



STATE OF NORTH CAROLINA

OFFICE OF THE STATE CONTROLLER

STATEWIDE FINANCIAL STATEMENT AUDIT PROCEDURES

FOR THE YEAR ENDED JUNE 30, 2010

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, 2010

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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, 2010. 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 the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

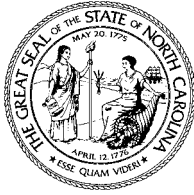
Our audit objective was to render an opinion on the State of North Carolina's financial statements and not the Office of the State Controller's financial statements. However, the report included herein is in relation to our audit scope at the Office of the State Controller and not to the State of North 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, 2010. 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.

A *deficiency in internal control* 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 *material weakness* is a deficiency or combination of deficiencies in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency or combination of

**REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING
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deficiencies in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.


Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies, or material weaknesses, and therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above. However, 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, as defined above.

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 its 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, 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 8, 2010

AUDIT FINDINGS AND RESPONSES

Matters Related to Financial Reporting

BANK ACCOUNT INADEQUATELY RECONCILED

The Office of the State Controller has not fully reconciled the monthly bank balance in the State's payroll account since the new payroll system was implemented in January 2008. This increases the risk that a misstatement in the State of North Carolina's financial statements could go undetected and uncorrected.

The State's payroll system is used to process over \$350 million of monthly payroll and related costs. The Office of State Controller prepares a monthly bank reconciliation, but each month "balancing entries," which represent a net difference between the book and bank balance, have been reported in the reconciliation. These monthly differences must be accumulated to make the payroll records reconcile to the bank account each month. Over the period of January 2008 to June 2010, these "balancing entries" have ranged from an understated book balance of \$48,000 to an overstated book balance of \$52,000. Although the Office of State Controller has attempted to resolve the differences, the cause of these reconciling items was not identified or resolved as of June 30, 2010.

The *North Carolina Administrative Code* (Section 20 NCAC 01C.0402) requires all agencies to reconcile their bank statements. In addition, the Department of the State Treasurer requires agencies to verify that reconciliations have been performed.

Significant aspects of this finding were reported as a result of the last two financial statement audits.

Recommendation: The Office of the State Controller should ensure that the bank statement for the State's payroll account is fully reconciled each month. Adequate reconciliation procedures include promptly investigating and resolving unexplained variances.

Agency Response: The Office of State Controller concurs with your audit finding that our office had not fully reconciled the monthly bank balance in the State's payroll disbursing account as of June 30, 2010. The Office continues to refine the bank reconciliation internal procedures to identify causes and make appropriate adjustments for differences between the bank balance and the general ledger balance for this account. It is also important to note that no material misstatements were made in the State of North Carolina's financial statements due to the bank account not being fully reconciled.

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