



STATE OF NORTH CAROLINA

EMPLOYMENT SECURITY COMMISSION

STATEWIDE FINANCIAL STATEMENT AUDIT PROCEDURES

FOR THE YEAR ENDED JUNE 30, 2009

OFFICE OF THE STATE AUDITOR

BETH A. WOOD, CPA

STATE AUDITOR

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STATE OF NORTH CAROLINA
Office of the 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>

AUDITOR'S TRANSMITTAL

The Honorable Beverly Eaves Perdue, Governor
Members of the North Carolina General Assembly
Mr. Moses Carey, 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, 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 Commission's financial statements. However, the report included herein is in relation to our audit scope at the Commission and not to the State of North Carolina as a whole.

The audit findings referenced in the report are also evaluated to determine their 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*, these findings are 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**

Mr. Moses Carey, Jr., Chairman
and management of Employment Security Commission

As part of our audit of the State of North Carolina's financial statements, we have audited selected elements of the Employment Security Commission'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 Employment Security Commission included the following:

- Enterprise Fund – Unemployment Compensation Fund

The audit results described below are in relation to our audit scope at the Commission 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 Commission'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 Commission's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Commission'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 certain deficiencies in internal control over financial reporting that we consider to be significant deficiencies.

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 prevent or detect misstatements on a timely basis. A significant deficiency is a control

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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 deficiencies described in all findings in the Audit Findings and Responses section of this report to be significant deficiencies 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 believe that none of the significant deficiencies 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 no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Management'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.

This report is intended solely for the information and use of management, Commission Chairman Carey, others within the entity, the Governor, the General Assembly, 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 4, 2009

AUDIT FINDINGS AND RESPONSES

Matters Related to Financial Reporting

The following findings and recommendations were identified during the current audit and discuss conditions that represent deficiencies in internal control and/or noncompliance with laws, regulations, contracts, or grants.

1. INAPPROPRIATE INFORMATION SYSTEM ACCESS

The Employment Security Commission allowed employees to have system access rights that were not necessary for their assigned job functions. As a result, there is an increased risk of errors and fraudulent transactions. We noted the following access deficiencies:

- In the financial accounting and reporting system, we identified 11 employees with inappropriate update authority to groups including the accounts payable, vendor master file, and procurement review and receipting groups.
- In the unemployment insurance tax system, we identified 208 users with inappropriate update authority to groups including the employer master file, wage record update, accounts receivable/payable creation, employer contribution rate update and tax department management function. Additionally, there were six users with inappropriate update access rights to the unemployment tax table.
- In the unemployment insurance benefits system, we identified 2,822 instances of inappropriate or unnecessary update access. These improper accesses allowed the various users the ability to manipulate data, which impacts the amount of benefits paid as well as access to confidential information.

In addition, we identified 12 instances where users were assigned multiple user names in error by the Commission's information systems help desk.

Maintaining proper access controls over computer systems helps protect the confidentiality and integrity of information by preventing alteration, unauthorized use, or loss of data. Statewide information technology standards specify that system access be controlled and prescribe procedures such as documented reviews of users' rights.

Aspects of this finding were also reported in a previous fiscal control audit of the Commission.

Recommendation: The Commission should improve internal controls to ensure periodic security reviews are conducted and personnel are granted only the necessary system access necessary to perform their job duties.

Agency's Response: The Commission's Help Desk distributes a RACF access listing on a quarterly basis. Managers and supervisors are required to review this report and certify that the employees under their supervision require the stated clearances to perform their job duties. Unneeded clearances may be deleted by so indicating on the report. The manager via the Network User Request (NUR) process must request any additional clearances.

AUDIT FINDINGS AND RESPONSES (CONCLUDED)

The auditors recommended that a second report be created and provided to data owners on a periodic basis to allow review of which employees have access to each clearance level. When coupled with the current quarterly review, this report will provide an access cross check. ESC agrees with this recommendation and is in the process of designing the reports and associated response process (evaluation of the special extracts done for the auditors revealed these reports to be inappropriate for general distribution). Once complete, the new reports will be distributed to the data owners on an annual basis.

The instances of inappropriate access identified by the auditors either have been corrected or currently are in the correction process. The Help Desk will run additional checks prior to the issuance of new user IDs to preclude the erroneous assignment of multiple user IDs to the same employee. The Help Desk also will conduct periodic reviews to assure the process is working as designed.

2. WEAKNESSES NOTED IN CASH RECONCILIATION PROCESS

The Employment Security Commission did not fully reconcile the cash balance in the accounting records to the balance in the bank. Failing to properly reconcile accounts and resolve outstanding items may lead to unrecorded or improperly recorded transactions, resulting in financial reporting errors and possibly misappropriations that go undetected.

The Commission's reconciliation for the State Treasurer account begins with the bank balance but only reconciles to a daily recap spreadsheet of checks written, cancelled, cleared, and voided. It does not clearly reconcile to the balance in the accounting records.

The Commission reconciles the U.S. Treasury account to a daily cash flow summary spreadsheet but does not clearly reconcile to the balance in the accounting records.

Additionally, the reconciliations have several reconciling items that have been outstanding for months and even years. The State Treasurer account reconciliation has reconciling items in excess of \$85,000 that have been outstanding since 2006. Also, the U.S. Treasury account reconciliation as of June 2009 had a \$20,870 amount that could not be reconciled and a \$319,000 reconciling item that had not cleared in eight months.

Recommendation: The Commission should implement internal controls to ensure that complete and proper reconciliations are performed. Management should dedicate the necessary resources to ensure that balances in the accounting records are clearly reconciled to the bank balances and that reconciling items are properly investigated and resolved.

Agency's Response: The Commission will implement an additional internal control which will tie the current individual reconciliation processes together and clearly demonstrate that balances in the accounting records reconcile to the bank balances.

In addition, efforts will be made to resolve the outstanding reconciling items in a timely manner.

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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. 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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