



# STATE OF NORTH CAROLINA

**EMPLOYMENT SECURITY COMMISSION**

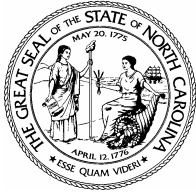
**STATEWIDE FINANCIAL AUDIT PROCEDURES**

**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

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

2 S. Salisbury Street  
20601 Mail Service Center  
Raleigh, NC 27699-0601  
Telephone: (919) 807-7500  
Fax: (919) 807-7647  
Internet  
<http://www.ncauditor.net>

March 24, 2008

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 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 Employment Security Commission included the following:

State of North Carolina's Financial Statements

Enterprise Fund: Unemployment Compensation Fund

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

Unemployment Insurance  
Employment Service Cluster  
Trade Adjustment Assistance  
Workforce Investment Act Cluster

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

The results of our audit procedures yielded audit findings for the Commission related to the State's financial statements and federal financial assistance programs that may require disclosure in the aforementioned reports. These findings are included in the Audit Findings and Responses section of this report.

The Employment Security Commission's responses to the findings identified in our audit are included in the Audit Findings and Responses section of this report. We did not audit the responses, and accordingly, we express no opinion on them.

*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." in a cursive script.

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

## **AUDIT FINDINGS AND RESPONSES**

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### **Matters Related to Financial Reporting or Federal Compliance Objectives**

The following findings were identified during the current audit and discuss conditions that represent significant deficiencies in internal control and/or noncompliance with laws, regulations, contracts or grants. Finding number 4 was also reported in the prior year.

#### **1. DEFICIENCIES IN FINANCIAL REPORTING**

The Employment Security Commission financial statements contained some misstatements that could be misleading to readers. During the audit, we identified the following misstatements:

- The Commission misclassified \$23 million of non-current contribution receivables, as current contributions receivable. The misclassified amount represents benefits paid during fiscal year 2007 that will not be billed until November 2008 and not collected until January 2009.
- Employer tax contributions were included in both the contributions receivable and accounts receivable year-end amounts. This caused receivables to be overstated by \$4.9 million.
- The tax rate for one employer was improperly changed while the employer tax account was in adjudication status. This caused receivables to be overstated by \$3.5 million.

Management at the Employment Security Commission is responsible for the fair presentation of its financial statements in accordance with generally accepted accounting principles.

*Recommendation:* The Commission should implement effective procedures to ensure the completeness and accuracy of the financial statements.

*Agency's Response:* The Commission will continue to improve, implement, and monitor the procedures associated with the classification of Accounts Receivables.

#### **2. CONTROLS OVER JOURNAL ENTRIES NEED IMPROVEMENT**

Controls were not in place to ensure that journal entries posted to the accounting records were appropriate or reasonable. This condition increases the risk of errors in the financial statements.

A number of journal entries were posted that transferred cash totaling \$15.1 million from the Unemployment Insurance State Reserve Fund to the Unemployment Insurance

## **AUDIT FINDINGS AND RESPONSES (CONTINUED)**

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Clearing Fund. The journal entries were made based on e-mails from the Tax Accounting section with no supporting documentation attached. The journal entries were not reviewed by anyone other than the preparer for appropriateness or reasonableness. Our review of the supporting documentation revealed that the journal entries should have transferred cash from the Unemployment Insurance Clearing Fund to the Unemployment Insurance State Reserve Fund, resulting in a \$30.2 million error.

Management is responsible for establishing internal controls which ensure that all journal entries are prepared correctly.

*Recommendation:* The Commission should establish policies and procedures that ensure that journal entries are correct and properly supported by adequate documentation. The journal entries should be reviewed and approved by someone knowledgeable for appropriateness and reasonableness, prior to posting to the general ledger.

The Commission should determine the total amounts transferred in error from the Unemployment Insurance State Reserve Fund and reimburse the appropriate amount back to the fund. In addition, the Commission should review the process of distributing collections to the Reserve Fund and determine if future journal entries are necessary.

*Agency's Response:* The journal entries in question were supported by the Daily Bank Deposit Report received from the Tax Department. Although the amounts to transfer were accurately reflected on the report, the correct sign was not used in preparing the journal entry.

The Commission has strengthened our internal controls and added additional approval steps when handling carryover adjustments. Adjusting entries correcting the carryover error will be handled in February, 2008

### 3. BENEFIT OVERPAYMENT NOT RECOUPED

During our tests of 117 Unemployment Insurance benefit payments we found that one recipient received excessive benefits. The claimant was paid \$164 for one week after she reported to work. Since the recipient was employed during this week, she was not eligible to receive these benefits. The claimant reported she had returned to work; however, no action was initiated to recover the overpayment. Because likely questioned costs exceed \$10,000 in the population, we are questioning the \$164 overpayment.

*Recommendation:* The Commission should recoup the overpayment from the claimant. The Commission should stress the importance of following established procedures regarding recouping overpayments.

*Agency's Response:* The Audit cited a claim in which one recipient received excessive benefits for one week after she reported to work and she was not eligible to receive these benefits. On May 31, 2007, the claimant had reported to the Commission that she had

## **AUDIT FINDINGS AND RESPONSES (CONTINUED)**

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returned to work on May 22, 2007. After the time of the audit, the Commission had not initiated any action to recover the overpayment because the current operating procedures were not followed. The possibility of an overpayment was presented by the auditor and the Commission initiated action on October 8, 2007, and determined the claimant to be overpaid. On October 12, 2007 an overpayment was established and on October 22, 2007 the claimant agreed and entered in payment agreement. The UI Management staff trains and retrains employees on continual bases to ensure all employees follow established guidelines and procedures for when a person reports they have returned to work.

#### 4. CONTROLS OVER EQUIPMENT MANAGEMENT NEED IMPROVEMENT

Documentation supporting the annual inventory taken in December 2006 was incomplete. We sampled 20 cost centers and noted the following issues:

- Six cost centers did not have printed inventory reports.
- One cost center had no written follow-up regarding its missing asset and assets error reports.

There was no tracking system in place to ensure that each cost center's inventory had been conducted. The fixed asset coordinator was on extended leave during our testing and the Commission had not designated backup personnel to this position, making it difficult to determine if the inventories had not been performed or if the documentation had been misfiled.

Additionally, during our inspection of 24 equipment items on the June 2007 active equipment listing, we identified the following exceptions:

- Fourteen equipment items were not located. Further review revealed that these equipment items were noted as 'missing' per the December 2006 annual physical inventory. These missing equipment items were not removed from the active equipment listing until September 2007.
- Three equipment items had no fixed asset tag; however, we identified two of the items by the serial number.

Title 29 CFR section 97.32 requires the State to use, manage, and dispose of equipment in accordance with its laws and procedures. Office of State Controller's Fixed Asset Policies requires inventory to be taken at least annually. The risk that items could be lost or misappropriated without detection increases when inventories are not taken and reconciled to the property records.

This finding impacts the Employment Services program for grant year July 1, 2006 – June 30, 2007 (Grant number ES157140656).

## AUDIT FINDINGS AND RESPONSES (CONCLUDED)

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*Recommendation:* The Commission should strengthen procedures to ensure that the annual physical inventory is performed on all cost centers and reconciled to the fixed asset system. The reconciliation process should include locating, determining and recording the disposition of all missing assets in a timely manner. Additionally, all equipment items should be properly tagged to ensure that fixed assets can be scanned and located.

*Agency's Response:* The current inventory process is being reviewed and some procedures are being changed to ensure that all cost centers are inventoried. New cost centers folders are being prepared to ensure that all documentation pertaining to that cost center are filed in one location. New procedures have been put in place regarding new IT equipment that is received. Assets that did not have a property tag will be tagged and new tag information entered into Magic. The current inventory will be completed by the end of June, 2008. The reconciliation process will include locating, determining, and recording the disposition of all missing assets in a timely manner. Cross-training is being done to ensure that the inventory program is not dependent on one person.

## **ORDERING INFORMATION**

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Audit reports issued by the Office of the State Auditor can be obtained from the web site at [www.ncauditor.net](http://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:

Office of the State Auditor  
State of North Carolina  
2 South Salisbury Street  
20601 Mail Service Center  
Raleigh, North Carolina 27699-0601

Telephone: 919/807-7500

Facsimile: 919/807-7647