



STATE OF NORTH CAROLINA

DEPARTMENT OF CORRECTION

FISCAL CONTROL AUDIT

OFFICE OF THE STATE AUDITOR

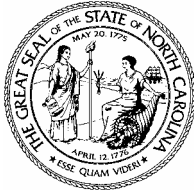
LESLIE W. MERRITT, JR., CPA, CFP

STATE AUDITOR

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THEODIS BECK, SECRETARY



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AUDITOR'S TRANSMITTAL

The Honorable Michael F. Easley, Governor
The General Assembly of North Carolina
Mr. Theodis Beck, Secretary
Department of Correction

This report presents the results of our fiscal control audit of the Department of Correction. 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
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BACKGROUND INFORMATION

The Department of Correction is one of the largest agencies in state government. With over 19,000 employees, the Department is responsible for the custody, supervision and care of individuals sentenced after the conviction of a felony or serious misdemeanor. The Secretary of the Department, Mr. Theodis Beck, oversees the Department's operations and an annual budget of approximately \$1 billion. The major divisions of the Department include the Division of Prisons, the Division of Community Corrections, and Correction Enterprises.

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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 Department of Correction.

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 January 31, 2006 and included selected internal controls in the following organizational units:

Division of Administration – Controller’s Office

This organizational unit is responsible for the general accounting functions of the Department. The unit accounts for and issues financial reports covering all Department operations.

Division of Prisons

This Division houses, clothes, and feeds approximately 37,000 inmates incarcerated in 78 prisons located throughout the State.

Division of Community Corrections

The Division of Community Corrections supervises offenders released into the community, either probationers whose active sentences have been suspended, or parolees and post release offenders who have served a prison sentence and are being reintegrated into the community. The Division supervises approximately 113,000 probationers and more than 2,800 parolees and post-release offenders.

OBJECTIVES, SCOPE, METHODOLOGY, AND RESULTS (CONTINUED)

Correction Enterprises

Correction Enterprises operates the State's prison industries. More than 2,200 inmates work in jobs ranging from manufacturing to farming. The Division's plants manufacture license plates, highway signs, paint and janitorial products. Inmates work in printing, duplicating, sewing, and woodworking jobs. There are also farms, laundries, a cannery, a meat processing plant, and an optical plant.

During our audit we considered internal control related to the following accounts and control objectives and also followed up on all prior year audit findings:

Contract Employees – These expenditures are for the payment of contract employees hired by the Department. We examined internal control designed to ensure that the Department properly paid these employees based on the terms of their employment contracts.

Inmate Labor – These expenditures are for the payment of wages to inmates. We examined internal control designed to ensure that hours worked were properly documented and approved.

Purchased Services – These expenditures are for the purchase of services from vendors outside of state government. We audited six different accounts dealing with the purchase of medical services for inmates. We also audited the miscellaneous contractual expenditures account. We examined internal control designed to ensure the Department properly accounts for and reports these expenditures.

Cellular Phone Service- These expenditures are for the payment of cellular phone services. We examined the internal controls designed to ensure the Department properly accounts for the usage of these phones.

Small Purchases of Direct Raw Materials – Direct raw materials are expenditures incurred primarily by the Division of Correction Enterprises for the purchase of raw materials to be used in the production of products for sale to customers. We audited the small purchases of these raw materials for compliance with both State and Departmental small purchasing policies.

OBJECTIVES, SCOPE, METHODOLOGY, AND RESULTS (CONCLUDED)

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.

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.

AUDIT FINDINGS AND RECOMMENDATIONS

DISBURSEMENT PROCESS CONTAINS WEAKNESSES

The Department made payments that were not paid timely, were not cancelled to prevent duplicate payments, or were stamped with the wrong date of payment. There is an increased risk of duplicate payment when documentation is not marked or defaced when paid. Also, late payment of invoices prevents the Department from taking cash discounts.

We tested several types of expenditures made by the Department. The results of our tests of disbursements made by the accounts payable section were as follows:

- a. A test of 75 disbursements classified as “miscellaneous” by the Department uncovered the following exceptions.
 - 1) Nine items were not paid timely or in accordance with the purchase terms. These payments ranged from being one day to over 20 months late.
 - 2) Five items were not cancelled with a paid stamp to prevent duplicate payments.
 - 3) One item was paid from a copy of the invoice without having the additional documentation of approval as required by the Department’s policy. The Department does allow for payment of invoices from copies if the invoice is stamped “ok to pay” and approved by a supervisor.
- b. A test of 40 expenditures from the largest medical expenditures uncovered that 11 invoices were not date stamped when received by the Department’s Controller’s Office. Four of these invoices were paid from four months to over nine months after the service date. Since the invoices were not stamped when received, we could not determine if the invoices were paid timely after receipt.

Also, the following exceptions were noted in a sample of 60 disbursements made by the Division of Correction Enterprises.

- a. Six items were cancelled (stamped paid) several days after the actual paid date. This causes information in the accounting records to differ from the information stamped on the actual invoices.
- b. Eight items were not paid timely or in accordance with the purchase agreements, consequently two cash discounts were forfeited. The payment dates ranged from being four to 19 days late.
- c. Two items were not cancelled with a paid stamp to prevent duplicate payments.

AUDIT FINDINGS AND RECOMMENDATIONS (CONCLUDED)

Recommendation: The Department should adhere to prescribed policies and procedures for the processing of cash disbursements. Invoices should be cancelled or defaced to prevent duplicate payments. Payments should be made in a timely manner and the date stamped on the invoice should be the actual date that the invoice was paid. In addition, the date received should be stamped on the invoice.

Agency's Response: We concur with your audit finding and recommendation and we will remind our central accounting staff of our requirements related to the processing of cash disbursements. Central accounting will review submission of invoices for compliance with policy and will notify division management when policies are not being followed.

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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