



STATE OF NORTH CAROLINA

NORTH CAROLINA GENERAL ASSEMBLY FISCAL CONTROL AUDIT

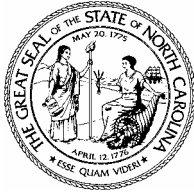
OFFICE OF THE STATE AUDITOR

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STATE AUDITOR

NORTH CAROLINA GENERAL ASSEMBLY
FISCAL CONTROL AUDIT

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AUDITOR'S TRANSMITTAL

The Honorable Michael F. Easley, Governor
The General Assembly of North Carolina
Mr. George R. Hall, Jr., Legislative Services Officer

This report presents the results of our fiscal control audit of the North Carolina General Assembly. Our work was performed by authority of Article 5A of Chapter 147 of the *North Carolina General Statutes* and was conducted in accordance with the standards contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. The objective of a fiscal control audit is to gather and evaluate evidence about internal control over selected fiscal matters, such as financial accounting and reporting; compliance with finance-related laws, regulations, and provisions of contracts or grant agreements; and/or management of financial resources.

The results of our audit disclosed deficiencies in internal control and/or instances of noncompliance or other matters that are considered reportable under *Government Auditing Standards*. These items are described in the Audit Findings and Recommendations section of this report.

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.

Leslie W. Merritt, Jr.

Leslie W. Merritt, Jr., CPA, CFP
State Auditor

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BACKGROUND INFORMATION

The General Assembly is responsible for making the laws, or statutes, of North Carolina. The North Carolina General Assembly (NCGA) is made of two bodies or houses; the Senate and the House of Representatives, which consist of 50 and 120 legislative members, respectively.

The managing authority for the General Assembly is the Legislative Services Commission, which consist of seven members from each house. The Commission, through the Legislative Services Office oversees the operations of the General Assembly. The NCGA consists of five divisions under the Legislative Services Office: the Administrative Division, the Bill Drafting Division, the Fiscal Research Division; the Research Division; and the Information System Division.

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OBJECTIVES, SCOPE, METHODOLOGY, AND RESULTS

OBJECTIVES

As authorized by Article 5A of Chapter 147 of the *North Carolina General Statutes* and in accordance with the standards contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, we have conducted a fiscal control audit at the North Carolina General Assembly.

The objective of a fiscal control audit is to gather and evaluate evidence about internal control over selected fiscal matters, such as financial accounting and reporting; compliance with finance-related laws, regulations, and provisions of contracts or grant agreements; and/or management of financial resources. Our audit does not provide a basis for issuing an opinion on internal control, and consequently, we have not issued such an opinion.

Management is responsible for establishing and maintaining effective internal control. Internal control is a process designed to provide reasonable assurance that relevant objectives are achieved. Because of inherent limitations in internal control, errors or fraud may nevertheless occur and not be detected. Also, projections of any evaluation of internal control to future periods are subject to the risk that conditions may change or compliance with policies and procedures may deteriorate.

SCOPE

Our audit scope covered the period July 1, 2005, through February 28, 2006, and included selected internal controls for the Administrative Division. This Division is responsible for the financial services for the North Carolina General Assembly which includes:

- Police services
- Food services duties
- Consultant services
- Supplies and equipment purchases
- Facility maintenance
- Receptionists and guides for the facilities
- Printing of information
- Distribution of printed bills

The food services include the snack bar in the Legislative Office Building as well as a snack bar and cafeteria in the State Legislative Building. Our testwork focused on the following accounts:

Food and Vending Revenue – This account consists of the funds collected from food sales in the General Assembly's cafeteria and two snack bars. The General Assembly reported

OBJECTIVES, SCOPE, METHODOLOGY, AND RESULTS (CONTINUED)

approximately \$513,000 in revenues collected during the audit period. We examined internal controls designed to ensure that the revenues were properly accounted for and reported in the financial records.

Payroll Expenditures – We reviewed expenditures for temporary wages, overtime pay and shift premium. The General Assembly employs temporary personnel to assist and serve during its legislative sessions to perform necessary duties. Overtime pay compensates those employees who work beyond the normal forty-hour work week. Shift premium is paid when employees, mainly police officers, work before or after traditional business hours. The General Assembly reported these types of payroll expenditures to be approximately \$4.2 million during the audit period. In addition, we reviewed the processes for granting and documenting pay increases for all levels of staffing. The General Assembly is not subject to the State Personnel Manual; however, guidance is provided by its own personnel manual. The President Pro Tempore of the Senate and the Speaker of the House have the authority to establish personnel policies for staff of their respective house. We examined internal controls designed to ensure that payroll expenditures were made in compliance with the General Assembly’s personnel policies and properly recorded.

Supplies and Materials Expenditures – We examined expenditures for janitorial, general office, and food supplies. Janitorial expense accounts for supplies used by facility maintenance in cleaning the Legislative Office Building and Legislative Building. The general office supplies represent expenditures for normal office supplies (such as copy paper, pens, pencils, toner, etc) to be used by all employees and legislators. The food supplies category includes items such as plates, cups, napkins, utensils, serving trays, etc. used in serving food in the cafeteria and snack bars. During the period under audit, the General Assembly reported purchases of supplies and materials of approximately \$191,000. We examined internal controls designed to ensure that the General Assembly’s supplies and materials inventory system complies with State inventory policies and that these expenditures were properly accounted for and recorded.

Purchase for Resale – This expenditure is for the purchase of food and drink items to be sold in the cafeteria, two snack bars, and vending machines. The General Assembly reported purchases for resale of approximately \$355,000. We examined internal controls designed to ensure that the General Assembly’s purchase for resale inventory system complies with State inventory policies and that these expenditures were properly accounted for and recorded.

METHODOLOGY

To accomplish our audit objectives, we gained an understanding of internal control, performed tests of control effectiveness, and/or performed direct tests of the accounts and transactions as we considered necessary in the circumstances. Specifically, we performed procedures such as interviewing personnel, observing operations, reviewing policies, analyzing accounting records and examining documentation supporting recorded transactions and balances.

OBJECTIVES, SCOPE, METHODOLOGY, AND RESULTS (CONCLUDED)

RESULTS

The results of our audit disclosed deficiencies in internal control and/or instances of noncompliance or other matters that are considered reportable under *Government Auditing Standards*. These items are described in the Audit Findings and Recommendations section of this report. We noted certain other matters that we reported to management of the General Assembly in a separate letter dated August 14, 2006.

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AUDIT FINDINGS AND RECOMMENDATIONS

1. INVENTORY CONTROL WEAKNESSES

Our tests disclosed weaknesses in the purchasing, tracking, and recording of office, janitorial and food inventories as well as the related expenditures. Our tests identified the following errors:

Office and Janitorial Supplies:

- Of 49 test items, five invoices were paid without all required final approvals to pay. Seven invoices tested were classified incorrectly. One item was missing an approved purchase order. Additional scanning of accounting records identified 23 items as potential misclassifications based on transaction descriptions.
- Access to office supply rooms is not adequately limited. There are 23 keys issued to various agency personnel.
- Financial Services could not produce inventory count sheets for the quarter ending December 2005.
- A database is maintained to account for inventory levels; however, the database was not accurately updated to reflect actual amounts per the June 2005 year-end physical inventory counts. Our comparison of the database amounts and the inventory count sheet amounts identified 41 variances.
- A physical count was performed for a sample of items identified on the March 2006 inventory listings. Errors were noted for all 27 sample items tested.

Food Services:

- Purchase orders are not created and approved prior to orders being submitted directly online, by fax or by phone.
- Of 49 test items, eight invoices were classified incorrectly. In addition, two items were paid without the proper authorizations to pay.
- Financial Services could not produce inventory count sheets for the month ending December 2005.
- The database used to record the inventory was not accurately updated to reflect actual amounts per the June 2005 year-end physical inventory counts. Our comparison of the database amounts and the inventory count sheets identified 39 errors noted due to inconsistent data.
- The Food Services section does not use a perpetual inventory system, which prevents it from properly tracking usage and identifying theft in a timely manner.

AUDIT FINDINGS AND RECOMMENDATIONS (CONTINUED)

The weaknesses in internal controls could result in the misstatement of the inventories and/or related expenditures on the financial statements. Additionally, the failure to safeguard and track inventories increases the risk of misuse or theft of assets.

Best practices provide that all transactions be properly documented. The Office of State Controller's policies require agencies to safeguard assets and have internal policies regarding the maintaining and accounting of financial statement transactions.

Recommendation: The Agency should establish policies and procedures to ensure inventory transactions are properly approved, documented and recorded. Additionally, controls should be implemented to ensure inventories are properly safeguarded and tracked. The Agency should investigate the implementation of a perpetual inventory system.

Agency's Response: We agree with the findings. Action has been taken to address the areas of weakness. Operational procedures are being reviewed to assure that inventory policies and procedures are in place and followed. Additionally, control measures are being adjusted to assure greater inventory security. We are also investigating the implementation of a perpetual inventory system to replace the current system.

2. INADEQUATE SUPPORT FOR SENATE AND HOUSE STAFF SALARY INCREASES

Our review identified instances where North Carolina Senate and House of Representative staff members were awarded salary increases in excess of 10% within a one-year period without documented justification. The *North Carolina General Assembly Personnel Manual* states that no employee shall be granted more than a 10% increase in a calendar year. However, the manual has a qualifier that states that the President Pro Tempore of the Senate and the Speaker of the House have the authority to establish personnel policies for staff in their respective house. We found no additional written policies for either the Senate or the House that would establish the procedures necessary for providing and documenting salary adjustments.

Our testwork identified instances where staff member salaries were increased with limited or no documentation as to the rationale for the increase. In some cases, a personnel form requesting the increase would be submitted. In others, the documentation consisted of only a memo requesting that the salary increase be implemented. Justification for the increases might consist of a notation stating that "additional duties" had been given to the staff member; however, there was no description of what those additional duties might be beyond those provided by the rules of their respective House. In other cases, there was no explanation provided for the salary increases.

North Carolina General Statute 120-37 provides guidance for the provision of salaries and additional staff for members of the General Assembly. While the legislation allows Senate and House leadership latitude to establish their own personnel policies, they should be written and clearly communicated. Policies establish uniformity, help reduce

AUDIT FINDINGS AND RECOMMENDATIONS (CONTINUED)

the perception of inequities, and ensures that employee relations are handled in a fair and consistent manner.

Recommendation: The Legislative leadership should establish written compensation practices and pay schedules for its staff or consider following the practices already identified in the *North Carolina General Assembly Personnel Manual*. If separate compensation policies are established, they should address the documentation requirements necessary to justify the awarding of those salary adjustments.

Agency's Response: The Speaker of the House and President Pro Tempore of the Senate are authorized by statute to approve expenditures for their respective chamber. The increases in question were properly approved. Your findings and recommendations will be forwarded to the Speaker and President Pro Tempore.

3. RECONCILIATION OF PAYROLL SYSTEM AND NCAS NOT PERFORMED

The Agency has its own payroll system which does not interface with the North Carolina Accounting System (NCAS). The Agency does not reconcile the payroll system to NCAS on a periodic basis. As part of our testwork, we performed a reconciliation of these two systems and identified several variances that were brought to the attention to staff. The failure to perform periodic reconciliations may allow payroll transactions to be omitted, incorrectly recorded, and/or allow for non-payroll transactions to be misclassified in the accounting system.

When accounting data is entered and processed by multiple accounting systems, it is important to ensure that the information is also consistently reported. Reconciliation procedures performed for the various accounting systems provides evidence for the agreement of the underlying accounting data and should be performed on a regular basis.

Recommendation: We recommend that the Agency implement procedures to ensure that the internal payroll system is periodically reconciled to the NCAS accounting system.

Agency's Response: We agree with the finding. Journal entries generated from the payroll system are being flagged to facilitate the reconciliation between the payroll system and the NCAS accounting system. The reconciliation between the payroll system and NCAS will be done monthly.

4. FAILURE TO COMPLY WITH THE DAILY DEPOSIT ACT

We noted instances where the funds from the Legislative Office Building Snack Bar were not deposited on a timely basis in accordance with *North Carolina General Statute 147-77*, Daily Deposit of Funds to Credit of Treasurer. The Cafeteria Manager is responsible for making the daily deposit; however, the Manager does not have a backup in the event that other duties or absence prevents him from making the deposit.

AUDIT FINDINGS AND RECOMMENDATIONS (CONCLUDED)

The failure to make daily deposits causes the Agency to be noncompliant with State regulations. Additionally, there is an increased risk of theft or misplacement of funds because undeposited funds remain in the cash register, rather than being placed in a safe, until the deposit is made.

Recommendation: The Agency should implement procedures to ensure compliance with the Daily Deposit Act. This should include the designation of backup personnel to perform necessary functions due to the unavailability of the Cafeteria Manager.

Agency's Response: We agree with the finding. A backup has been designated to make the Legislative Office Building snack bar deposit when the Food Services Manager is not available.

ORDERING INFORMATION

Audit reports issued by the Office of the State Auditor can be obtained from the web site at www.ncauditor.net. Also, parties may register on the web site to receive automatic email notification whenever reports of interest are issued. Otherwise, copies of audit reports may be obtained by contacting the:

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