



STATE OF NORTH CAROLINA

DEPARTMENT OF ENVIRONMENT AND NATURAL RESOURCES

STATEWIDE FINANCIAL AUDIT PROCEDURES

FOR THE YEAR ENDED JUNE 30, 2006

OFFICE OF THE STATE AUDITOR

LESLIE W. MERRITT, JR., CPA, CFP

STATE AUDITOR



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Office of the State Auditor

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March 7, 2007

The Honorable Michael F. Easley, Governor
Members of the North Carolina General Assembly
Mr. William Ross, Secretary
Department of Environment and Natural Resources

We have completed certain audit procedures at the Department of Environment and Natural Resources related to the State of North Carolina reporting entity as presented in the *Comprehensive Annual Financial Report (CAFR)* and *Single Audit Report* for the year ended June 30, 2006. Our audit was performed by authority of Article 5A of Chapter 147 of the *North Carolina General Statutes*.

In the *CAFR*, the State Auditor expresses an opinion on the State's financial statements. In the *Single Audit Report*, the State Auditor presents the results of tests of internal control and compliance with laws, regulations, contracts and grants applicable to the State's financial statements and to its federal financial assistance programs. Our 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 the Single Audit Act as applicable. Our audit scope at the Department of Environment and Natural Resources included the following:

State of North Carolina's Financial Statements

EPA Clean Water Revolving Loan Fund

EPA Drinking Water Revolving Loan Fund

State of North Carolina's Administration of Federal Financial Assistance Programs

Capitalization Grants for Clean Water State Revolving Funds

Capitalization Grants for Drinking Water State Revolving Funds

Our audit procedures at the Department of Environment and Natural Resources were less in scope than would be necessary to report on the financial statements that relate solely to the Department or its administration of federal programs. Therefore, we do not express such conclusions.

The results of our audit procedures yielded an audit finding and recommendation for the Department related to the State's federal financial assistance programs that may require disclosure in the aforementioned reports. The finding is included in the audit findings and recommendations section contained herein. Our recommendations for improvement and management's response follow the finding.

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.

A handwritten signature in black ink that reads "Leslie W. Merritt, Jr." with a stylized flourish at the end.

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

DRAFT AUDIT FINDING AND RECOMMENDATION

Matters Related to Financial Reporting or Federal Compliance Objectives

The following finding and recommendation was identified during the current audit and discusses a condition that represents a deficiency in internal control and/or noncompliance with laws, regulations, contracts or grants.

CONTROLS NOT IN PLACE TO ENSURE COMPLIANCE WITH FEDERAL SUSPENSION AND DEBARMENT REQUIREMENTS

The Department did not have controls in place to ensure that covered transactions (contracts and procurements in excess of \$25,000) were made only to vendors that were eligible to participate in federal programs. The failure to comply with these requirements increases the risk that the Department may contract with suspended or debarred providers.

During our audit year, there was one contract funded by the Drinking Water State Revolving Fund (DWSRF) that exceeded \$25,000. The Clean Water State Revolving Fund also had one contract that exceeded \$25,000. The Department had not verified the federal debarment status for these vendors. The grant award and grant period impacted for the DWSRF program is FS-98433899 (August 2000 – September 2006) and for the CWSRF program is CS-37000105 (July 2005 – December 2008). Testing by the auditor determined that none of the vendors involved were currently debarred and there were no questioned costs.

Title 40 CFR section 32.300 subpart C requires verification for procurement transactions, expected to equal or exceed \$25,000, which are considered “covered transactions.” This ensures that the recipients of federal funds are not suspended or debarred. The grant agreements for both the DWSRF and the CWSRF contain a clause requiring the Department to comply with this regulation. The Department may verify suspension and debarment by checking the Excluded Parties List System, collecting a certification from the entity, or adding a clause or condition to the covered transaction with that entity.

Recommendation: The Department should establish and implement procedures to ensure compliance with federal suspension and debarment regulations.

Agency’s Response: The Department agrees with the finding and has initiated corrective action.

The language of the federal regulations (Title 40 CFR, Section 32.300) is confusing. The Department’s interpretation was that the procurement transactions were not included. We were only including grants and other non-procurement transactions in our federal suspension and debarments requirements. We are now including the requirement on all contracts involving federal funding

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