



# STATE OF NORTH CAROLINA

**DEPARTMENT OF STATE TREASURER**

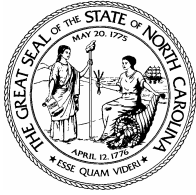
**STATEWIDE FINANCIAL AUDIT PROCEDURES**

**FOR THE YEAR ENDED JUNE 30, 2007**

**OFFICE OF THE STATE AUDITOR**

**LESLIE W. MERRITT, JR., CPA, CFP**

**STATE AUDITOR**



STATE OF NORTH CAROLINA  
Office of the State Auditor

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February 1, 2008

The Honorable Michael F. Easley, Governor  
Members of the North Carolina General Assembly  
The Honorable Richard H. Moore, State Treasurer  
Department of State Treasurer

We have completed certain audit procedures at the Department of State Treasurer 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, 2007. 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 State Treasurer included the following:

State of North Carolina's Financial Statements

- State Treasurer's Investment Funds
- Teachers and State Employees' Retirement System
- Retiree Health Benefit Plan
- General Long-term Debt Accounts and Transactions

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

- Subrecipient Monitoring - Local Government and Public Authority Audit Reports

Our audit procedures at the Department of State Treasurer 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 for the Department related to the State's financial statements that may require disclosure in the aforementioned reports. The finding is included in the Audit Finding and Response section of this report.

The Department of State Treasurer's response to the finding identified in our audit is included in the Audit Finding and Response section of this report. We did not audit the response, and accordingly, we express no opinion on it.

*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

## **AUDIT FINDING AND RESPONSE**

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### **Matters Related to Financial Reporting Objectives**

The following finding was identified during the current audit and discussed conditions that represent significant deficiencies in internal control and/or noncompliance with laws, regulations, contracts or grants.

#### DEFICIENCIES IN FINANCIAL STATEMENT DISCLOSURES

The Department of the State Treasurer's financial statement disclosures submitted to the Office of the State Controller contained certain technical deficiencies. The Office of the State Controller uses the financial statement packages prepared by the agencies to complete the State's *Comprehensive Annual Financial Report*, which is relied on by creditors and others to evaluate the State's financial condition and operations.

Deficiencies noted include:

- The principal amounts in the disclosure of interest rate ranges by investment type were actually carrying amounts/fair market values which resulted in an overstatement of the principal amounts.
- The disclosure of the Escheat Investment Account contained several misstatements. International equities were incorrectly classified as domestic, resulting in a misclassification of \$15 million. Also, the Department did not make the necessary disclosures related to foreign currency risk or how investments were valued. Furthermore, a custodial credit risk disclosure was made when the risk did not exist.
- The interest for General Obligation Bonds Payable was understated by \$141 million due to an incomplete spreadsheet used to calculate the amount.
- The Department reported the Highway Refunding, Series 2004 bonds as noncapital debt rather than capital debt, resulting in a misclassification of \$97 million.
- The disclosure of prior year bond defeasances included a current year refunding, resulting in an overstatement of \$80 million.

We proposed audit adjustments for the missclassifications noted, all of which were made by the Department.

*Recommendation:* The Department should implement effective internal controls over the year-end financial reporting process to ensure the completeness and accuracy of its financial statement disclosures.

*Agency's Response:* We consider the technical deficiencies identified to not be material in relation to our financial statements nor would these items impact creditors or others' evaluation of the State's financial condition and operations. For example, the misclassification you noted in the Escheat Investment Fund amounts to just two percent of the total fund. The General Obligation bonds payable item is less than two percent of outstanding debt and the finding related to the Highway Bonds refunding is just over one percent.

Having a strong system of internal control is a top priority and we will continue our efforts to strengthen our existing internal controls as they relate to the CAFR reporting schedules especially in relation to account classification, completeness and accuracy. We strive for total accuracy in all aspects of our agency's functions.

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