good standing with the department. Since standard reports for these transactions are not produced on a regular basis for management review, these transactions are at a heightened risk. Many of the employees with this update access receive checks, even though the department payment instructions state the checks are to be sent directly to the Department of the Treasury, Division of Revenue. Employees with this update access for the Assessments module also have the ability to adjust bills for other departmental programs that are on NJEMS. There is no restriction built into NJEMS that would allow for program specific access.

In addition, we found that 66 employees with the update access to the Assessments module also had the ability to add/delete billable entities from the NJEMS Masterfile. Since transactions are not systematically monitored, allowing employees to adjust bills and add/delete billable entities may allow for errors or fraud to occur and remain undetected by management.

Accounting for Penalties

Abatements arising from debt negotiations should be accounted for.

There is a lack of accounting and audit trails in NJEMS when enforcement penalties are adjusted. For the majority of enforcement penalties, department inspectors routinely offer violators a 50 percent reduction of the penalty, if the regulated entity signs a negotiated settlement agreement. NJEMS does not account for this penalty abatement. Department employees enter the discounted portion of the debt as the full billable amount. Also, if a settlement agreement is not signed initially but is agreed upon afterwards, the full amount of the original bill is canceled and a new bill is created for the discounted amount. In addition, unless the NJEMS user references the new bill number, no audit trail would be created cross referencing these transactions. Proper accounting procedures dictate the full penalty and abatement amounts be recorded.

Transfers

Source of incoming debit and credit transfer bill number should be recorded.

NJEMS has no data field to record and track debit and credit transfers. These transactions are necessary to reallocate funds for the payment of multiple bills with one check. There is no audit trail to identify the bill numbers impacted by these transactions.

Permit and License Periods

Permit and license periods should be recorded.

There are no data fields in the Assessments module that identifies permit and license periods. When payments are made late it is not clear what period the payment is for. This makes it very difficult to ensure payments were received for these specific activities.

Revenue Reconciliations

Revenue reconciliations should be performed.

There are limited revenue reconciliation procedures in place. We analyzed selected solid waste revenue sources within our audit scope to determine if revenue reconciliation and verification procedures are feasible. Under the current system structure, we were unable to perform a complete reconciliation. However, we have concluded that with minor system changes revenue reconciliation would be possible. This would significantly strengthen internal controls over the billing and revenue collection cycle.

Recommendation

We recommend the department implement the following controls.

- Management should restrict employees' access rights to match their job responsibilities. Controls should be added to NJEMS that would segregate employees' ability to add, delete, or adjust billable amounts and only allow employees access to update bills in their specific program. A report should be generated for these types of transactions and should be reviewed by management for propriety.
- A data field should be created in NJEMS to account for abatement amounts arising from debt negotiations.
- A data field should be created for recording the bill number when debit and credit transfers are required.
- Date fields should be added that would capture the license and permit periods to improve reporting, internal control, and monitoring.
- Revenue reconciliation procedures should be developed in order to verify that all revenues are received and recorded.

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Receivables

The department should comply with the Department of the Treasury's collection guidelines.

We found that the department collection efforts could be more aggressive at pursuing outstanding debt for licenses, permits, and other fee type revenues. Receivables for these revenues should be minimal. Following is a summary of the outstanding receivable balances by fiscal year for programs within our scope as of September 2011 per NJEMS.

Fiscal Year Ending June 30	2008	2009	2010	Total
Outstanding Receivable Balances	\$723,305	\$757,615	\$1,332,557	\$2,813,477

Our discussions with agency personnel disclosed that the receivable amounts above may need to be reviewed and adjusted by program management.

The Department of the Treasury Circular Letters 06-03-OMB and 11-20-OMB require agencies to transfer uncollected debt after 90 days to the Department of the Treasury, Division of Revenue for further collection efforts. We found only \$390,000 of the \$2.8 million has been transferred for collection. There is no automatic collections referral built into NJEMS. Instead, the program units are responsible for manually changing the bill status so the receivable can be forwarded for collection. Our discussions with program personnel disclosed that most were unaware of this manual task.

Recommendation

We recommend the department review the receivable detail to determine their collectability and forward those items over 90 days old to the Department of the Treasury, Division of Revenue for collections in accordance with the circular letters.

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Bureau of Pesticide Operations

Controls over cash receipts should be strengthened.

The Bureau of Pesticide Operations certify and license pesticide applicators and dealers in the state, register pesticide products, and issue permits for aquatic pesticide use. Annual revenues during our audit period averaged \$5 million of which \$1 million was collected at the program level.

Checks are received by the secretary at the program level who also logs in and distributes the checks to various employees for verification. We were unable to determine whether the checks were restrictively endorsed. Once verified, the checks are returned to the secretary who then prepares a deposit report and sends the checks and report to the Department of the Treasury, Division of Revenue for deposit. Excessive handling of checks and lack of segregation of duties increases the possibility of theft or loss and delays deposit.

Recommendation

We recommend checks received by the bureau be immediately endorsed and deposited in accordance with state guidelines. We also recommend there be a segregation of duties over the initial processing and logging of checks and preparation of deposit reports.

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State of New Jersey

Department of Environmental Protection

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BOB MARTIN
Commissioner

June 26, 2012

Mr. John J. Termyna
Assistant State Auditor
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125 South Warren Street
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Dear Mr. Termyna:

Thank you for the opportunity to review and respond to the draft audit report regarding the Department of Environmental Protection, Environmental Regulation and Selected Programs of Compliance and Enforcement, for the period July 1, 2009 to December 31, 2011.

We are pleased that the audit concluded that the financial transactions included in your testing were related to the programs, were judged to be reasonable and were accurately and properly recorded in the State's accounting systems. Also, you noted our compliance with applicable ARRA and DERA Diesel Grant requirements.

The audit report also noted certain matters which merit Management's attention. We hereby offer information on current program status, as well as our planned corrective actions to address these issues and their corresponding recommendations.

DIESEL RETROFIT PROGRAM

Recommendation: We recommend the Department have at least a one-time visual inspection performed for retrofitting off-road equipment to verify the installation. We also recommend the diesel retrofit program unit continue to refer those no-reporting vehicle owners to the compliance and enforcement unit for further follow-up to ensure the OTCI form signed by a DEIC or MVC inspector is submitted. Furthermore, the Department's diesel inspection unit could share the inspection reports from DEIC and

MVC with the diesel retrofit program unit to assist in determining whether the devices have been installed.

Response: The Bureau of Mobile Sources agrees with the recommendation that visual verifications should occur to confirm installation of retrofit devices on off-road equipment, although not required by the Mandatory Diesel Retrofit Law (P.L. 2005, C.219). We plan to verify a sampling in installations covering a cross-section of authorized installers, device types and equipment owners. We will perform the verifications during the next several years as the retrofit devices are installed on the off-road equipment. The Bureau also agrees with the recommendation to use any available opacity inspection results received by the diesel inspection unit to determine whether retrofits have been installed on on-road vehicles, as required the Mandatory Diesel Retrofit Law.

NEW JERSEY ENVIRONMENTAL MANAGEMENT SYSTEM (NJEMS)

Recommendation: Management should restrict employees' access rights to match their job responsibilities. Controls should be added to NJEMS that would segregate employees' ability to add, delete, or adjust billable amounts and only allow employees access to update bills in their specific program. A report should be generated for these types of transactions and should be reviewed by management for propriety.

Response: A design session was held with our contract vendor on May 21, 2012 to create a security group that would limit access to a particular program area. We will meet with the NJEMS Core Team to discuss limiting access to the Assessments module based more closely on job duties, however, with staff decreasing it is sometimes necessary for the same staff person to perform duties which may seem to be in conflict. Once the security is in place, the report may not be needed.

Recommendation: A data field should be created in NJEMS to account for abatement amounts arising from debt negotiations.

Response: A design session was held with our contract vendor on May 21, 2012 to determine how to make it more clear to the user an initial assessment and then the final assessment. At this time, we are proposing to "link" the records using an internal system identification number and then have the ability for the user to display all of the "linked" records. Because our assessment records in an enforcement case are linked on a one to one basis with activities (i.e., initial penalty notice and settled penalty notice), there was no visual or database link between these assessments – this enhancement will provide a step toward making this link more transparent.

Recommendation: A data field should be created for recording the bill number when debit and credit transfers are required.

Response: A design session was held with our contract vendor on May 21, 2012 to add fields to the database and to the user interface to show the bill identification number of the record from which and to which monies have been transferred. For example, in a credit record, the bill identification number of the record from which the money was transferred will be displayed and in the debit record the bill identification number of the record to which the money was transferred will be displayed.

Recommendation: Date fields should be added that would capture the license and permit periods to improve reporting, internal control, and monitoring.

Response: A design session was held with our contract vendor on May 21, 2012 to determine how best to capture the license/permit periods. By policy, the Assessment Start Date and Assessment End Date fields are designed to capture this information for licenses, permits, enforcement actions, and fees. There is a mechanism to auto populate these fields, which requires some programming. Our contract vendor will work with each license/permitting program to determine the rules for determining the start and end date of the license/permit and will add programming to NJEMS to auto populate the Assessment Start Date and Assessment End Date. With this programming in place, reporting, internal control and monitoring should be made easier.

Recommendation: Revenue reconciliation procedures should be developed in order to verify that all revenues are received and recorded.

Response: NJDEP is working with the Department of Treasury to reconcile our revenue data. Currently, there are areas where NJEMS and VCL (the Treasury mainframe system) are out of sync. Since the VCL system is antiquated, it is not likely that changes to this system will occur. The VCL system does not allow for reporting to an electronic output or customized reporting by users and therefore, it is difficult to reconcile that data entering VCL is being captured by NJEMS appropriately. NJDEP will continue to work with the Department of Treasury to improve the reconciliation of revenues received and recorded.

The enhancements discussed in the May 21, 2012 design session with our contract vendor, as noted above, will be developed over the summer with testing in November 2012 and implementation in January 2013.

RECEIVABLES

Recommendation: We recommend the Department review the receivable detail to determine their collectability and forward those items over 90 days old to the Department of Treasury, Division of Revenue for collections in accordance with the Treasury circular letters.

Response: Over the past ten months, from September, 2011 thru June, 2012, the Department has been engaged in a vigorous and thorough review of all receivables resulting from licenses and permits, as well as from fines and penalty assessments. This review, conducted via an internal task force, guided by our Chief of Staff, along with various Assistant Commissioners, has resulted in a significant, measurable and on-going increase in debt referrals to the Treasury's Division of Revenue.

In addition, we are currently exploring additional enhancements to our NJEMS Assessments module which would enable automatic referral of debt once the 90 day collection period has expired.

Also, all operating units are now aware, through the task force's efforts, of the reporting and referral requirements of Treasury Circular Letters 06-03-OMB and 11-20-OMB, and the Department will strive to achieve full compliance with those mandates.

BUREAU OF PESTICIDES OPERATIONS

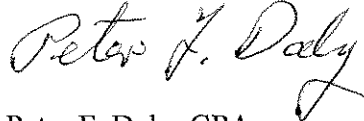
Recommendation: We recommend checks received by the Bureau be immediately endorsed and deposited in accordance with state guidelines. We also recommend there be a segregation of duties over the initial processing and logging of checks and preparation of deposit reports.

Response: All checks received by the Bureau, via mail, are now immediately endorsed and logged in the Bureau's Program database. Over the past few years, the Bureau has implemented online payment options for licenses and pesticide products. The Bureau continues to emphasize this online payment feature through the Department's website and mailings. The Bureau also encourages the regulated community to directly send their payment to the Department of Treasury, Division of Revenue for faster processing. The Bureau plans, that within nine months, to have the Aquatic Pesticide Permits Program fully accessible online, including payment. This alone will potentially eliminate approximately 500 paper check payments from being submitted to our Bureau for processing. The Bureau is currently looking at other Programs that may benefit from this automated online payment/processing that will lessen the burden to both the regulated community, as well as, to the Bureau in these times of diminishing staffing allocations.

Regarding segregation of duties, the Bureau employs compensating internal control procedures, i.e., supervisory verification of payment/deposit functions and monthly reconciliations of transaction data.

In closing, I would like to commend both the field audit staff for their professionalism and thoroughness exhibited during the course of the audit, as well as, the management and technical review staff for excellent oversight and guidance during this engagement.

Sincerely,

A handwritten signature in cursive script that reads "Peter F. Daly". The signature is written in black ink and is positioned above the printed name.

Peter F. Daly, CPA
Controller

C: Bob Martin, Commissioner
Magdalena Padilla, Esq., Chief of Staff