

**STATE OF NEW JERSEY  
DEPARTMENT OF LABOR  
P. O. BOX 110  
TRENTON, NEW JERSEY 08625**

**AUDIT OF INDIRECT COSTS CHARGED TO  
U.S. DEPARTMENT OF LABOR GRANT AWARDS  
DURING THE PERIOD  
OCTOBER 1, 1997 THROUGH SEPTEMBER 30, 2001**

**This audit report was prepared by Tichenor & Associates, LLP, under contract to the U.S. Department of Labor, Office of Inspector General, and, by acceptance, it becomes a report of the Office of Inspector General.**

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**Acting Deputy Inspector General for Audit  
U.S. Department of Labor**

**Report No: 03-02-002-03-315**

**Date Issued: March 29, 2002**

**TICHENOR & ASSOCIATES, LLP  
CERTIFIED PUBLIC ACCOUNTANTS AND MANAGEMENT CONSULTANTS**

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## TABLE OF CONTENTS

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<b>ACRONYMS AND GLOSSARY</b> .....	i
<b>EXECUTIVE SUMMARY</b> .....	1
<b>INTRODUCTION</b> .....	4
Background .....	4
Objectives and Scope .....	7
Federal Cost Reimbursement Principles .....	7
<b>FINDINGS</b> .....	11
1. NJDOL Failed to Reimburse UI Grants for AS&T Costs When It Reimbursed Other Costs for the Collection of State Taxes .....	12
2. Allocation Base Used by NJDOL to Distribute its AS&T Costs was Flawed Because Certain State-Funded Projects were Excluded .....	16
<b>CONCLUSIONS AND RECOMMENDATIONS</b> .....	19
<b>INDEPENDENT ACCOUNTANT'S REPORT ON AUDIT</b> .....	21
<b>EXHIBITS</b>	
Exhibit A. Departmental AS&T Costs Applicable to UI Tax Function that Should Have Been Reimbursed by NJDOL to UI Grants .....	24
Exhibit B. Comparison of NJDOL and Auditor Allocation of AS&T Costs to DOL Grants for FFY 1998 .....	25
Exhibit C. Comparison of NJDOL and Auditor Allocation of AS&T Costs to DOL Grants for FFY 1999 .....	26
Exhibit D. Comparison of NJDOL and Auditor Allocation of AS&T Costs to DOL Grants for FFY 2000 .....	27
Exhibit E. Comparison of NJDOL and Auditor Allocation of AS&T Costs to DOL Grants for FFY 2001 .....	28
<b>AUDITEE'S RESPONSE</b> .....	29



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## ACRONYMS AND GLOSSARY

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AS&T	Administrative Staff and Technical (indirect costs)
CFR	Code of Federal Regulations
CPA	Certified Public Accountant
DOL	U.S. Department of Labor
ETA	U.S. Department of Labor, Employment and Training Administration
FFY	Federal Fiscal Year - October 1 to September 30
HHS	U.S. Department of Health and Human Services
NJDOL	New Jersey Department of Labor
OCD	U.S. Department of Labor, Office of Cost Determination
OIG	U.S. Department of Labor, Office of Inspector General
OMB	U.S. Office of Management and Budget
OSHA	Occupational Safety and Health Administration
SWCAP	Statewide Cost Allocation Plan
UI	Unemployment Insurance

## **GLOSSARY**

- Direct Cost:** A cost that can be identified specifically with a particular cost objective, e.g., the DOL Unemployment Insurance Program.
- Indirect Cost:** A cost which cannot be identified with a single, final cost objective, but is identified with two or more final cost objectives, one or more of which benefits Federal programs. Such costs are combined into groupings or pools for distribution to benefitting final cost objectives. Indirect cost pools should be distributed to benefited cost objectives on bases that will produce an equitable result in consideration of relative benefits derived.
- Questioned Cost:** A cost that is questioned because of:
- (a) an alleged violation of a provision of a law, regulation, contract, grant, cooperative agreement, or other agreement or document governing the expenditure of funds; or
  - (b) at the time of the audit, such cost is not supported by adequate documentation; or
  - (c) the expenditure of funds for the intended purpose is unnecessary or unreasonable.

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## EXECUTIVE SUMMARY

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Tichenor & Associates, LLP, Certified Public Accountants and Management Consultants, under contract to the U.S. Department of Labor (DOL), Office of Inspector General (OIG), conducted an audit of the Administrative Staff and Technical (AS&T) costs claimed by the New Jersey Department of Labor (NJDOL) as being applicable to grant awards from the DOL. Our audit covered Federal fiscal years (FFYs) ended September 30, 1998, 1999, 2000, and 2001. NJDOL records show that it claimed and was reimbursed by DOL for over \$54.2 million of indirect costs for the 4-year period covered by our audit.

Our audit found that the NJDOL did not comply with OMB Circular A-87 requirements that indirect costs, such as AS&T costs, be allocated to all projects/programs on the basis of "relative benefits received." Our audit disclosed that for the 4-year period ended September 30, 2001, NJDOL had billed and received a total of over \$54.2 million in AS&T costs from DOL. However, NJDOL's actual allowable AS&T costs properly allocable to DOL grant awards, on the basis of "relative benefits received," totaled only \$48.0 million during this period. As a result, NJDOL overcharged DOL grant awards by about \$6.2 million for AS&T costs during this 4-year period.

Based on our audit, we question \$6,166,318 in AS&T costs claimed and recovered by NJDOL on DOL grant awards during the 4-year period ended September 30, 2001, primarily because:

- Although NJDOL reimbursed the Unemployment Insurance (UI) grant account for certain UI tax collection costs allocable to State tax programs which "piggy-back" on the UI tax collection system, it failed to include departmental AS&T costs in the amounts reimbursed. Consequently, the total costs charged to DOL for the UI program included AS&T costs that should have been reimbursed by State-funded programs.
- The allocation base used by NJDOL to distribute its AS&T costs to final cost objectives was flawed because it did not include all projects.

The net effect of the matters summarized above was a substantial shifting of costs from NJDOL's State programs (to which such costs were properly allocable) to DOL grant awards, resulting in a significant overrecovery of indirect costs on the DOL grant awards. We expect that a similar overrecovery of indirect costs on DOL grant awards will also occur in FFY 2002 because the conditions discussed above had not changed as of the completion of our fieldwork in December 2001.

## **Recommendations**

We recommend that the cognizant DOL grant officer(s) to: (1) direct NJDOL to refund the \$6,166,318 in AS&T costs which it over-recovered for FYs 1998, 1999, 2000, and 2001; and (2) to adjust its billings to DOL for FY 2002 for AS&T costs to preclude further overrecoveries of AS&T costs.

Further, we are recommending that the Assistant Secretary for Employment and Training direct NJDOL ensure that its proposals on AS&T cost allocation methodology rate proposals fully comply with the reasonableness, allocability, and allowability criteria mandated by OMB Circular A-87; and that the Assistant Secretary for Employment and Training direct NJDOL to include a provision in its annual audit plans for periodic audit of the implementation of negotiated agreements applicable to the sharing of UI tax collection costs and the allocation of AS&T costs directly to projects.

\* \* \* \* \*

We held an exit conference with NJDOL officials on December 13, 2001, in which we presented a summary of our findings. Generally, they reserved comment on the findings pending receipt of our draft audit report. However, we discussed in some detail the methodology we used for both findings included in this report, and, based on additional information provided by them shortly after the meeting, we made a minor adjustment to the data used in reallocating their AS&T costs to all projects.

## **Auditee's Response**

In their response to our draft report, NJDOL officials disagreed with the report's findings and recommendations, concluding that NJDOL had not overrecovered its indirect costs and, therefore, did not owe a refund to DOL. NJDOL stated that while it did not reimburse UI for AS&T costs applicable to NJDOL shared UI tax collection costs, an audit of the entire process for sharing such costs would have revealed that NJDOL overreimbursed the UI program by about \$6.1 million as opposed to the underreimbursement of AS&T costs of \$4.8 million. Regarding the exclusion of several State programs from the base for allocating AS&T costs, NJDOL stated that it direct charged AS&T costs to State programs, and such direct charging does not violate Federal requirements.

We have incorporated NJDOL's detailed comments at the end of each finding, as appropriate. In addition, a copy of NJDOL's written response is included, in its entirety, as an appendix to this report.

## **Auditors's Conclusion**

NJDOL's written response admits that it improperly excluded AS&T costs from its reimbursement of UI tax collection costs. At the same time, NJDOL contends it overreimbursed UI because its reimbursement methodology was flawed. However, our audit showed that the methodology was consistent with its negotiated, written agreement with DOL. In addition, NJDOL's contention that it direct charged AS&T costs to State programs is misleading because the amounts so charged were arbitrarily determined so that they would equal the AS&T amount appropriated by the State for these programs — they were not determined on the basis of relative benefits received as required by Federal cost principles.

NJDOL's comments do not warrant any changes to the report findings. All the recommendations are considered unresolved and will be addressed in ETA's formal audit resolution process.



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## INTRODUCTION

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### BACKGROUND

The New Jersey Department of Labor (NJDOL) is responsible for providing income maintenance to the disabled and the unemployed; training and retraining the State's workforce; and ensuring safety in the workplace. Most of the Department's programs are fully funded with Federal or dedicated (State trusts) funds. At the time of our audit, NJDOL consisted of four operating units — Labor and Planning Analysis, Workforce New Jersey, Labor Standards and Safety Enforcement, and Disability Services — each under the overall supervision of an assistant commissioner. Each assistant commissioner is responsible for the operation of several programs, and reports directly to the Deputy Commissioner.

For the State fiscal year ended June 30, 2000, NJDOL reported expenditures of over \$429.4 million, and employed more than 3,800 people. The operating unit, Workforce New Jersey, administers the U.S. Department of Labor (DOL) grants and was the largest unit within NJDOL. Other Federal agencies that fund programs through NJDOL include the Social Security Administration and the U.S. Departments of Education and Health and Human Services (HHS). A brief discussion of the major divisions within the various NJDOL operating units follows.

**Division of Unemployment Insurance.** This division administers New Jersey's unemployment insurance (UI) program, providing temporary economic security for workers separated from their jobs through no fault of their own. This program is State-administered and federally funded, except for the UI benefits which are provided and collected through unemployment taxes on employers by the State.

**Division of Employment and Training.** This division provides employment and training services to job seekers and employers through the One-Stop Career System. In addition, this division provides the employment and training component for the Welfare-to-Work and Work First New Jersey programs.

**Division of Public Safety and Occupational Safety and Health.** This division protects the public through inspection and enforcement under the Mine Safety, Explosives, Safe Dispensing of Retail Gasoline and High Voltage Proximity Acts. The division also provides free consultation services to private sector employers. The consultations cover Federal Occupational Safety and Health Administration (OSHA) standards and are designed to make work sites safer.

**Division of Disability Determination Services.** This division documents, evaluates, and adjudicates disability claims filed by New Jersey residents under the Social Security disability programs of the Social Security Administration.

**Division of Vocational Rehabilitation Services.** This division enables individuals with disabilities to obtain jobs consistent with their strengths, priorities, needs, and capabilities. The division also assists businesses that employ persons with disabilities through free consultation services which include providing pre-screened, qualified workers for job openings.

**Division of Wage and Hour Compliance.** This division enforces laws and regulations that protect workers from exploitation and employers from unfair competition, including minimum wage levels, overtime, child labor, and other workplace standards, as well as the payment of prevailing wage rates on public works projects.

**Division of Workers' Compensation.** This division provides benefits to workers or their beneficiaries who are injured or who contract an occupational disease on the job. The benefits include medical care, temporary disability payments, and compensation for a resulting permanent disability. The division maintains an administrative adjudication system to resolve disputes between employers and employees regarding benefits.

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NJDOL annually prepares and submits to DOL's Office of Cost Determination (OCD) an indirect cost rate proposal for the various projects/programs operated by NJDOL, including many DOL programs. NJDOL's indirect cost rate proposal contains the NJDOL portion of the New Jersey Statewide Cost Allocation Plan (SWCAP) as the total NJDOL indirect costs. The SWCAP is used to allocate the costs of various State central services to all departments and agencies within the State. The indirect costs are then allocated to the NJDOL projects/programs based on direct personal services costs (salaries and wages) for each project in relation to the total direct personal services costs for all NJDOL projects to arrive at the indirect cost rate. The negotiated/approved indirect cost rate agreements are based on actual costs incurred, and the agreements are subject to audit.

The administrative costs for operating NJDOL (department-level services including accounting, budgeting, internal auditing, planning and research, office services, procurement, and property and equipment management) are distributed through direct charges to projects/programs. These costs are accumulated in an account entitled Administrative Staff and Technical (AS&T) costs, and are periodically billed directly to projects/programs on the basis of each project's direct labor hours (regular, overtime, and leave) in relation to the total departmental direct labor hours for regular, overtime, and leave. Personal benefits costs (fringe benefits) include costs such as pension, health benefits, temporary disability, and unemployment insurance, and are charged to projects on the

basis of the rate(s) negotiated with the HHS. The negotiated rates are applied to the total personal services costs. AS&T non-personal services include costs such as rent, insurance, telephone and other communications, postage, and supplies, and, generally, are allocated similar to personal services costs. While AS&T rates are not established in the negotiated indirect cost rate agreements, the methodology for direct billing of AS&T costs to projects is included in these agreements.

## **OBJECTIVES AND SCOPE**

Our objective was to conduct an audit of direct and indirect costs charged to the Unemployment Insurance (UI) program for Federal fiscal year (FFY) ended September 30, 2000, to determine whether such costs were reasonable, allocable, and otherwise allowable under the Federal cost principles set forth in OMB Circular A-87 — *Cost Principles for State, Local and Indian Tribal Governments*, and the implementing guidelines set forth in ASMB C-10 — *Cost Principles and Procedures for Establishing Cost Allocation Plans and Indirect Cost Rates for Agreements with the Federal Government*. Further, the audit objective provided that, depending on the results of our audit of direct and indirect costs charged to the UI program in FFY 2000, the scope of the audit could be expanded to include additional years and other DOL grant programs.

Our preliminary audit of costs charged to the UI grant program indicated potential significant problems with the allocability of AS&T costs beginning as early as October 1, 1997, and continuing to the end of our fieldwork. Accordingly, the primary focus of our audit was on the allocation of AS&T costs to DOL grants administered by NJDOL for FFYs ended September 30, 1998, 1999, 2000, and 2001.

The objective of our audit was to examine the NJDOL methodology for allocating AS&T costs to projects/programs and recovering such costs. We were not engaged to, and did not, perform an audit of NJDOL's total costs, the objective of which would have been the expression of an opinion on the total costs claimed by NJDOL, and, accordingly, we do not express such an opinion.

This engagement was performed in accordance with auditing standards established by the American Institute of Certified Public Accountants, and with the *Government Auditing Standards* issued by the Comptroller General of the United States, except that the scope of our engagement did not include expressing a formal written opinion on the reasonableness and allowability of the total costs claimed by NJDOL, its system of internal controls, or its compliance with laws and regulations applicable to all Federal grants/contracts.

Our audit fieldwork was performed at NJDOL offices in Trenton, New Jersey, primarily during the period October 9, 2001, through December 14, 2001. An exit conference was held on December 13, 2001, with the NJDOL Director, Division of Accounting, and various other Division of Accounting officials.

## **FEDERAL COST REIMBURSEMENT PRINCIPLES**

DOL grants provide for payment of allowable, reasonable, and allocable incurred costs as determined by OMB Circular A-87. In addition to Circular A-87, the grant award and the "Common Rule" (as implemented by DOL at 29 CFR § 97) governing grants to State and local governments, contain a number of compliance requirements which must be met for costs to be allowable. Among other things, the costs must be in accordance with generally accepted

accounting principles, and the grant accounting records must be supported by adequate source documentation such as canceled checks, paid bills, payroll records, time and attendance records, contract and subcontract award documents, etc.

### **General Principles for Determining Allowable Costs**

Attachment A to OMB Circular A-87 establishes general principles for determining allowable costs, both direct and indirect, incurred by state, local, and Indian tribal governments under grants, cost-reimbursement contracts, and other agreements with Federal agencies. The principles are established for the purpose of determining the reasonableness, allowability, and allocability of costs claimed and are not intended to dictate the extent of Federal or contractor/grantee participation in the financing of a particular program or project. Accordingly, they describe what may be reimbursed or recovered under a Federal award. The principles are designed to ensure that the Federal Government bears its fair share of costs incurred, except where specifically restricted or prohibited by law.

Under OMB Circular A-87, Attachment A, paragraph C, costs charged to Federal programs must meet the tests of allowability, reasonableness, and allocability. To be **allowable**, costs must meet the following general criteria:

- a. Be necessary and reasonable for proper and efficient performance and administration of Federal awards.
- b. Be allocable to Federal awards under the Circular (e.g., on the basis of relative benefits received).
- c. Be authorized (or not prohibited) under state or local laws and regulations.
- d. Conform to any limitations or exclusions set forth in these principles, Federal laws, the terms and conditions of the Federal award, or any other governing regulations as to types and/or amounts of cost items.
- e. Be consistent with policies, regulations, and procedures that apply uniformly to both Federal awards and other activities/programs of the governmental unit.
- f. Be accorded consistent treatment. A cost may not be assigned to a Federal award as a direct cost if any other cost incurred for the same purpose in like circumstances has been allocated to the Federal award as an indirect cost.  
[Note: Similarly, a cost may not be allocated to a Federal award as an indirect cost if any other cost incurred for the same purpose in like circumstances has been charged to the award as a direct cost.]
- g. Except as otherwise provided for in the Circular, costs must be determined in accordance with generally accepted accounting principles.
- h. Not be included as a cost or used to meet cost-sharing or matching requirements of any other Federal award in either the current or a prior period, except as specifically provided by Federal law or regulation.
- i. Be the net of all applicable credits.
- j. Be adequately documented.

A cost may be considered reasonable if, in its nature and amount, it does not exceed that which would be incurred by a prudent person under the circumstances prevailing at the time the decision was made to incur the costs. The question of reasonableness is particularly important when governmental units or components are predominantly federally funded. In determining **reasonableness** of a given cost, consideration will be given to:

- a. Whether the cost is of a type generally recognized as ordinary and necessary for the operation of the governmental unit or the performance of the Federal award.
- b. The restraints or requirements imposed by such factors as sound business practices; arms-length bargaining; Federal, state, and other laws and regulations; and terms and conditions of the Federal award.
- c. Market prices for comparable goods or services.
- d. Whether the individuals concerned acted with prudence in the circumstances considering their responsibilities to the governmental unit, its employees, the public at large, and the Federal Government.
- e. Significant deviations from the established practices of the governmental unit which may unjustifiably increase the Federal award's cost.

The basic guidelines for costs to be **allocable** are briefly summarized, as follows:

- a. A cost is allocable to a particular cost objective if the goods or services involved are chargeable or assignable to such cost objective in accordance with the "relative benefits received."
- b. All activities which benefit from the governmental unit's indirect costs, including unallowable activities and services donated to the governmental unit by third parties, will receive an appropriate allocation of the indirect costs.
- c. Any cost allocable to a particular Federal award or cost objective under the principles provided for in this Circular may not be charged to other Federal awards to overcome fund deficiencies, to avoid restrictions imposed by law or terms of the Federal awards, or for other reasons. However, this prohibition would not preclude governmental units from shifting costs that are allowable under two or more awards in accordance with existing program agreements.
- d. Where an accumulation of indirect costs will ultimately result in charges to a Federal award, a [approved] cost allocation plan [and/or an approved indirect cost rate agreement] will be required as described in Attachments C, D, and E.

OMB Circular A-87 mandates that the HHS issue implementing guidelines for A-87 on behalf of the entire Federal Government. HHS has developed and issued these guidelines in ASMB C10 — *Cost Principles and Procedures for Establishing Cost Allocation Plans and Indirect Cost Rates for Agreements with the Federal Government*. These additional guidelines include discussions of the requirements for preparing and submitting cost allocation plans, public assistance cost allocation plans, and state and local indirect cost rate proposals. In addition, these guidelines address types of indirect cost rates, acceptable methodologies for indirect cost rate

determinations, allocation bases, special rates, the submission and documentation of indirect cost rate proposals, the review, negotiation, and approval of indirect cost rates, etc.

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## FINDINGS

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The NJDOL did not comply with OMB Circular A-87 requirements that indirect costs such as AS&T be allocated to cost objectives on the basis of “relative benefits received.” Our audit disclosed that for the 4-year period ended September 30, 2001, NJDOL had billed and received a total of \$54,214,688 in AS&T costs from DOL. However, NJDOL’s actual allowable AS&T costs properly allocable to DOL grant awards, on the basis of “relative benefits received,” totaled only \$48,048,370 during this period. As a result, NJDOL overcharged DOL grant awards a total of \$6,166,318 in AS&T costs during this 4-year period. The following schedule summarizes the NJDOL’s AS&T costs charged to DOL grants, the allowable AS&T costs based on audit results, and any over/under-recovery of AS&T costs from DOL for the 4-year period covered by our audit.

(Thousands of dollars)

Description	1998	1999	2000	2001	Total
AS&T Costs Charged to DOL Grants	\$11,730	\$13,881	\$14,353	\$14,251	\$54,215
Allowable AS&T Costs on DOL Grants	\$10,319	\$12,326	\$12,747	\$12,657	\$48,049
<b>AS&amp;T Over Charges on DOL Grants</b>	<b>\$1,411</b>	<b>\$1,555</b>	<b>\$1,606</b>	<b>\$1,594</b>	<b>\$6,166</b>

Note: Differences in totals due to rounding of figures to nearest thousand.

Based on our audit, we questioned a total of \$6,166,318 in AS&T costs which were improperly claimed and recovered by NJDOL on DOL/ETA grant awards during FFYs 1998,1999, 2000, and 2001, for the following reasons:

1. 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).



2. The allocation base used by NJDOL to distribute its AS&T costs to its final cost objectives was flawed because its 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.

The net effect of the matters summarized above was a substantial shifting of costs from NJDOL's State programs (to which such costs were properly allocable) to DOL grant awards which resulted in a significant over-recovery of AS&T costs on the DOL/ETA grant awards.

Further, we expect that a similar overrecovery of AS&T costs on DOL/ETA grant awards will also occur in FY 2002 because the conditions discussed above had not changed as of the completion of our fieldwork in December 2001.

The detailed results of our audit are presented in the individual findings on the following pages of this report.

<p><b>FINDING 1. NJDOL Failed to Reimburse UI Grants for AS&amp;T Costs When It Reimbursed Other Costs for the Collection of State Taxes</b></p>
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Our audit disclosed that NJDOL annually reimburses to the UI program millions of dollars of costs for the UI tax collection function because this function also collects three State taxes as well as the UI tax. NJDOL reimbursed the UI program for its share of the UI tax collection function costs including direct personal services, personal benefits, non-personal services, and associated division-level AS&T costs. However, it did not reimburse the UI program for almost \$4.8 million in departmental AS&T costs also allocable to the UI tax collection function for FFYs 1998, 1999, 2000, and 2001.

As required by OMB Circular A-87, DOL and NJDOL had entered into a cost-sharing agreement in which NJDOL would reimburse the UI account for its share of the costs of the UI tax collection function since the UI tax collection function significantly benefits State programs as well as the UI program. The cost-sharing agreement states that departmental administrative staff costs will be included with the UI tax collection function's direct costs for personal services, personal benefits, and non-personal services. Indirect costs, such as departmental AS&T, must be included in cost-sharing agreements to comply with the OMB Circular A-87 requirement that all activities which benefit from the indirect costs will receive an appropriate allocation of the indirect costs. Because NJDOL did not reimburse the UI program for departmental AS&T costs properly allocable to the three State tax programs, NJDOL over-recovered almost \$4.8 million of AS&T costs from the DOL UI program. The amount of departmental AS&T costs not reimbursed are summarized in the following table.

<b>Description</b>	<b>FFY 1998</b>	<b>FFY 1999</b>	<b>FFY 2000</b>	<b>FFY 2001</b>	<b>Total</b>
Personal Services	\$792,807	\$777,788	\$868,873	\$851,524	\$3,290,992
Personal Benefits	\$169,661	\$184,569	\$228,514	\$216,287	\$799,031
Non-Personal Services	\$144,473	\$231,122	\$161,250	\$148,472	\$685,317
<b>Totals</b>	<b>\$1,106,941</b>	<b>\$1,193,479</b>	<b>\$1,258,637</b>	<b>\$1,216,283</b>	<b>\$4,775,340</b>

As required by OMB Circular A-87 and DOL General Administrative Letter 4-91 "Allocation of Costs of Assessing and Collecting State Taxes," the DOL/OCD has had negotiated agreements with NJDOL for many years regarding the sharing of UI tax collection costs. The last agreement, dated March 17, 1992, stated that NJDOL would reimburse the UI program for 44.42 percent of the cost of the UI tax collection function because it was also being used to collect a State disability tax. Subsequently, NJDOL unilaterally increased its share to 55.15 percent because it had added two more State taxes to be collected by the UI tax collection function beginning in FY 1997.

DOL/OCD is currently awaiting statistical data from NJDOL to negotiate a new agreement for the three taxes. The current agreement states that

The actual amount of the State reimbursement will be calculated from the costs reported on the Department of Labor's cost accounting system.

These costs will include:

- Personal Services
- Personal Benefits
- Non-Personal Services
- Departmental Administrative Staff Costs

Our audit of the costs reimbursed by NJDOL to the UI program, in accordance with the agreement, showed that the reimbursements occurred monthly and included the costs for personal services, personal benefits, non-personal services, and an equitable share of the AS&T costs of the UI unit. For example, for the month of September 2000, NJDOL reimbursed the UI program \$966,632. This amount included \$598,697 (or 55.15 percent) of the \$1,085,579 direct personal services costs and an equitable portion of the UI unit's AS&T costs. Personal benefits costs (based on a HHS-approved percentage of personal services costs) totaled \$151,171, and non-personal services costs were \$216,764.

However, the September reimbursement did not include any departmental AS&T costs. We found the same to be true for all of the other months during the 4-year period ended September 30, 2001. NJDOL's failure to include departmental AS&T costs as part of its reimbursement violated the Federal cost principles set forth in OMB Circular A-87 and the negotiated agreement on cost-sharing.

Accordingly, we determined the amount of departmental AS&T which should have been reimbursed to the UI program for the 4-year period. As opposed to NJDOL's monthly calculations to determine the monthly reimbursements, we formulated yearly averages for various parts of NJDOL's monthly calculations. Using these yearly averages, we found that departmental AS&T costs totaling \$4,775,340 should have been reimbursed by NJDOL to the UI program. Because this was not done, the DOL UI grants were over-charged by that amount, and NJDOL over-recovered \$4,775,340 in AS&T costs from the UI grants. Data used in our calculations are listed below. Exhibit A contains all the factors used in our calculations for the four FFYs.

### Departmental AS&T Costs Not Reimbursed

Description	FFY 1998	FFY 1999	FFY 2000	FFY 2001
UI positions related to Tax Function - Direct plus UI AS&T	351	308	296	274
Total UI positions	1,424	1,335	1,232	1,176
Department AS&T PS Costs Applicable to UI	\$5,830,411	\$6,117,395	\$6,559,532	\$6,633,006
Department AS&T PS Applicable to Tax Function	\$1,437,546	\$1,410,314	\$1,575,472	\$1,544,014
<b>AS&amp;T PS Reimbursable By NJDOL (55.15%)</b>	<b>\$792,807</b>	<b>\$777,788</b>	<b>\$868,873</b>	<b>\$851,524</b>
Personal Benefits Rate	21.40%	23.73%	26.30%	25.40%
<b>Personal Benefits = % of PS Reimbursable by NJDOL</b>	<b>\$169,661</b>	<b>\$184,569</b>	<b>\$228,514</b>	<b>\$216,287</b>
AS&T Non-Personal Costs Applicable to UI Unit	\$1,062,474	\$1,817,801	\$1,217,354	\$1,156,536
AS&T Non-Personal Costs Applicable to Tax Function	\$261,963	\$419,078	\$292,384	\$269,215
<b>AS&amp;T Non-Personal Costs Reimbursable by NJDOL</b>	<b>\$144,473</b>	<b>\$231,122</b>	<b>\$161,250</b>	<b>\$148,472</b>
<b>Total Reimbursable and Over Recovery</b>	<b>\$1,106,941</b>	<b>\$1,193,479</b>	<b>\$1,258,637</b>	<b>\$1,216,283</b>
<b>Grand Total of Over Recovery</b>				<b>\$4,775,340</b>

We discussed NJDOL's failure to include departmental AS&T costs in the amounts reimbursed to the UI program with the NJDOL Director of Internal Audit. He stated that his office has reviewed the amounts being reimbursed by State programs to assure that the monthly charges are supportable. However, he stated that his office had not reviewed the reimbursement calculations to determine whether NJDOL was complying with the negotiated agreement and the provisions of OMB Circular A-87.

We also asked the NJDOL Director of Accounting why the departmental AS&T costs were not included in the amounts reimbursed to the UI program by State-funded programs. Initially, he stated the reimbursements were calculated in accordance with the terms of the agreement. Subsequently, an assistant director of accounting stated that it was believed that the inclusion of the UI unit's AS&T was adequate to meet the terms of the agreement. In our opinion, neither answer given was responsive to our question, nor directly addressed the issue.

The failure by NJDOL to comply with the agreement, and the corresponding monthly over-recoveries of departmental AS&T costs from UI grants, continue.

### **Auditee's Response**

In their response to our draft report, NJDOL officials stated, in part, that:

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. . . . Our review of the allocations made has determined that 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 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 form your opinion on this, we have attached a schedule . . . 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. . . .

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.

### **Auditor's Conclusion**

NJDOL readily admits that, as our report states, it did not allocate departmental AS&T costs to the State-funded programs sharing the costs of the UI tax collection function. However, it claims that it overreimbursed the UI program because, in calculating the State's share of the cost of the tax collection function, it allocated UI program AS&T costs proportionately based on UI direct labor dollars rather than just allocating the UI program AS&T costs solely related to the tax collection function. [Note: Departmental AS&T costs relate to administrative, staff and technical costs which generally benefit all programs/projects within the department, whereas UI program AS&T costs pertains to administrative, staff and technical support costs which benefit all direct program functions carried out by the Division of Unemployment Insurance.]

NJDOL apparently has been allocating the UI program AS&T costs on the basis of UI direct labor dollars at least since the negotiation of its last cost sharing agreement with DOL, dated March 17, 1992, and the allocation base used (direct labor dollars) appears to satisfy the requirements of OMB Circular A-87. While the allocation of UI program level AS&T costs to the tax collection function is not explicitly mentioned in the cost sharing agreement, failure to allocate these costs out to all benefitting cost objectives, including the tax collection function, would violate Federal cost principles. NJDOL's comments regarding an alleged inequity in the methodology used during the period covered by our audit, should be addressed to the DOL officials responsible for negotiating such agreements with NJDOL for resolution. As auditors, we do not have authority to set aside all or a portion of any such cost sharing agreement. Further, the scope of our review did not include a review of the equity of this cost sharing agreement.

In summary, NJDOL has acknowledged that it did not allocate departmental AS&T to State programs sharing in the UI program costs of the tax collection function. Therefore, no changes are being made in this finding or its related conclusions and recommendations.

**FINDING 2. Allocation Base Used by NJDOL to Distribute its AS&T Costs was Flawed Because Certain State-Funded Projects were Excluded**

Our review of NJDOL's methodology for allocating AS&T costs directly to projects disclosed that not all projects were included in the allocation base. A comparison of the project list used to allocate AS&T costs to projects and the NJDOL time distribution list disclosed that a number of projects were not included in the allocation base. We found the excluded projects comprised about 4 to 6 percent of the employee positions in the allocation base, and these projects were primarily funded by State general fund revenues. We recreated the NJDOL allocation of AS&T costs to projects for the 4-year period ended September 30, 2001, added the excluded projects, and found that DOL had been overcharged about \$1.4 million during this period. The DOL Indirect Cost Negotiation Agreement and OMB Circular A-87 both require that all projects of the department be included in the allocation base. NJDOL officials were aware the DOL was being overcharged for AS&T costs but they believed that the amount was not discernible.

OMB Circular A-87 states that indirect cost pools, such as AS&T costs, should be distributed to benefited cost objectives on bases that will produce an equitable result in consideration of "relative benefits derived." In addition, as discussed earlier in this report, the Federal cost principles state that "the basic guidelines for costs to be **allocable** require all activities which benefit from the governmental unit's indirect costs, including unallowable activities and services donated to the governmental unit by third parties, will receive an appropriate allocation of the indirect costs."

In addition, there is a negotiated agreement between DOL and NJDOL on indirect costs for each of the 4 years. The negotiated indirect cost agreement provides that certain department-level administrative support services will be allocated to DOL projects through direct charges. These supporting services are mainly those centralized departmental services which include accounting,

budgeting, internal auditing, planning and research, personnel administration, training, procedures and system development, office services, procurement, and property and equipment management. These costs, generally referred to as AS&T costs, were supposed to be billed directly to the grant and/or activity according to a cost allocation plan that included all projects. We found that AS&T costs were being allocated based on actual personal services (salaries, wages and leave) costs which is the same base on which statewide support services costs (referred to as the Statewide Cost Allocation Plan) are allocated to DOL and other projects.

Our review of the methodologies used by NJDOL in allocating statewide support service costs and AS&T expenses disclosed that NJDOL included personal services costs for all Federal and State projects in the base when determining the statewide support services cost rate for allocation purposes. However, NJDOL included only Federal projects and state-funded trust fund projects in the base for allocating AS&T expenses — state general fund projects were not included in the base for allocating AS&T expenses. The exclusion of state general fund projects from the allocation base results in an inequitable distribution of AS&T costs to all Federal projects and State trust fund projects, especially DOL grant awards which are NJDOL's biggest funding source.

Our comparison of the projects recorded in the monthly report on the allocation of AS&T costs, and the projects listed in the monthly time distribution accounting report, disclosed that a number of projects were excluded every month. For example, in October 1997, we found that 20 projects had been excluded with a total of 210.84 positions paid, or 6.2 percent of the total 3,401 positions paid in the allocation process for that month. For FFY 1998, we found that the paid positions for excluded projects each month ranged from 4.5 to 6.3 percent of the total used in the allocation process. For the FFYs 1999, 2000, and 2001 the percentage of paid positions for excluded projects ranged from 4.1 to 5.3 percent.

We compared the amount of AS&T costs allocated to DOL projects by NJDOL with our calculations which contained two differences from the method used by NJDOL. First, our calculations included the previously excluded projects, thereby expanding the base over which the AS&T costs would be allocated. Also, we added the state-appropriated amount for AS&T costs which had been placed in a separate account and not included in total AS&T costs allocated directly to projects. Other than those two changes, our calculations were identical to those used by NJDOL. This comparison showed that DOL had been overcharged \$1,390,978 during the 4-year period ended September 30, 2001. The comparative data presented in summary fashion follows.

<b>Federal Fiscal Year</b>	<b>NJDOL Allocation</b>	<b>Auditor Allocation</b>	<b>Over Charges</b>
1998	\$11,729,908	\$11,425,999	\$303,909
1999	\$13,880,748	\$13,519,257	\$361,491
2000	\$14,353,202	\$14,005,500	\$347,702
2001	\$14,250,830	\$13,872,954	\$377,876
<b>TOTALS</b>	<b>\$54,214,688</b>	<b>\$52,823,710</b>	<b>\$1,390,978</b>

A more detailed comparison of the overcharges to DOL is included in Exhibits B, C, D, and E. We discussed NJDOL’s failure to include all projects in the allocation base for AS&T costs directly charged to projects with the NJDOL Director of Internal Audit. We also informed him that our audit had highlighted two problem areas where NJDOL was overcharging DOL grant awards for AS&T costs. He stated that his office had audited the amounts of AS&T costs allocated to projects to assure their supportability. However, he stated that his office had not reviewed the NJDOL calculations used to allocate AS&T costs to determine whether NJDOL was complying with the negotiated agreement and A-87.

We also discussed this situation with other NJDOL officials who stated this problem had been caused by the failure of the State of New Jersey to allocate sufficient funds to pay for all NJDOL AS&T costs applicable to state general fund projects. They stated early in the audit that they were aware of this situation, but believed that the additional costs to DOL and other Federal agencies would not be discernible.

**Auditee’s Response**

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 federal requirement.

**Auditor’s Conclusion**

We agree that there is no universal rule for classifying certain costs as either direct or indirect under every accounting system. However, NJDOL cannot charge its AS&T costs on one basis to Federal grant awards (i.e., allocated based on direct labor hours), while direct charging an

arbitrary portion of the salary and fringe benefits of certain AS&T employees to a separate account to be charged only to State-funded projects. As previously discussed in this report, OMB Circular A-87, Attachment A, paragraph C.1. states, among other things that, to be allowable, costs must “Be consistent with policies, regulations, and procedures that apply uniformly to both Federal awards and other activities/programs of the governmental unit.” In addition, OMB Circular A-87, Attachment A, paragraph D.2. states, in part, that “. . . it is essential that each item of cost be treated consistently in like circumstances either as a direct or an indirect cost.” Moreover, NJDOL has not provided any substantive evidence showing that its unorthodox deviations from these criteria resulted in its AS&T costs being allocated/charged to all benefiting cost objectives on the basis of “relative benefits received.” To the contrary, our audit disclosed that the employees whose personnel services costs were being charged arbitrarily to State-funded programs were performing duties and responsibilities that benefitted all projects within the department — not just particular State projects. In short, the disparate methods used to charge Federal grants versus State-funded programs violate Federal cost principles and are, therefore, unallowable.

We recalculated the AS&T costs which should have been allocated to the DOL grant awards by adding the indirect costs for the State projects in question to the total NJDOL indirect cost pool, and added the salaries of those State projects to the base on which the pool costs were allocated to projects. This resulted in all NJDOL indirect costs being allocated to all projects regardless of funding source.

In summary, that NJDOL’s written response did not provide any new or compelling evidence which would warrant any change in this finding or its related conclusions and recommendations.

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## **CONCLUSIONS AND RECOMMENDATIONS**

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### **CONCLUSIONS**

We concluded that NJDOL has overcharged DOL grant awards a total of \$6,166,318 in AS&T costs during FFYs 1998, 1999, 2000, and 2001. This occurred because NJDOL did not comply with (1) Federal cost principles mandated by OMB Circular A-87, (2) negotiated agreements with DOL, and (3) the terms and conditions of the various DOL grant awards.

As discussed in the body of this report, our audit disclosed that DOL grants were overcharged for AS&T costs because NJDOL had (1) improperly excluded AS&T costs from its reimbursement to the UI grant for costs related to the DOL/NJDOL sharing of costs of the UI tax function; and (2) excluded certain state-funded projects from the base on which AS&T costs were allocated directly to projects.



In our discussions with NJDOL officials, it appeared to us that they were aware that NJDOL's actions, as spelled out in this report, were contrary to the negotiated agreements.

## **RECOMMENDATIONS**

We recommend that:

1. The cognizant DOL Grant Officer(s) direct NJDOL to refund the \$6,166,318 in unallowable costs questioned in this report.
2. The cognizant DOL Grant Officer(s) direct NJDOL to adjust its billings to DOL for FY 2002 for AS&T costs to preclude further over-recoveries of AS&T costs attributable to the findings in this report.
3. The Assistant Secretary for Employment and Training direct NJDOL to ensure that its proposals on AS&T cost allocation methodology rate proposals fully comply with the reasonableness, allocability, and allowability criteria mandated by OMB Circular A-87.
4. The Assistant Secretary for Employment and Training direct NJDOL to include a provision in its annual audit plans for periodic audit of the implementation of negotiated agreements applicable to the sharing of UI tax collection costs and the allocation of AS&T costs directly to projects.

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**INDEPENDENT ACCOUNTANT'S REPORT ON AUDIT**

Tichenor & Associates, LLP, under contract to the U.S. Department of Labor (DOL), Office of Inspector General (OIG), conducted an audit of direct and indirect costs charged to DOL grant awards by the State of New Jersey's Department of Labor (NJDOL) for Federal fiscal years (FFYs) 1998, 1999, 2000, and 2001, to determine whether such costs were reasonable, allowable, and allocable under the Federal cost principles set forth in OMB Circular A-87.

Our preliminary audit of direct costs and the DOL negotiated NJDOL indirect costs charged to the UI program indicated significant problems with the allowability and allocability of claimed AS&T costs (departmental indirect costs) beginning as early as October 1, 1997, and continuing on to the present time. Accordingly, we focused the balance of our audit on the NJDOL claims for and recovery of AS&T costs applicable to DOL grants for FFYs ended September 30, 1998, 1999, 2000, and 2001.

We were not engaged to, and did not perform, an audit of NJDOL's total costs charged to DOL grant awards, the objective of which would have been the expression of an opinion on the total costs claimed by NJDOL, and, accordingly, we do not express such an opinion.

Based on the results of our audit, we questioned a total of \$6,166,318 in AS&T costs charged to DOL grant awards during FFYs ended September 30, 1998, 1999, 2000, and 2001 because NJDOL procedures were not in compliance with the Federal costs principles mandated by OMB Circular A-87, and negotiated agreements between DOL and NJDOL.

More specifically, we found that:

- (1) NJDOL had failed to reimburse UI grant awards for AS&T expenses, as required by the negotiated agreements between DOL and NJDOL, when it reimbursed other costs for the collection of State taxes; and
- (2) The personal services allocation base used by NJDOL to distribute AS&T expenses was flawed because certain state-funded projects were excluded.

This limited-scope audit was performed in accordance with applicable standards established by the American Institute of Certified Public Accountants, and the *Government Auditing Standards* issued by the Comptroller General of the United States. Our engagement did not include expressing a written opinion on the reasonableness and allowability of NJDOL's total claimed costs, the adequacy of its overall system of internal controls, or its compliance with laws and regulations applicable to Federal grant awards. Our detailed findings, conclusions, and recommendations are contained in the accompanying report.

This report is intended solely for the use of the U.S. Department of Labor; however, the final report is a matter of public record and its distribution is not limited.

TICHENOR & ASSOCIATES, LLP  
Louisville, Kentucky  
December 14, 2001

## **EXHIBITS**

**New Jersey Department of Labor  
Summary of Departmental AS&T Costs Applicable to UI Tax Function  
that Should Have Been Reimbursed by NJDOL to UI Grants**

<b>Designation Formula</b>	<b>Description</b>	<b>FFY 1998</b>	<b>FFY 1999</b>	<b>FFY 2000</b>	<b>FFY 2001</b>
<b>A</b>	<b>Total UI Tax Positions Acct(306-325) - Annual Average</b>	<b>282.81</b>	<b>250.96</b>	<b>244.90</b>	<b>225.84</b>
<b>B</b>	<b>UI AS&amp;T Positions Acct (400-440) - Annual Average</b>	<b>276.72</b>	<b>246.34</b>	<b>211.85</b>	<b>205.35</b>
<b>C</b>	<b>Total UI PS Positions- Annual Average</b>	<b>1423.75</b>	<b>1334.90</b>	<b>1231.50</b>	<b>1175.54</b>
<b>D=C-B</b>	<b>Net UI Positions - UI PS less AS&amp;T Positions - Annual Average</b>	<b>1147.03</b>	<b>1088.56</b>	<b>1019.65</b>	<b>970.19</b>
<b>E=A/D</b>	<b>Percent of UI Tax Positions to Net UI Positions</b>	<b>24.66%</b>	<b>23.05%</b>	<b>24.02%</b>	<b>23.28%</b>
<b>F=ExB</b>	<b>UI AS&amp;T Positions Applicable to Tax Function</b>	<b>68.23</b>	<b>56.79</b>	<b>50.88</b>	<b>47.80</b>
<b>G=A+F</b>	<b>Total Positions Applicable to Tax Function</b>	<b>351.04</b>	<b>307.75</b>	<b>295.78</b>	<b>273.64</b>
<b>H=G/C</b>	<b>Ratio of Tax Positions to Total UI Positions</b>	<b>24.66%</b>	<b>23.05%</b>	<b>24.02%</b>	<b>23.28%</b>
<b>I</b>	<b>NJDOL AS&amp;T PS Cost Applicable to UI</b>	<b>\$5,830,411</b>	<b>\$6,117,395</b>	<b>\$6,559,532</b>	<b>\$6,633,006</b>
<b>J=HxI</b>	<b>NJDOL AS&amp;T PS Cost Applicable to Tax Function</b>	<b>\$1,437,546</b>	<b>\$1,410,314</b>	<b>\$1,575,472</b>	<b>\$1,544,014</b>
<b>K</b>	<b>Percent of UI Tax Function Cost to Be Reimbursed by State</b>	<b>55.15%</b>	<b>55.15%</b>	<b>55.15%</b>	<b>55.15%</b>
<b>L=JxK</b>	<b>UI NJDOL AS&amp;T PS Cost Not Reimbursed by State</b>	<b>\$792,806</b>	<b>\$777,788</b>	<b>\$868,873</b>	<b>\$851,523</b>
<b>M</b>	<b>NJDOL Average Personal Benefit Rate</b>	<b>21.40%</b>	<b>23.73%</b>	<b>26.30%</b>	<b>25.40%</b>
<b>N=LxK</b>	<b>UI NJDOL AS&amp;T PB Cost Not Reimbursed by State</b>	<b>\$169,660</b>	<b>\$184,569</b>	<b>\$228,513</b>	<b>\$216,287</b>
<b>O</b>	<b>UI NJDOL AS&amp;T NPS Cost</b>	<b>\$1,062,474</b>	<b>\$1,817,801</b>	<b>\$1,217,354</b>	<b>\$1,156,536</b>
<b>P=OxH</b>	<b>UI NJDOL NPS Cost Applicable to Tax Function</b>	<b>\$261,963</b>	<b>\$419,078</b>	<b>\$292,384</b>	<b>\$269,215</b>
<b>Q=PxK</b>	<b>UI NJDOL AS&amp;T NPS Cost Not Reimbursed By State</b>	<b>\$144,473</b>	<b>\$231,122</b>	<b>\$161,250</b>	<b>\$148,472</b>
<b>R=L+N+Q</b>	<b>TOTAL UI NJDOL AS&amp;T COSTS NOT REIMBURSED</b>	<b>\$1,106,939</b>	<b>\$1,193,479</b>	<b>\$1,258,636</b>	<b>\$1,216,282</b>

Note: Differences in the calculations are due to rounding.

**RECAP OF AS&T COSTS NOT REIMBURSED**

<b>1998</b>	<b>\$1,106,939</b>
<b>1999</b>	<b>\$1,193,479</b>
<b>2000</b>	<b>\$1,258,636</b>
<b>2001</b>	<b>\$1,216,282</b>
<b>Total</b>	<b>\$4,775,335</b>

**EXHIBIT B****NEW JERSEY DEPARTMENT OF LABOR****Comparison of NJDOL and Auditor Allocation  
of AS&T Costs to DOL Grants for FFY 1998****AS&T Personal Services Costs**

<b>Month/ Year</b>	<b>NJDOL Allocation</b>	<b>Auditor Allocation</b>	<b>Over Charges</b>
<b>Oct. '97</b>	<b>\$724,857</b>	<b>\$718,525</b>	<b>\$6,332</b>
<b>Nov. '97</b>	<b>\$618,459</b>	<b>\$615,332</b>	<b>\$3,127</b>
<b>Dec. '97</b>	<b>\$751,368</b>	<b>\$734,070</b>	<b>\$17,298</b>
<b>Jan. '98</b>	<b>\$722,610</b>	<b>\$701,532</b>	<b>\$21,078</b>
<b>Feb. '98</b>	<b>\$651,890</b>	<b>\$633,917</b>	<b>\$17,973</b>
<b>Mar. '98</b>	<b>\$712,415</b>	<b>\$692,419</b>	<b>\$19,996</b>
<b>Apr. '98</b>	<b>\$702,245</b>	<b>\$685,204</b>	<b>\$17,041</b>
<b>May '98</b>	<b>\$671,253</b>	<b>\$651,160</b>	<b>\$20,093</b>
<b>Jun. '98</b>	<b>\$700,708</b>	<b>\$679,317</b>	<b>\$21,391</b>
<b>Jul. '98</b>	<b>\$738,606</b>	<b>\$716,622</b>	<b>\$21,984</b>
<b>Aug. '98</b>	<b>\$683,414</b>	<b>\$674,721</b>	<b>\$8,693</b>
<b>Sep. '98</b>	<b>\$728,691</b>	<b>\$715,499</b>	<b>\$13,192</b>
<b>Sub-Totals</b>	<b>\$8,406,516</b>	<b>\$8,218,318</b>	<b>\$188,198</b>

**AS&T Personal Benefit Costs - 21.4%**

<b>Sub-Totals</b>	<b>\$1,798,994</b>	<b>\$1,758,720</b>	<b>\$40,274</b>
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**AS&T Non-Personal Services Costs**

<b>Dec. 97</b>	<b>\$106,480</b>	<b>\$101,008</b>	<b>\$5,472</b>
<b>Mar. '98</b>	<b>\$437,319</b>	<b>\$413,286</b>	<b>\$24,033</b>
<b>Jun. '98</b>	<b>\$437,841</b>	<b>\$414,668</b>	<b>\$23,173</b>
<b>Sep. '98</b>	<b>\$542,758</b>	<b>\$519,999</b>	<b>\$22,759</b>
<b>Sub-Totals</b>	<b>\$1,524,398</b>	<b>\$1,448,961</b>	<b>\$75,437</b>

<b>TOTALS</b>	<b>\$11,729,908</b>	<b>\$11,425,999</b>	<b>\$303,909</b>
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**Note: AS&T Non-Personal Services Costs are allocated quarterly.**

**EXHIBIT C**

**NEW JERSEY DEPARTMENT OF LABOR**

**Comparison of NJDOL and Auditor Allocation  
of AS&T Costs to DOL Grants for FFY 1999**

**AS&T Personal Services Costs**

<b>Month/ Year</b>	<b>NJDOL Allocation</b>	<b>Auditor Allocation</b>	<b>Over Charges</b>
<b>Oct. '98</b>	<b>\$742,348</b>	<b>\$724,829</b>	<b>\$17,519</b>
<b>Nov. '98</b>	<b>\$717,519</b>	<b>\$700,791</b>	<b>\$16,728</b>
<b>Dec. '98</b>	<b>\$791,823</b>	<b>\$772,011</b>	<b>\$19,812</b>
<b>Jan. '99</b>	<b>\$734,341</b>	<b>\$717,131</b>	<b>\$17,210</b>
<b>Feb. '99</b>	<b>\$696,379</b>	<b>\$682,083</b>	<b>\$14,296</b>
<b>Mar. '99</b>	<b>\$824,483</b>	<b>\$804,017</b>	<b>\$20,466</b>
<b>Apr. '99</b>	<b>\$744,674</b>	<b>\$727,093</b>	<b>\$17,581</b>
<b>May '99</b>	<b>\$728,407</b>	<b>\$708,560</b>	<b>\$19,847</b>
<b>Jun. '99</b>	<b>\$765,055</b>	<b>\$747,547</b>	<b>\$17,508</b>
<b>Jul. '99</b>	<b>\$767,501</b>	<b>\$751,246</b>	<b>\$16,255</b>
<b>Aug. '99</b>	<b>\$770,048</b>	<b>\$753,106</b>	<b>\$16,942</b>
<b>Sep. '99</b>	<b>\$789,984</b>	<b>\$771,623</b>	<b>\$18,361</b>
<b>Sub-Totals</b>	<b>\$9,072,562</b>	<b>\$8,860,037</b>	<b>\$212,525</b>

**AS&T Personal Benefit Costs - 23.73%**

<b>Sub-Totals</b>	<b>\$2,152,919</b>	<b>\$2,102,487</b>	<b>\$50,432</b>
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**AS&T Non-Personal Services Costs**

<b>Dec. 98</b>	<b>\$127,081</b>	<b>\$122,208</b>	<b>\$4,873</b>
<b>Mar. '99</b>	<b>\$665,770</b>	<b>\$642,221</b>	<b>\$23,549</b>
<b>Jun. '99</b>	<b>\$768,387</b>	<b>\$739,255</b>	<b>\$29,132</b>
<b>Sep. '99</b>	<b>\$1,094,029</b>	<b>\$1,053,049</b>	<b>\$40,980</b>
<b>Sub-Totals</b>	<b>\$2,655,267</b>	<b>\$2,556,733</b>	<b>\$98,534</b>

<b>TOTALS</b>	<b>\$13,880,748</b>	<b>\$13,519,257</b>	<b>\$361,491</b>
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**Note: AS&T Non-Personal Services Costs are allocated quarterly.**

**EXHIBIT D****NEW JERSEY DEPARTMENT OF LABOR****Comparison of NJDOL and Auditor Allocation  
of AS&T Costs to DOL Grants for FFY 2000****AS&T Personal Services Costs**

<b>Month/ Year</b>	<b>NJDOL Allocation</b>	<b>Auditor Allocation</b>	<b>Over Charges</b>
<b>Oct. '99</b>	<b>\$769,330</b>	<b>\$760,333</b>	<b>\$8,997</b>
<b>Nov. '99</b>	<b>\$805,771</b>	<b>\$796,045</b>	<b>\$9,726</b>
<b>Dec. '99</b>	<b>\$856,115</b>	<b>\$826,876</b>	<b>\$29,239</b>
<b>Jan. '00</b>	<b>\$804,146</b>	<b>\$789,384</b>	<b>\$14,762</b>
<b>Feb. '00</b>	<b>\$806,768</b>	<b>\$784,962</b>	<b>\$21,806</b>
<b>Mar. '00</b>	<b>\$886,918</b>	<b>\$864,263</b>	<b>\$22,655</b>
<b>Apr. '00</b>	<b>\$762,644</b>	<b>\$745,900</b>	<b>\$16,744</b>
<b>May '00</b>	<b>\$858,295</b>	<b>\$834,773</b>	<b>\$23,522</b>
<b>Jun. '00</b>	<b>\$825,828</b>	<b>\$814,075</b>	<b>\$11,753</b>
<b>Jul. '00</b>	<b>\$814,611</b>	<b>\$796,758</b>	<b>\$17,853</b>
<b>Aug. '00</b>	<b>\$894,490</b>	<b>\$875,016</b>	<b>\$19,474</b>
<b>Sep. '00</b>	<b>\$831,092</b>	<b>\$813,794</b>	<b>\$17,298</b>
<b>Sub-Totals</b>	<b>\$9,916,008</b>	<b>\$9,702,179</b>	<b>\$213,829</b>

**AS&T Personal Benefit Costs - 26.30%**

<b>Sub-Totals</b>	<b>\$2,607,910</b>	<b>\$2,551,673</b>	<b>\$56,237</b>
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**AS&T Non-Personal Services Costs**

<b>Dec. 99</b>	<b>\$164,069</b>	<b>\$156,953</b>	<b>\$7,116</b>
<b>Mar. '00</b>	<b>\$559,934</b>	<b>\$538,342</b>	<b>\$21,592</b>
<b>Jun. '00</b>	<b>\$473,742</b>	<b>\$454,125</b>	<b>\$19,617</b>
<b>Sep. '00</b>	<b>\$631,539</b>	<b>\$602,228</b>	<b>\$29,311</b>
<b>Sub-Totals</b>	<b>\$1,829,284</b>	<b>\$1,751,648</b>	<b>\$77,636</b>

<b>TOTALS</b>	<b>\$14,353,202</b>	<b>\$14,005,500</b>	<b>\$347,702</b>
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**Note: AS&T Non-Personal Services Costs are allocated quarterly.**



**EXHIBIT E****NEW JERSEY DEPARTMENT OF LABOR****Comparison of NJDOL and Auditor Allocation  
of AS&T Costs to DOL Grants for FFY 2001****AS&T Personal Services Costs**

<b>Month/ Year</b>	<b>NJDOL Allocation</b>	<b>Auditor Allocation</b>	<b>Over Charges</b>
<b>Oct. '00</b>	<b>\$868,486</b>	<b>\$841,381</b>	<b>\$27,105</b>
<b>Nov. '00</b>	<b>\$887,794</b>	<b>\$865,951</b>	<b>\$21,843</b>
<b>Dec. '00</b>	<b>\$835,422</b>	<b>\$822,715</b>	<b>\$12,707</b>
<b>Jan. '01</b>	<b>\$883,793</b>	<b>\$858,864</b>	<b>\$24,929</b>
<b>Feb. '01</b>	<b>\$758,668</b>	<b>\$737,721</b>	<b>\$20,947</b>
<b>Mar. '01</b>	<b>\$844,829</b>	<b>\$823,414</b>	<b>\$21,415</b>
<b>Apr. '01</b>	<b>\$777,729</b>	<b>\$756,846</b>	<b>\$20,883</b>
<b>May '01</b>	<b>\$861,794</b>	<b>\$838,230</b>	<b>\$23,564</b>
<b>Jun. '01</b>	<b>\$766,631</b>	<b>\$745,743</b>	<b>\$20,888</b>
<b>Jul. '01</b>	<b>\$835,824</b>	<b>\$820,395</b>	<b>\$15,429</b>
<b>Aug. '01</b>	<b>\$899,468</b>	<b>\$878,068</b>	<b>\$21,400</b>
<b>Sep. '01</b>	<b>\$770,029</b>	<b>\$756,536</b>	<b>\$13,493</b>
<b>Sub-Totals</b>	<b>\$9,990,467</b>	<b>\$9,745,864</b>	<b>\$244,603</b>

**AS&T Personal Benefit Costs - 25.4%**

<b>Sub-Totals</b>	<b>\$2,537,579</b>	<b>\$2,475,449</b>	<b>\$62,130</b>
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**AS&T Non-Personal Services Costs**

<b>Dec. '00</b>	<b>\$303,067</b>	<b>\$289,881</b>	<b>\$13,186</b>
<b>Mar. '01</b>	<b>\$607,839</b>	<b>\$582,952</b>	<b>\$24,887</b>
<b>Jun. '01</b>	<b>\$489,593</b>	<b>\$468,449</b>	<b>\$21,144</b>
<b>Sep. '01</b>	<b>\$322,285</b>	<b>\$310,359</b>	<b>\$11,926</b>
<b>Sub-Totals</b>	<b>\$1,722,784</b>	<b>\$1,651,641</b>	<b>\$71,143</b>

<b>TOTALS</b>	<b>\$14,250,830</b>	<b>\$13,872,954</b>	<b>\$377,876</b>
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**Note: AS&T Non-Personal Services Costs are allocated quarterly.**

**AUDITEE'S RESPONSE**



## 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

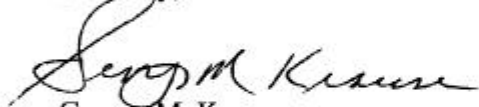
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AD-18.62 (1-02)

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**

	<b>FY 1998</b>	<b>FY 1999</b>	<b>FY 2000</b>	<b>FY 2001</b>	<b>Total</b>
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	
<b>TOTAL VARIANCE PS/PB/NPS</b>	<b>1,827,873</b>	<b>1,537,092</b>	<b>1,317,001</b>	<b>1,387,701</b>	<b>6,069,667</b>
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
<b>NET VARIANCE</b>	<b>720,934</b>	<b>343,613</b>	<b>58,365</b>	<b>171,419</b>	<b>1,294,331</b>

<b>TOTAL</b>	
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

<b>COST CENTER</b>	<b>DIVISION/OFFICE</b>	<b>FY 1998</b>	<b>FY 1999</b>	<b>FY2000</b>	<b>FY 2001</b>
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
03A00600	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
<b>03C01410</b>	<b>Employer Accounts</b>	<b>1,510,254.57</b>	<b>1,443,968.30</b>	<b>1,532,640.14</b>	<b>1,474,481.34</b>
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 <sup>1</sup>	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
<b>TOTAL COSTS ALLOCATED</b>	<b>966,631.92<sup>1</sup></b>	<b>628,310.75</b>	<b>309,322.21</b>	<b>28,998.96</b>

<sup>1</sup> Amount per audit report - page 11

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

<b>COST CENTER</b>	<b>DIVISION/OFFICE</b>	<b>AMOUNT</b>
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
<b>03C01410</b>	<b>Employer Accounts</b>	<b>116,817.26</b>
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
		<b>830,457.57</b>
		<b>830,457.57</b>
Total 210 Charges Sept. 2000		3,868,038.81
Less UI Overhead		830,457.57
Net UI		<b>3,037,581.24</b>
Tax Functions/Net UI (852,511/3,037,581)		28.07%
Overhead Applicable to State Programs:		
830,457 * 28.07%		<b>233,068</b>
		<b>233,068</b>

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 :

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