



STATE OF NORTH CAROLINA

DEPARTMENT OF TRANSPORTATION

STATEWIDE FINANCIAL STATEMENT AUDIT PROCEDURES

FOR THE YEAR ENDED JUNE 30, 2010

OFFICE OF THE STATE AUDITOR

BETH A. WOOD, CPA

STATE AUDITOR

DEPARTMENT OF TRANSPORTATION

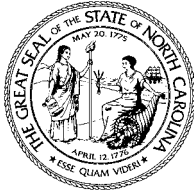
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AUDITOR'S TRANSMITTAL

The Honorable Beverly Eaves Perdue, Governor
Members of the North Carolina General Assembly
Mr. Eugene A. Conti, Jr., Secretary
Department of Transportation

We have completed certain audit procedures at the Department of Transportation 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.

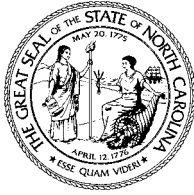
Our audit objective was to render an opinion on the State of North Carolina's financial statements and not the Department's financial statements. However, the report included herein is in relation to our audit scope at the Department and not to the State of North Carolina as a whole.

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. Eugene A. Conti, Jr.
and Management of Department of Transportation

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

- Special Revenue - Highway Fund
- Special Revenue - Highway Trust Fund
- Capital Assets Used In Governmental Activities

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

**REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING
AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN
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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 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 all of the deficiencies described in the Audit Findings and Responses section of this report to be significant deficiencies 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 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, Secretary Conti, others within the entity, the Governor, the General Assembly, 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

1. PAYROLL TIME ENTRIES NOT VERIFIED

The Department's control procedures to ensure the accuracy of payroll time entries are not being followed. As a result, there is an increased risk of improper payroll payments.

A report is produced from the payroll system after each employee's time has been entered into the payroll system. The Department's policy requires the hours on this report to be agreed to the timesheets. The policy also states that a copy of the report should be printed, initialed, dated, and retained along with original timesheets.

In our sample of 60 employees, we noted the following:

- Three instances where the payroll reports were not printed, initialed, dated, or retained along with the original timesheets.
- Ten instances where the payroll reports were not initialed or dated to confirm that the accuracy of time entry was checked.
- Nine instances where the payroll reports were not dated to confirm when the accuracy of the time entry was verified.

This finding was also reported in the prior year.

Recommendation: The Department should ensure that policies and procedures regarding time entry and approval are followed to ensure that time entered into the payroll system is properly verified.

Agency Response: NCDOT will intensify efforts to educate time keepers of the control procedures that must be followed to ensure time entered into financial system is properly verified. An Employee News notification will be distributed to all NCDOT system users in January, 2011. Quarterly reminders will be sent to time keepers and paymasters through automated system workflow messages. A quick view reminder will be developed and distributed to serve as a checklist for those entering time into the system in February, 2011. Areas identified in the audit were contacted and proper procedures were reviewed in October, 2010.

Anticipated Completion Date: Various

2. INAPPROPRIATE ACCESS TO INFORMATION SYSTEMS

The Department did not maintain adequate internal control over access to its computer systems and data. As a result, there is an increased risk that unauthorized access to accounting systems and inappropriate changes to financial data could occur and go undetected.

AUDIT FINDINGS AND RESPONSES (CONTINUED)

The following deficiencies were noted:

- Four of 11 terminated employees tested did not have their access to the accounting system terminated for at least 30 days after they were separated. One of the four was terminated for conduct but continued to have access to the accounting system for 54 days. The *Statewide Information Security Manual* requires access to be immediately terminated upon leaving employment.
- The Department's accounting system and highway construction management subsystem inactivity parameters are not in compliance with statewide standards. A user's access is automatically disabled after 60 days of inactivity in the accounting system and 90 days of inactivity in the highway construction management subsystem. The *Statewide Information Security Manual* states that user IDs must be disabled after 30 days of inactivity.
- The Department did not review and has never recertified the access rights granted to users of the highway construction management subsystem. Statewide standards require a documented review of users' rights semi-annually.

Recommendation: The Department should ensure that its procedures for promptly disabling separated employees' access are followed. The Department should set parameters in both the accounting system and the highway construction materials system to disable a user's ID after 30 days of inactivity. Semi-annual reviews should be performed to ensure that employees' access is appropriate.

Agency Response: The NCDOT Information Technology Unit at BSIP (Business System Improvement Project) receives an automated report of terminated employees from the State's Human Resource Information System (Beacon) that is run daily and emailed to BSIP Security. The BSIP Security team then works this report daily to revoke user access of terminated employees based on the data provided. The data on this report is only as accurate as the data entered to Beacon by the business units when the actual dates of termination occur. The IT unit continues to work with our Human Resources Unit to stress that a delay in entering the dates of termination causes delays in system revocation of access. There is no other source to notify us to revoke access of users so dependency on correct and timely entry of termination is critical.

After review of our accounting system and highway construction management system for inactivity parameters, both systems are being corrected to be 30 consecutive days of inactivity, per the *Statewide Information Security Manual*.

Anticipated Completion Date: March 31, 2011

Statewide standards require a documented review of users' rights semi-annually. To accomplish this for HiCAMS the Information Technology Unit will generate a report semi-annually for review by the Central Construction Unit (CCU) and Materials & Tests Unit (M&T) of all NCDOT users rights to the system for internal users. For external users, IT will generate a report, segregated by company, for review by CCU and M&T,

AUDIT FINDINGS AND RESPONSES (CONCLUDED)

which can be forwarded to each material supplier/producer for review of users with rights to enter/review data for their company.

Anticipated Completion Date: February 28, 2011

3. APPROVAL PROCEDURES NOT FOLLOWED FOR RIGHT OF WAY ACQUISITIONS

The Department paid for right of way acquisitions without obtaining the approvals that were required by its policy. The lack of proper approval increases the risk that claims for the acquisition of right of way or other property could be made in error or that fraudulent transactions could occur.

The final report form and other supporting documents are assembled after negotiations have been concluded with a property owner for the acquisition of rights of way. The Department's policy states that these documents will be submitted to either the Manager of Right of Way or the Assistant Manager of Right of Way for acceptance and approval for payment. The policy also states that the State Highway Administrator must approve claims with total payments exceeding \$500,000.

Our test of 89 disbursements for right of way acquisitions revealed the following:

- One right of way final report was approved by the right of way accountant instead of the right of way manager or assistant manager. This presents a segregation of duties problem since the accountant also has the ability to enter and approve the payment in the accounting system.
- Three of the five right of way documents in our sample that were for amounts exceeding \$500,000 were not approved by the State Highway Administrator as required by the Department's policy.

Three of the four errors noted above were for acquisitions funded by the Highway Construction Grant.

Federal Grant Award Information: Highway Planning and Construction 2010

Recommendation: The Department should ensure that all final reports for right of way acquisitions are approved in accordance with the guidelines set forth in its *Right of Way Manual*. Care should be taken when assigning tasks to ensure that duties are adequately segregated.

Agency Response: The Right of Way Branch has reinforced with staff members the need to follow established procedures and guidelines in the approval of final reports for right of way acquisitions. In addition, a check list has been developed to better track required reviews and approvals and ensure segregation of duties. This has been incorporated in the *Right of Way Manual*.

Anticipated Completion Date: October, 2010

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