



STATE OF NORTH CAROLINA

OFFICE OF THE STATE CONTROLLER

STATEWIDE FINANCIAL STATEMENT AUDIT PROCEDURES

FOR THE YEAR ENDED JUNE 30, 2009

OFFICE OF THE STATE AUDITOR

BETH A. WOOD, CPA

STATE AUDITOR

OFFICE OF THE STATE CONTROLLER

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FOR THE YEAR ENDED JUNE 30, 2009

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BETH A. WOOD, CPA

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Beth A. Wood, CPA
State Auditor

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Office of the State Auditor

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AUDITOR'S TRANSMITTAL

The Honorable Beverly Eaves Perdue, Governor
Members of the North Carolina General Assembly
David T. McCoy, State Controller
Office of the State Controller

We have completed certain audit procedures at the Office of the State Controller 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, 2009. 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. Our audit procedures were conducted in accordance with auditing standards generally accepted in the United States of America and *Government Auditing Standards*, issued by the Comptroller General of the United States.

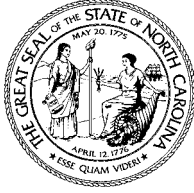
Our audit objective was to render an opinion on the State of North Carolina's financial statements and not the Office of the State Controller's financial statements. However, the report included herein is in relation to our audit scope at the Office of the State Controller and not to the State of North Carolina as a whole.

The audit finding referenced in the report is also evaluated to determine its impact on the State's internal control and the State's compliance with rules, regulations, contracts and grants. If determined necessary in accordance with *Government Auditing Standards*, the finding is reported in the State's *Single Audit 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.

A handwritten signature in cursive script that reads "Beth A. Wood".

Beth A. Wood, CPA
State Auditor



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**REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING
AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN
AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH
GOVERNMENT AUDITING STANDARDS**

David T. McCoy, State Controller
and Management of the Office of the State Controller

As part of our audit of the State of North Carolina's financial statements, we have audited selected elements of the Office of the State Controller's financial statements, as of and for the year ended June 30, 2009. Our report on the State of North Carolina's financial statements is included in the State's *Comprehensive Annual Financial Report*. Our financial statement audit scope at the Office of the State Controller included the following:

- Internal Control over Statewide Financial Reporting
- Preparation of the State's *Comprehensive Annual Financial Report*

The audit results described below are in relation to our audit scope at the Office of the State Controller and not to the State of North Carolina as a whole.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Office of the State Controller's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the State's financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Office of the State Controller's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Office of the State Controller's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, we identified a deficiency in internal control over financial reporting that we consider to be a significant deficiency.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to

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prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control. We consider the deficiency described in the Audit Findings and Responses section of this report to be a significant deficiency in internal control over financial reporting.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the entity's internal control.

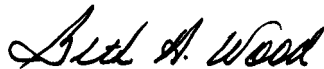
Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, we do not believe the significant deficiency described above is a material weakness.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the State's financial statements are free of material misstatement, we performed tests of compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed an instance of noncompliance that is required to be reported under *Government Auditing Standards* and which is described in the Audit Findings and Responses section of this report.

Management's response to the finding identified in our audit is included in the Audit Findings and Responses section of this report. We did not audit the response, and accordingly, we express no opinion on it.

This report is intended solely for the information and use of management, the State Controller, others within the entity, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.



Beth A. Wood, CPA
State Auditor

December 8, 2009

AUDIT FINDINGS AND RESPONSES

Matters Related to Financial Reporting

BANK ACCOUNT NOT RECONCILED TIMELY

The Office of State Controller did not complete monthly bank reconciliations of the State's payroll account in a timely manner. This increases the risk that a misstatement in the State of North Carolina's financial statements could go undetected and uncorrected.

In January 2008, the Office of the State Controller implemented a new payroll system called BEACON that is used to process over \$350 million of monthly payroll and related costs. The process of reconciling the BEACON payroll records to the corresponding bank account was under development during 2008, but a fully-developed reconciliation process was not implemented until March 2009. Although, the March 2009 bank reconciliation was performed within 15 days of the date of the bank statement, there were several reconciling items that originated as early as July 2008 that were not resolved until July 2009. In addition, the three monthly reconciliations for April 2009 through June 2009 were completed 17 to 51 days after the statement date. Accordingly, outstanding items were not identified, researched, and corrected in a timely manner.

The *North Carolina Administrative Code* (Section 20 NCAC 01C.0402) requires all agencies to reconcile their bank statements, called disbursing account statements, within 15 days of the statement date. In addition, the Department of State Treasurer makes account statements available on the first day of each month for the previous month and requires agencies to verify the reconciliations have been performed.

Significant aspects of this finding were also reported in the prior year.

Recommendation: The Office of State Controller should enhance internal control to ensure the bank statement for BEACON payroll is properly reconciled each month. Adequate reconciliation procedures include promptly investigating and resolving outstanding items, as well as an appropriate level of management review and approval.

Agency Response: The Office of the State Controller concurs with your audit finding that the payroll disbursing account bank reconciliation process was not completed within 15 days of the statement date each month during the fiscal year ended June 30, 2009. During FY2008-2009, the bank reconciliation processes were re-designed to align with the payroll accounting operations staff's system access security. Certain reconciling entries were identified and researched that allowed the payroll accounting staff to be trained in the new processes using real-life scenarios and provided additional verification that the reconciling item was valid. All reconciling items were posted to the General Ledger for year end closing. It is also important to note that no material misstatements were made in the State of North Carolina's financial statements due to these late reconciliations.

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