



State of New Jersey

DEPARTMENT OF LABOR

JAMES E. MCGREEVEY
Governor

ALBERT G. KROLL
Commissioner

March 18, 2002

Michael T. Hill
Regional Inspector General for Audit
U.S. Department of Labor
Office of Inspector General
The Wanamaker Building
100 Penn Square East, Suite 602-B
Philadelphia, Pennsylvania 19107

Dear Mr. Hill:

We are responding to the draft report titled "Audit of Indirect Costs Charged to U.S. Department of Labor Grant Awards During the Period October 1, 1997 through September 30, 2001." While we welcome this opportunity to respond, we believe additional work on-site prior to the issuance of a final report would be beneficial to each organization.

The findings in the report will allow us to reconsider our approaches/methodologies for charging indirect costs to the federal grants. To the extent that this can be done efficiently and provides a more accurate accounting, it will be in our best interests to do so. However, we do not completely agree with the current findings which indicate that NJDOL has overcharged indirect costs or has used an inappropriate cost methodology.

We do agree that certain costs were not taken into account when the federal Unemployment Insurance Grant was reimbursed for collection costs of State taxes. However, the fact remains that the federal grant was reimbursed for significant costs in this area. These costs were not audited by the audit team. Had they done so, it would have revealed the fact that these charges were much more than should have been allocated. We believe these charges provide an offset to costs that, as correctly identified in the audit, were never charged. As the title of the report indicates, this was to be an audit of costs charged to the grant. Such an audit should address what was actually charged and not only what was not charged.



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DIVISION OF ACCOUNTING

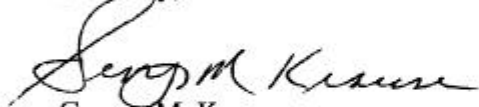
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AD-18.62 (1-02)

The Government Auditing Standards under which this audit was conducted provides for the evaluation by the auditor of auditee comments and a modification to the report if they find the comments valid. As previously indicated, information regarding our position is available for your review and we request that it be reviewed, if possible, prior to the issuance of the report. If that is not practical, we would appreciate your acknowledgement of our position and the fact that the actual allocation methodology for accounting for costs between the tax programs was not audited and needs to be included in any audit before any overall conclusion can be appropriately made as to whether the federal grant was overcharged.

The attachment to this letter provides the department's position in summary form. We are maintaining the detail at our site. We look forward to using your audit findings to make improvements in our allocation processes, and we believe that working together with our federal partner, the audit can be resolved to our mutual satisfaction.

Sincerely,



George M. Krause
Director and Chief Financial Officer

Attachment

**NEW JERSEY DEPARTMENT OF LABOR
RESPONSE TO
U.S. DEPARTMENT OF LABOR
AUDIT OF INDIRECT COSTS CHARGED TO
USDOL GRANT AWARDS
OCTOBER 1, 1997 THROUGH SEPTEMBER 30, 2001**

The New Jersey Department of Labor (NJDOL) does not concur with the audit's contention that indirect costs were overcharged to federal DOL grant awards by \$6.2 million for AS&T costs over the four year period. While certain costs amounting to \$4.8 million for AS&T were not reimbursed for tax operations, there was a corresponding over-reimbursement approximating \$6 million to the federal grant of costs associated with the joint tax operation. For the balance of the costs, \$1.4 million questioned in the audit, we disagree with the auditor's contention that our methodology is incorrect. While the method applied by the auditor is a valid approach, we also believe that direct charging of costs to a program is an acceptable practice. Therefore, until this methodology is eliminated, it is our position that the \$1.4 million is not due to the U.S. Department of Labor (USDOL). Should we not prevail in this position, the overall net effect of the two findings should leave NJDOL with no amounts due to USDOL.

The following details our position concerning each finding:

USDOL Finding 1 (Draft Audit Report, Page 9)

Although NJDOL reimbursed the UI account for certain UI tax collection costs properly allocable to state-funded programs, it failed to reimburse the UI account for about \$4.8 million in departmental AS&T costs also allocable to these state-funded programs. Instead, the \$4.8 million in AS&T costs were charged to and recovered on the DOL UI grants. These AS&T costs should have been charged to state-funded programs in accordance with Federal cost principles, and as provided in a written agreement between DOL and NJDOL for sharing of tax collection costs, because the UI tax function also collects three state taxes. The agreement states that the shared costs include departmental administrative costs (i.e., AS&T costs).

NJDOL Response

We concur in part.

We agree with the finding that certain AS&T costs were not allocated to State funded programs which operate joint tax activities with the Unemployment Insurance Program. The above statement, however, indicates that NJDOL did reimburse UI for certain other joint UI tax collection costs that were properly allocable to State-funded programs. Since these costs were not audited by the auditors, a statement that they were "properly" charged cannot be made. While the audit initially started to review the allocation of costs between the joint tax programs, it became focused only on what was not allocated – the departmental AS&T. Our review of the allocations made has determined that UI costs not associated with the joint tax collection process

have been reimbursed to the federal grant in the current methodology in use by NJDOL. The departmental results are presented in Exhibit I. The UI federal fund was over-reimbursed with State funds in the amount of \$6,069,667 during this four year period.

While we understand that as prudent auditors the evidence must be reviewed before you can form your opinion on this, we have attached a schedule (Exhibit II) that shows the breakout of the cost centers which had a portion of their overhead charged to State programs for the joint tax function. As is evidenced by the centers names and descriptions, most are not applicable to the tax function. Using the example cited on page 11 of the draft audit, we can provide clear evidence to support the premise behind our rationale for Exhibit II.

Attached as Exhibit III is the page from our original allocation for the month of September 2000. The audit states that the allocation of personal service costs and an equitable portion of the overhead came to \$598,697 – which number is shown on the exhibit. The overhead portion \$233,068 that was charged, however, was not in fact equitable. A detail of the make-up of that amount shows that only \$32,790 is related to tax function overhead. Had these costs been reviewed as part of the audit, it would have become clear there was an over-reimbursement to UI. The analysis of this over the four year period is what constitutes Exhibit II. Details from our cost accounting system are available and support these numbers. However, the make-up of the overhead charged such as UI operations, Board of Review, etc. would in itself be prima facie evidence to support our position.

We therefore only partially concur with the finding and continue to assert that prior to any overall conclusion as to whether the federal grant has been overcharged, that this issue of what was charged must be taken into account.

USDOL Finding 2 (Draft Audit Report, Page 9)

The allocation base used by NJDOL to distribute its AS&T costs to its final cost objectives was flawed because it excluded several State projects funded by State general fund revenue. This resulted in DOL grant awards being allocated about \$1.4 million more than their fair share of the AS&T costs.

NJDOL Response

We do not concur.

The audit disagrees with the methodology in use for allocating departmental indirect costs. Certain State funded projects were excluded from the allocation base and therefore it was believed these projects did not pay their share of those costs. We disagree in that State funded projects were direct charged for their costs. OMB Circular Letter A-87 states there is no universal rule for classifying certain costs as either direct or indirect under every accounting system. Therefore, certain costs were direct charged to the State programs. While we acknowledge we will review the auditors methodology for consideration of a change, we do not believe any funds are due back to the USDOL, since direct charging of State programs does not violate any federal requirement.

**NJDOL CALCULATION
OF OVER-REIMBURSEMENT TO
FEDERAL UI GRANT**

| | <u>FY 1998</u> | <u>FY 1999</u> | <u>FY 2000</u> | <u>FY 2001</u> | <u>Total</u> |
|---|------------------|------------------|------------------|------------------|------------------|
| Total Overhead Charged (PS) | | | | | |
| Monthly Joint Tax Allocations | 1,784,209 | 1,617,113 | 1,539,681 | 1,538,029 | |
| Revised Allocation | 592,169 | 636,887 | 697,609 | 676,263 | |
| Variance (PS) | 1,192,039 | 980,226 | 842,072 | 861,766 | |
| Personnel Benefits | 21.4% | 23.73% | 26.34% | 25.4% | |
| | 255,096 | 232,608 | 221,802 | 218,888 | |
| Non-Personal Services | 31.94% | 33.08% | 30.08% | 35.63% | |
| | 380,737 | 324,259 | 253,127 | 307,047 | |
| TOTAL VARIANCE PS/PB/NPS | 1,827,873 | 1,537,092 | 1,317,001 | 1,387,701 | 6,069,667 |
| LESS: | | | | | |
| Joint Tax AS&T Costs not reimb. per OIG | 1,106,939 | 1,193,479 | 1,258,636 | 1,216,282 | 4,775,336 |
| NET VARIANCE | 720,934 | 343,613 | 58,365 | 171,419 | 1,294,331 |

| | |
|--------------|------------------|
| TOTAL | |
| FY 1998 | 720,934 |
| FY 1999 | 343,613 |
| FY 2000 | 58,365 |
| FY 2001 | 171,419 |
| | <u>1,294,331</u> |

Exhibit II

DETAIL OF UI OVERHEAD COST CENTERS
CHARGED TO STATE PROGRAMS

| COST CENTER | DIVISION/OFFICE | FY 1998 | FY 1999 | FY2000 | FY 2001 |
|--------------------|--------------------------|---------------------|---------------------|---------------------|---------------------|
| 03A00500/550 | Commissioner/D. Comm. | 0.00 | 2,696.08 | 2,019.79 | 0.00 |
| 03C01000 | Admin. & Finance | 80,330.26 | 77,776.44 | 57,368.72 | 112,651.79 |
| 03A00800 | Board of Review | 3,370.15 | 6,185.57 | 6,948.02 | 11,159.51 |
| 03C01300 | Labor, Plan. & Analysis | 449,849.46 | 672,712.51 | 575,102.75 | 568,582.15 |
| 03C01410 | Employer Accounts | 1,510,254.57 | 1,443,968.30 | 1,532,640.14 | 1,474,481.34 |
| 03C02000 | Workforce NJ | 46,589.38 | 89,801.56 | 75,367.38 | 141,792.19 |
| 03A04000 | Asst. Comm. Income Sec. | 384,969.10 | 18,354.76 | 26,550.09 | 189,512.53 |
| 03C04500 | UI Operations | 9,526,796.43 | 9,001,329.94 | 7,990,721.93 | 7,863,565.74 |
| 03C05020 | Disability Insurance | 0.00 | 0.00 | 279.98 | 3,455.22 |
| 03C06000 | Labor Standards | 2,361.31 | 216.09 | 0.00 | 1,112.39 |
| | TOTAL | 12,004,520.66 | 11,313,041.25 | 10,267,018.80 | 10,366,312.86 |
| | 03C00500 | 12,004,520.66 | 11,313,041.25 | 10,267,018.80 | 10,366,312.86 |
| | Variance | 0.00 | 0.00 | 0.00 | 0.00 |

Of the above listed cost centers, only 03C01410 Employer Accounts pertains to the joint tax operation.

STATE OF NEW JERSEY - DEPARTMENT OF LABOR
 STATE PROGRAM - UI TAX COLLECTION PLAN OF ALLOCATION
 MONTH OF: SEPTEMBER 2000

Exhibit III

| PROJECT ACTIVITY CODE | DOLLARS CHARGED | POSITIONS PAID |
|-----------------------|--------------------|-------------------|
| 210 - 306 | 101,719.60 | 34.11 |
| 307 | 51,777.53 | 17.34 |
| 311 | 160,810.96 | 41.97 |
| 312 | 228,020.32 | 52.16 |
| 314 | 258,033.02 | 76.95 |
| 325 | 52,149.63 | 12.24 |
| | | |
| TOTAL | 852,511.06 | 234.77 |
| 210 - (400-440) | 830,457.57 | 210.92 |
| 210 TOTAL | 3,868,038.81 | |

CALCULATION OF UI OVERHEAD APPLICABLE TO STATE PROGRAMS: TOTAL

| | | |
|-----------------|---|------------|
| PERCENTAGE RATE | = | 28.07% |
| OVERHEAD | = | 233,067.92 |
| POSITIONS PAID | = | 59.19 |

| CALCULATION OF ALLOCABLE COSTS: | TOTAL | D I S | HEALTH CARE | WORKFORCE |
|---------------------------------|-------------------------|------------|-------------|-----------|
| ALLOCABLE P/S COSTS | 598,696.81 ¹ | 389,152.93 | 191,582.98 | 17,960.90 |
| POSITIONS PAID | 162.12 | 105.38 | 51.88 | 4.86 |
| YTD EQUIVALENT POSITIONS | 166.85 | 108.45 | 53.39 | 5.01 |
| PERSONAL SERVICES | 598,696.81 | 389,152.93 | 191,582.98 | 17,960.90 |
| PERSONAL BENEFITS | 25.25% 151,170.94 | 98,261.11 | 48,374.70 | 4,535.13 |
| NON-PERSONAL SERVICES = | 36.21% 216,764.17 | 140,896.71 | 69,364.53 | 6,502.93 |
| TOTAL COSTS ALLOCATED | 966,631.92 ¹ | 628,310.75 | 309,322.21 | 28,998.96 |

¹ Amount per audit report - page 11

UI OVERHEAD CHARGES
210-(400-440)
SEPTEMBER 2000

| COST CENTER | DIVISION/OFFICE | AMOUNT |
|--|-----------------------------|---------------------|
| 03A00500/550 | Commissioner/D. Comm. | 0.00 |
| 03C01000 | Admin. & Finance | 5,934.70 |
| 03A00600 | Board of Review | 188.40 |
| 03C01300 | Labor, Plan. & Analysis | 40,942.86 |
| 03C01410 | Employer Accounts | 116,817.26 |
| 03C02000 | Workforce NJ | 2,310.84 |
| 03A04000 | Asst. Comm. Income Security | 20,052.97 |
| 03C04500 | UI Operations | 644,210.54 |
| 03C05020 | Disability Insurance | 0.00 |
| 03C06000 | Labor Standards | 0.00 |
| | | 830,457.57 |
| | | 830,457.57 |
| Total 210 Charges Sept. 2000 | | 3,868,038.81 |
| Less UI Overhead | | 830,457.57 |
| Net UI | | 3,037,581.24 |
| Tax Functions/Net UI (852,511/3,037,581) | | 28.07% |
| Overhead Applicable to State Programs: | | |
| 830,457 * 28.07% | | 233,068 |
| | | 233,068 |

Of the above listed Cost Centers, only 03C01410 Employer Accounts pertains to the joint tax operation.

Approximate overhead applicable to Employer Accounts (Tax Functions) is as follows :

$$\$116,817 \times .2807 = \$32,790$$