



STATE OF NORTH CAROLINA

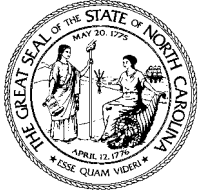
AUDIT RESULTS FROM
CAFR AND SINGLE AUDIT PROCEDURES
EMPLOYMENT SECURITY COMMISSION

FOR THE YEAR ENDED JUNE 30, 2003

OFFICE OF THE STATE AUDITOR

RALPH CAMPBELL, JR.

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April 29, 2004

The Honorable Michael F. Easley, Governor
Members of the North Carolina General Assembly
Mr. Harry E. Payne, Jr., Chairman
Employment Security Commission

We have completed certain audit procedures at the Employment Security Commission related to the State's *Comprehensive Annual Financial Report (CAFR)* and the State's *Single Audit Report*, for the year ended June 30, 2003. Our audit was performed by authority of Article 5A of Chapter 147 of the *North Carolina General Statutes*.

The results of these procedures, as described below, yielded audit findings and recommendations for the Commission related to the State's financial statements and the State's federal financial assistance programs that required disclosure in the aforementioned reports. The findings noted above are included in the findings and recommendations section contained herein. Our recommendations for improvement and management's response follow each finding.

We noted internal control weaknesses over information systems general controls, bank reconciliations, and fixed assets. We also noted that the required suspension and debarment certifications were not obtained from contractors. Further, required eligibility documentation was not available for thirty cases in the Unemployment Insurance program, and documentation was not maintained to support the calculation of the Trade Readjustment Allowances payments in four cases.

The accounts and operations of the Employment Security Commission are an integral part of the State's reporting entity represented in the *CAFR* and the *Single Audit Report*. In the *CAFR*, the State Auditor expresses an opinion on the State's financial statements. In the *Single Audit Report*, the State Auditor also presents the results of tests on the State's internal control and on the State's compliance with laws, regulations, contracts, and grants applicable to the State's financial statements and to its federal financial assistance programs. The audit procedures were conducted in accordance with auditing standards generally accepted in the United States of America, *Government Auditing Standards* issued by the Comptroller General of the United States, and Office of Management and Budget Circular A-133.

As part of the work necessary for issuance of the *CAFR* and the *Single Audit Report*, the following individual funds and federal programs of the State were subjected to audit procedures at the Employment Security Commission as we considered necessary:

Funds for the *Comprehensive Annual Financial Report*:

Enterprise Fund: Unemployment Compensation Fund

Special Revenue Fund: Employment Security Commission Fund

Federal Programs for the *Single Audit Report*:

Unemployment Insurance

Employment Services Cluster

Trade Adjustment Assistance – Workers

Workforce Investment Act Cluster

The individual funds and federal programs subjected to audit at the Employment Security Commission are substantially less in scope than would be necessary to report on the financial statements that relate solely to the Commission or the administration of federal programs by the Commission. Therefore, we do not express such conclusions.

North Carolina General Statutes require the State Auditor to make audit reports available to the public. Copies of audit reports issued by the Office of the State Auditor may be obtained through one of the options listed in the back of this report.



Ralph Campbell, Jr.
State Auditor

AUDIT FINDINGS AND RECOMMENDATIONS

Matters Related to Financial Reporting or Federal Compliance Objectives

The following findings and recommendations were identified during the current audit and describe conditions that represent significant deficiencies in internal control or noncompliance with laws, regulations, contracts, or grants. Finding numbers 1 and 5 were also reported in the prior year.

1. SIGNIFICANT WEAKNESSES OVER INFORMATION SYSTEMS GENERAL CONTROLS

The Employment Security Commission did not always follow its procedures to ensure that proper access rights were given to new hire employees and that access rights were deleted timely for separated employees. Improper access to computer systems can result in alteration, unauthorized use, or loss of information. Our tests revealed the following conditions.

- Two of the forty-five new employees tested had inappropriate access for their positions.
- Six of forty-five separated employees' access rights to the computer system were not revoked immediately upon separation or determination that they would not return to work within ninety days as prescribed by the Commission's *Internal Security Handbook*.
- Seventeen employees' access identifications had not been deleted after more than six months of non-use as required by Commission policy.

In addition, the *Internal Security Handbook*, Chapter 5, issued to all employees is outdated and needs revision. The electronic form and transmission method for access to and revocation from the information systems described in this chapter are no longer required.

Recommendation: The Commission should evaluate and strengthen its security procedures to ensure access is limited to employees on a need-to-use basis. Access rights for terminated employees should be revoked immediately and periodic reviews should be conducted to ensure that access is restricted to authorized users and that user ID's that have not been used within six months are deleted. Also, the *Internal Security Handbook*, Chapter 5 should be updated to reflect current procedures.

Agency Response: The responsibility for system access is shared by the supervisor of the unit in which the employee works, Human Resources, and the Information Systems Help Desk. In addition, the instructions have been amended without republication of a complete procedure. Successful control of system access depends on each party acting in a timely manner. The high volume of claims resulted in an increase of temporary staff to support extended benefit programs; staff turnover resulted in increased numbers of access authorization requests and internal turnover may have delayed timely review of separated employee user IDs in some cases. In some cases, management asked us to give access to individuals for added support. In these cases they asked us to leave the access in place longer than the six months time frame.

AUDIT FINDINGS AND RECOMMENDATIONS (CONTINUED)

In late 2003, the Commission began efforts to update and formalize its Information Systems Security Policies, Standards and Procedures. An Information Security Program charter and the policy and standard describing the structure of the program have been developed and approved by executive management. As part of this effort, the instructions relating to security which reside in various bulletins, manuals, handbooks, forms and associated instructions, work unit procedures, web pages and ISO9000 management system have been identified.

The content is being reviewed, updated and circulated for comment prior to publication. Those sections relating to granting and revoking system access will be incorporated in the Intranet based Integrated Management System which is accessible by all employees and will facilitate keeping the information and instructions current.

The revised and accessible procedures should help to alleviate these issues. Having these procedures will facilitate our ability to maintain and update them for currency and for staff and managers to reference them.

2. BANK RECONCILIATIONS NOT PERFORMED TIMELY OR WITH UNRESOLVED ITEMS

The bank reconciliations for the Claims and Benefits Account were not completed timely. The monthly reconciliations for the audit period were not made available to us prior to the completion of the financial statement audit fieldwork. The North Carolina Administrative Code requires each entity to reconcile its disbursing account within fifteen days of receipt of the statement from the State Treasurer.

Our testing of the Administrative Disbursing Account disclosed an unreconciled amount that ranged from \$29,735 to \$30,772 during the entire audit period. Further, there was no evidence of supervisory review for eight months. In addition, there were no formal policies addressing prompt resolution of outstanding reconciling items. These conditions increase the risk of unrecorded transactions and transactions recorded in error.

Recommendation: The Commission should strengthen internal controls to ensure that bank reconciliations are completed timely, all reconciliations are performed, and appropriate review and approval is documented.

Agency Response: Claims and Benefit Account: When the State Treasurer converted this account to the positive paycheck clearing process, ESC did not identify a necessary change to our bank reconciliation program. The result was erroneous month end figures that could not be reconciled. Because we did not know the automated program was producing erroneous figures, a great deal of time was spent analyzing irreconcilable figures. We eventually went to a daily bank reconciliation process, which identified the problem at the end of a month. A new process is now in place and operating correctly.

Administrative Disbursing Account: This account encountered an initial small discrepancy and then a series of very small discrepancies for a long period of time afterward. Because of the more serious problem in the claims and benefit account, this received limited attention until that issue was resolved. However, the account was analyzed each month and the Supervisor of Accounting and Reporting was appraised of the situation each month. There is now a team working to resolve the problem.

AUDIT FINDINGS AND RECOMMENDATIONS (CONTINUED)

The Commission will insure all bank reconciliations are performed timely and continue to strengthen our internal controls.

3. CONTROLS OVER EQUIPMENT MANAGEMENT NEED IMPROVEMENT

The Commission did not have controls in place to ensure that fixed asset records were properly maintained for equipment purchased with federal funds. The procedures on the Integrated Management System and the *Placement and Use of Property Tags Handbook* were not updated to reflect current procedures, and there were no written procedures for the annual inventory process. Inadequate controls increase the risk that items could be stolen and not detected.

In addition, lack of segregation of duties exists. The employee who participated in major parts of the physical inventory is also the fixed assets custodian at the Central Office.

Our test of thirty-nine items disclosed the following conditions.

- Two assets we inspected were not recorded to the Magic Service Desk System (Magic) masterfile. The Magic System is used to record and track fixed assets.
- Descriptions in the Magic System for two assets were inaccurate.
- One asset location per the Magic System was different from the physical location of the asset.
- One asset funding source and appropriation information was not recorded in the Magic System.

Our test of thirty-nine items that had been disposed disclosed the following.

- Seventeen assets had been deleted from the Magic System masterfile but the appropriate equipment disposition form had not been completed.
- Four assets on the Magic System were reflected in a cost center other than the appropriate disposal cost center.

Federal regulation 29 CFR 97.32 requires equipment records to include the description, location and disposition data of the equipment. Also it requires the State to use, manage, and dispose of equipment in accordance with its laws and procedures.

Recommendation: The Commission should strengthen internal controls over the fixed asset process to ensure that fixed assets are properly recorded. All policies and procedures should be updated to reflect current procedures.

Agency Response: Procedures on the Integrated Management System and “Placement and Use of Property Tags” were not updated to reflect current procedures since procedures evolved due to the recent use of scan guns and an issue concerning PC hard drives. The revised procedures and handbook should be completed no later than May 1. New procedures include documenting the inventory process and preclude the participation of the Fixed Asset Officer in the actual physical inventory.

AUDIT FINDINGS AND RECOMMENDATIONS (CONTINUED)

The specific responses to the audit findings are:

- The assets that weren't recorded in the Magic database were just simply not put in the system when they were originally tagged. These barcode numbers will be obtained and the information will be entered into Magic.
- Descriptions for assets are taken directly from the purchase order. The procedures mentioned above should address the validation of the descriptions during the annual inventory.
- Cost centers managers should also validate location during the annual inventory and make location corrections via the Asset Manager program. The revised procedures will reflect this process. In addition, reports can be produced to determine if no location is listed.
- Funding source information is typically pulled from the Purchase Order. The primary reason an asset wouldn't have the funding information included is because it may have been tagged during an inventory and not when it was originally purchased. Therefore, the Purchase Order number may not have been available. Reports can be produced to determine if no funding source is listed.
- The seventeen assets that the report says were deleted from the system were actually surplus and were transferred to the disposal cost center. The BM-51's were not signed by our staff when the equipment was picked up. No item had been deleted.
- The four assets that were reflected in a cost center other than the appropriate cost center were once listed on a BM-51 to be surplus, but were re-used in other cost centers.

4. REQUIRED DEBARMENT CERTIFICATIONS WERE NOT OBTAINED

The Commission did not obtain the required suspension and debarment certification from its contractors/vendors that received awards greater than \$100,000 in the Unemployment Insurance Grant. There were nine contracts or commodity purchases that did not have the required certifications. Failure to secure certifications increases the risk that the Commission may contract with contractors/vendors who have been denied participation by the federal government.

Federal regulation 29 CFR 98.510 requires a certification regarding debarment and suspension to be filed for covered transactions.

Recommendation: The Commission should implement procedures to ensure compliance with the governmentwide debarment and suspension requirement.

Agency Response: We have since obtained letters from vendors to fulfill the requirement as far back as July 2003. In the future the grant holders will review the grant documentation and inform Purchasing and other offices of any additional requirements noted.

AUDIT FINDINGS AND RECOMMENDATIONS (CONTINUED)

5. INSUFFICIENT DOCUMENTATION TO DETERMINE CLAIMANT ELIGIBILITY

Our test of the files for ninety claimants receiving Unemployment Insurance (UI) benefits revealed thirty that did not contain the required documentation or contained incomplete forms. Six of the thirty cases contained multiple deficiencies. These errors were primarily due to the local Employment Security Commission (ESC) offices' failure to produce the required eligibility documentation. Also, the Central Office did not maintain all electronic records for benefit claims for attached workers. The results of our testwork are as follows:

- Seventeen of the claimants lacked the required Form 506E (*Work Search Record*). This form is a record kept by the claimants of their job searches. The claimant is required to turn in the Work Search Record when he/she reports to the local office for the continuation of UI benefits. Because likely questioned costs exceed \$10,000, we are questioning the known costs of \$3,345.
- Thirteen of the claimants lacked a properly signed form NCUI 500 (*New Initial Intrastate Claim for Benefits*). This form is used to document initial claimant eligibility. Of these, two local ESC offices were unable to locate two claimants' files. Because likely questioned costs exceed \$10,000, we are questioning the known costs of \$1,469.
- Six of the claimants lacked the required Form NCUI 501 (*Benefit Claim for Attached Worker*). This form certifies that the worker is still attached to the employers' payroll during the week and that he/she worked less than 60% of normal work hours. Because likely questioned costs exceed \$10,000, we are questioning the known costs of \$1,477.

The Employment Security Law 96-13(a)(1) and Employment Security Commission Regulation 10.12(A) require claimants to register for work and report to the employment office, as directed, at regular intervals. The claimants' status must be reviewed at each reporting for continuing eligibility. Additionally, the signatures of both the claimant and the claimstaker are required by Section 3.5 of the Commission's *Local Office Claims Manual* to certify that the claimant has met the registration for work requirements and that the local ESC representative has explained the eligibility requirements.

Recommendation: The Commission should ensure that the local offices are placing adequate emphasis on signing, maintaining and documenting the work registration and the continuation of Unemployment Insurance benefits. All forms should be properly completed and maintained in accordance with the *Local Office Claims Manual*, Employment Security Law, and ESC regulations. The Commission should also ensure that documentation in electronic form be retained for audit.

Agency Response: The Employment Security Commission will take steps to ensure that all local offices maintain appropriate documentation of work registration and the continuation of Unemployment Insurance benefits, including appropriate signatures. Local offices will be reminded that all forms must be completed and maintained in accordance with the *Local Office Claims Manual*, Employment Security Law, and ESC regulations.

AUDIT FINDINGS AND RECOMMENDATIONS (CONCLUDED)

6. DOCUMENTATION NOT MAINTAINED FOR CALCULATION OF BENEFITS FOR TAA

The Commission did not maintain the necessary documentation to support the Trade Readjustment Allowances (TRA) payments in four of the forty-seven claimants tested. The initial Unemployment Insurance (UI) benefits data for these four claimants had been purged from the electronic database. Since the UI payment is used to compute the TRA payment, we were unable to determine that the payment was calculated correctly. Because likely questioned costs exceed \$10,000, we are questioning the known costs of \$1,093.

Twenty CFR section 617.13 states the amount of TRA payable for a week of total unemployment shall be an amount equal to the most recent weekly benefit amount of UI payable to the individual for a week of total unemployment preceding the individual's first exhaustion of UI following the individual's first qualifying separation.

Recommendation: The Commission should ensure that adequate documentation is maintained to document the Trade Readjustment Allowances payments.

Agency Response: The Employment Security Commission will ensure that adequate documentation is maintained to document all payments of Trade Readjustment Allowance benefits.

DISTRIBUTION OF AUDIT REPORT

In accordance with General Statutes 147-64.5 and 147-64.6(c)(14), copies of this report have been distributed to the public officials listed below. Additional copies are provided to other legislators, state officials, the press, and the general public upon request.

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May 11, 2004

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