



# STATE OF NORTH CAROLINA

**OFFICE OF INFORMATION TECHNOLOGY SERVICES**

**STATEWIDE FEDERAL COMPLIANCE AUDIT PROCEDURES**

**FOR THE YEAR ENDED JUNE 30, 2008**

**OFFICE OF THE STATE AUDITOR**

**BETH A. WOOD, CPA**

**STATE AUDITOR**

**OFFICE OF INFORMATION TECHNOLOGY SERVICES**  
**STATEWIDE FEDERAL COMPLIANCE AUDIT PROCEDURES**  
**FOR THE YEAR ENDED JUNE 30, 2008**

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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**

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The Honorable Beverly E. Perdue  
Members of the North Carolina General Assembly  
Mr. George Bakolia, State Chief Information Officer  
Office of Information Technology Services

We have completed certain audit procedures at the Office of Information Technology Services related to the State of North Carolina reporting entity as presented in the *Single Audit Report* for the year ended June 30, 2008. Our audit was performed by authority of Article 5A of Chapter 147 of the *North Carolina General Statutes*.

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 major federal 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.

Our audit objective was to render an opinion on the State of North Carolina's administration of federal programs and not the Office of Information Technology Services' administration of major federal programs. However, the report included herein is in relation to our audit scope at the Office of Information Technology Services 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* or the Single Audit Act, this 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 COMPLIANCE WITH REQUIREMENTS APPLICABLE TO EACH  
MAJOR PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE  
IN ACCORDANCE WITH OMB CIRCULAR A-133**

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Mr. George Bakolia  
and Management of the Office of Information Technology Services

Compliance

As part of our audit of the State of North Carolina's compliance with the types of requirements described in the *OMB Circular A-133 Compliance Supplement* that are applicable to each of its major programs for the year ended June 30, 2008, we have performed audit procedures at the Office of Information Technology Services. Our report on the State of North Carolina's compliance with requirements applicable to each major program and on internal control over compliance in accordance with OMB Circular A-133 is included in the State's *Single Audit Report*. Our federal compliance audit scope at the Office of Information Technology Services included the following:

- Billed Central Services Costs

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

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination of compliance with those requirements.

The results of our audit procedures at the Office of Information Technology Services disclosed no instances of noncompliance that are required to be reported in accordance with OMB Circular A-133.

**REPORT ON COMPLIANCE WITH REQUIREMENTS APPLICABLE TO EACH  
MAJOR PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE  
IN ACCORDANCE WITH OMB CIRCULAR A-133 (CONTINUED)**

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Internal Control Over Compliance

Management is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered internal control over compliance with the requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of internal control over compliance.

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

A control deficiency in an entity's internal control over compliance 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 noncompliance with a type of compliance requirement of a federal program on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to administer a federal program such that there is more than a remote likelihood that noncompliance with a type of compliance requirement of a federal program 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.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that material noncompliance with a type of compliance requirement of a federal program will not be prevented or detected by the entity's internal control. We did not consider the deficiency described in the Audit Findings and Responses section of this report to be a material weakness in relation to our audit scope at the Office of Information Technology Services.

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.

**REPORT ON COMPLIANCE WITH REQUIREMENTS APPLICABLE TO EACH  
MAJOR PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE  
IN ACCORDANCE WITH OMB CIRCULAR A-133 (CONCLUDED)**

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This report is intended solely for the information and use of management, Mr. Bakolia, 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*

Beth A. Wood, CPA  
State Auditor

March 10, 2009

## **AUDIT FINDINGS AND RESPONSE**

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### **Matters Related to Federal Compliance Objectives**

#### UNALLOWABLE COSTS TRANSFERRED TO THE COMPUTING SERVICES FUND

The Office of Information Technology Services transferred unallowable costs to the Computing Services Fund resulting in noncompliance with federal central service cost guidelines. Enterprise license expense of \$500,000 was transferred from the SAS Licensing Fund to the Computing Services Fund so that the SAS Licensing Fund would not have a negative balance. The cost of the license fees did not benefit the agencies charged for computing services and should not have been transferred to this fund.

OMB Circular A-87, Attachment C, G.1 states that each billed central service activity must separately account for all expenses incurred to furnish the service. Also, inclusion of the unallowable cost will affect future rate setting for billed computing services central service costs.

*Recommendation:* The Office of Information Technology should correct the error for future rate setting and incorporate this adjustment in the revised 2008 refund calculation. Management should be reminded of the importance of accurately accounting for costs in each billed service fund.

*Agency Response:* ITS partially agrees with this finding. A portion of the \$500k transferred from the SAS Licensing Fund to the Computing Services Funds did benefit the agencies charged for computing services. Approximately \$251k of the \$500k was allowable as it supports SAS licenses that are deployed by State Agencies.

ITS has recalculated the refund which created a difference of \$7,645.95 for Computing Services. This difference will be applied to the agencies' subsequent year's refund(s). ITS will more carefully analyze each proposed transfer from a "Billed Service Fund" to determine the correctness of each transfer as an allowable cost, based on the Circular A-87 Guidelines. Additionally, ITS has created distinctive call centers beginning this fiscal year to assist in tracking these expenses.

*Anticipated Completion Date:* The recalculation was completed on February 18, 2009 and the difference will be applied during the next refund cycle.

*Auditor's Response:* At the time of the audit, ITS did not present documentation regarding the \$251K. Based on the additional information provided by ITS, this amount was computed by allocating \$600,000 to the Computer Services Fund based on maintenance fees expense. We were unable to substantiate why \$600,000 was used instead of the \$500,000 in question, nor why the costs were allocated based on maintenance fees instead of license fees expense. Therefore, we did not modify the \$500,000 unallowable cost issue in this audit finding.

## 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:

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