



# STATE OF NORTH CAROLINA

DEPARTMENT OF COMMERCE

STATEWIDE FEDERAL COMPLIANCE AUDIT PROCEDURES

FOR THE YEAR ENDED JUNE 30, 2010

OFFICE OF THE STATE AUDITOR

BETH A. WOOD, CPA

STATE AUDITOR

**DEPARTMENT OF COMMERCE**

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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 Eaves Perdue, Governor  
Members of the North Carolina General Assembly  
Mr. J. Keith Crisco, Secretary  
Department of Commerce

We have completed certain audit procedures at the Department of Commerce related to the State of North Carolina reporting entity as presented in the *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 *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; 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*.

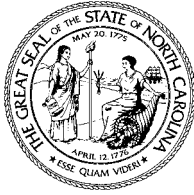
Our audit objective was to render an opinion on the State of North Carolina's, and not the Department's, administration of major federal programs. However, the report included herein is in relation to our audit scope at the Department and not to the State of North Carolina as a whole.

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* or the OMB Circular A-133, 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



Beth A. Wood, CPA  
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**REPORT ON COMPLIANCE WITH REQUIREMENTS THAT COULD HAVE A  
DIRECT AND MATERIAL EFFECT ON EACH MAJOR PROGRAM AND ON  
INTERNAL CONTROL OVER COMPLIANCE  
IN ACCORDANCE WITH OMB CIRCULAR A-133**

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Secretary J. Keith Crisco  
and Management of the Department of Commerce

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 could have a direct and material effect on each of its major programs for the year ended June 30, 2010, we have performed audit procedures at the Department of Commerce. Our report on the State of North Carolina's compliance with requirements that could have a direct and material effect on 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 Department of Commerce included the following:

- Community Development Block Grant - State-Administered Small Cities Program Cluster (CFDA 14.228 and CFDA 14.255)
- Workforce Investment Act of 1998 (WIA) Cluster - Adult Program (CFDA 17.258), Youth Activities (CFDA 17.259), Dislocated Workers (CFDA 17.260)
- Weatherization Assistance for Low-Income Persons (CFDA 81.042)

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 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

**REPORT ON COMPLIANCE WITH REQUIREMENTS THAT COULD HAVE A  
DIRECT AND MATERIAL EFFECT ON EACH MAJOR PROGRAM AND ON  
INTERNAL CONTROL OVER COMPLIANCE  
IN ACCORDANCE WITH OMB CIRCULAR A-133 (CONTINUED)**

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opinion. Our audit does not provide a legal determination of the Department's compliance with those requirements.

The results of our audit procedures at the Department of Commerce disclosed instances of noncompliance that are required to be reported in accordance with OMB Circular A-133 and which are described in findings 1 through 7 and 9 through 11 in the Audit Findings and Responses section of this report.

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 to determine the auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133, 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.

*A deficiency in internal control over compliance* exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. *A material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. *A significant deficiency in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Our consideration of the internal control over compliance 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 compliance 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. However, we consider the deficiencies described in findings 1, 2, 3, 7, and 11 in the Audit Findings and Responses section of this report to be material weaknesses in internal control over compliance, as defined above. Furthermore, we consider the deficiencies described in

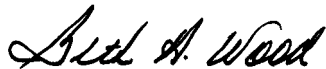
**REPORT ON COMPLIANCE WITH REQUIREMENTS THAT COULD HAVE A  
DIRECT AND MATERIAL EFFECT ON EACH MAJOR PROGRAM AND ON  
INTERNAL CONTROL OVER COMPLIANCE  
IN ACCORDANCE WITH OMB CIRCULAR A-133 (CONCLUDED)**

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findings 4, 5, 6, 8, 9, and 10 in the Audit Findings and Responses section of this report to be significant deficiencies in internal control over compliance, as defined above.

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 J. Keith Crisco, 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

March 11, 2011

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## **AUDIT FINDINGS AND RESPONSES**

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

#### **WEATHERIZATION ASSISTANCE FOR LOW-INCOME PERSONS - CFDA 81.042**

##### **1. SUBRECIPIENT MONITORING NEEDS IMPROVEMENT**

The Department of Commerce did not consistently perform adequate monitoring procedures to ensure subrecipients of the Weatherization Assistance for Low-Income Persons grant were in compliance with all applicable federal requirements. As a result, there is an increased risk that noncompliance with federal requirements could occur at the subrecipient level and not be detected by the Department.

During our review of the Department's on-site monitoring inspections, we noted the following deficiencies:

- a. The Department's procedures and current staffing levels were not adequately designed to ensure all subrecipients receive comprehensive monitoring at least once per year as required by guidance from the U.S. Department of Energy. As a result, we found that the Department did not monitor 23 of 28 subrecipients receiving American Recovery and Reinvestment Act (ARRA) funds, nor did they monitor 12 of 28 subrecipients receiving regular Weatherization Assistance funds.
- b. The Department's procedures were not designed to ensure that for each subrecipient at least 5% of completed units were inspected as required by guidance from the U.S. Department of Energy. As a result, we found that the Department did not inspect the required amount of completed units for 26 of 28 subrecipients receiving ARRA funds and 13 of 28 subrecipients receiving regular Weatherization Assistance funds. As a result, there is an increased risk that the weatherization work being performed could be deficient and not be detected timely by the Department and perhaps not be corrected.
- c. In our tests of the site visits that were conducted by the Department, we found the monitoring documentation for one of the five that we tested had not been reviewed and approved by the appropriate supervisory personnel. As a result, there is a deficiency in internal control and an increased risk that the site visits performed may be incomplete or inaccurate.
- d. The Department's procedures did not include monitoring their subrecipients' activities for compliance with suspension and debarment requirements. As a result, the Department did not ensure that the subrecipients were not entering into transactions with suspended or debarred entities.
- e. The Department's procedures did not include monitoring their subrecipients for compliance with federal requirements related to vehicle purchases. As a result, the Department did not ensure that vehicles purchased by the subrecipients with federal funds received prior approval from the U.S. Department of Energy.



## AUDIT FINDINGS AND RESPONSES (CONTINUED)

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- f. The Department's procedures did not include monitoring their subrecipients for compliance with program income requirements. As a result, the Department did not determine if program income had been earned and, when applicable, properly used by the subrecipients.
- g. The Department's procedures did not include monitoring their subrecipients' average cost per completed unit. As a result, the Department did not ensure that subrecipients' average cost per unit weatherized was within the required federal limits.
- h. For ARRA awards, the Department's procedures did not include monitoring their subrecipients' Schedule of Expenditures of Federal Awards (SEFA) for compliance with federal reporting requirements. As a result, the Department did not ensure that subrecipients properly identified ARRA funds in their SEFA.

The *OMB Circular A-133 Compliance Supplement* states that subrecipients should be monitored to provide reasonable assurance that the subrecipient administers federal awards in compliance with laws, regulations, and the provisions of contracts or grant agreements and that performance goals are achieved. Per the *U.S. Department of Energy Program Year 2010 Weatherization Grant Guidance*, the State must conduct comprehensive monitoring of each subgrantee at least once per year. The comprehensive monitoring must include a review of client files and subgrantee records, as well as actual inspection of at least five percent of the completed units.

*Federal Award Information:* This finding affects CFDA 81.042 Weatherization Assistance for Low-Income Persons award DE-FG26-07NT43134 for the award period July 1, 2007 - June 30, 2010 and ARRA award DE-EE0000118 for the award period April 1, 2009 - March 31, 2012.

*Recommendation:* The Department should strengthen internal controls to ensure that all applicable federal compliance requirements are included in their subrecipient monitoring procedures. The Department should also ensure the appropriate staff is in place so that all subrecipients can be adequately monitored once per year and that at least five percent of the completed units are inspected.

*Agency Response:*

- a. For ARRA, the Department hired seven staff in August 2010 who now are trained and equipped to meet DOE Guidelines for monitoring. For regular WAP, the Department is in the final stages of hiring an additional program monitor. The Department has instituted a tracking spreadsheet to ensure comprehensive monitoring takes place.
- b. The Department has completed one (1) comprehensive monitoring visit for each agency and plans to have monitored five (5) percent of units completed by subrecipients prior to March 30, 2011. Thereafter, subrecipients will be adequately monitored through the end of the fiscal year to comply with DOE monitoring guidance. The Department will complete 5% monitoring prior to the end of the fiscal year - June 2011.

## **AUDIT FINDINGS AND RESPONSES (CONTINUED)**

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- c. The Department instituted internal controls to prevent this oversight in the future. Supervisory personnel will now verify that all necessary signatures have been obtained before signing the final assessment letter.
- d. Contracts between the Department and its subrecipients require the subrecipient to certify that they will not use contractors that are on the debarment, suspension, and ineligible and voluntary exclusion lists. Effective March 2011, the Department will review subrecipients' activities for compliance with suspension and debarment requirements as part of fiscal monitoring and include additional provisions on the monitoring tool related to suspension and debarment.
- e. The Department has updated its subrecipient policy and guidelines manual and has trained subrecipients on the compliance procedures related to vehicle purchases. Effective March 2011, the Department will review and document their subrecipients' compliance with federal requirements related to vehicle purchases as part of fiscal monitoring.
- f. The Department captures subrecipient program income on the monthly financial status report. Effective March 2011, the Department will review and document their subrecipients' compliance with program income requirements as part of fiscal monitoring.
- g. The subrecipients' average cost per unit is now detailed on the monthly financial status report and electronically flagged for excessive averages. The average cost per unit was reviewed and supplemental documentation provided to each subrecipient in September 2010 and February 2011. The Department is in compliance with federal rules for North Carolina average cost per unit requirements.
- h. The Department notified subrecipients in October 2009 of federal requirements related to SEFA compliance. Effective March 2011, the Department will review and document subrecipients' compliance with SEFA as part of fiscal monitoring.

Anticipated Completion Date: June 30, 2011

### **2. DEFICIENCIES IN CASH MANAGEMENT**

For the Weatherization Assistance for Low-Income Persons grant, the Department of Commerce did not have effective procedures in place to ensure timely disbursement of federal funds or to timely request federal reimbursement of program expenditures paid to subrecipients. Payments to subrecipients were generally made using funds other than federal Weatherization funds, and as a result, the Department has violated both state and federal cash management requirements.

The Department of Commerce began processing subrecipient payments and federal drawdowns for the Weatherization grant in January 2010 (the program was previously administered by another state department). Based on our review of the Department's federal drawdown procedures from January 2010 to June 2010, we noted that for the Weatherization grant they did not consider the actual expenditures paid to subrecipients to determine the requested amount and they did not attempt to minimize the time between

## AUDIT FINDINGS AND RESPONSES (CONTINUED)

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the date of disbursement and the date a drawdown request was sent to the federal agency. As a result, a receipt from the federal agency could take place weeks before or after the payments were made to subrecipients.

We analyzed the population of Weatherization grant payments to subrecipients and the corresponding federal draws that were processed by the Department. For the 231 ARRA payment requests and 340 regular Weatherization payment requests, we noted the following deficiencies:

- For 13 ARRA payments to subrecipients valued at \$653,414 and five regular Weatherization payments to subrecipients valued at \$54,147, the funds were drawn from the federal agency four to nine working days before they were disbursed to subrecipients. As a result, the Department did not comply with federal requirements to minimize the time elapsing between the drawdown of funds and disbursement to subrecipients.
- For 196 ARRA payments to subrecipients valued at \$16.7 million and 169 regular Weatherization payments to subrecipients valued at \$2.68 million the funds were drawn from the federal agency four to 33 working days after the Department paid the subrecipients. As a result, funds used to pay the subrecipients were not promptly reimbursed as required by state statute. However, for these subrecipient payments, it is unclear whether the funds used for the payments were from state funds or other federal programs. We noted that for the period of January 2010 to June 2010, the account used to make the Weatherization payments included deposits from other federal grants, such as the Workforce Investment Act (WIA) Cluster, the State Energy Program ARRA, the Energy Efficient Appliance Rebate Program ARRA, and others.

The *OMB Circular A-133 Compliance Supplement* requires the State to follow procedures to minimize the time elapsing between the transfer of funds from the U.S. Treasury and disbursement. In addition, per *General Statute* 147-86.11 (f.3), North Carolina's cash management policy requires federal and other expenditure reimbursements paid from state funds be paid immediately to the source of the state funds.

*Federal Award Information:* This finding affects CFDA 81.042 Weatherization Assistance for Low-Income Persons award DE-FG26-07NT43134 for the award period July 1, 2007 - June 30, 2010 and ARRA award DE-EE0000118 for the award period April 1, 2009 - March 31, 2012.

*Recommendation:* The Department should strengthen procedures to ensure that federal funds are drawn and disbursed in accordance with federal and state cash management requirements.

*Agency Response:* Weatherization transferred into the Department of Commerce, State Energy Office by legislative fiat for fiscal year 2009 - 10 (SB897) from the Department of Health and Human Services. The merger was made ex post facto; hence, Commerce

## AUDIT FINDINGS AND RESPONSES (CONTINUED)

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did not begin processing payments for Weatherization until January 2010 as referenced in the audit finding.

The Department has implemented a procedure to pay grantees promptly, and in compliance with federal and state cash disbursement requirements.

Anticipated Completion Date: March 31, 2011.

### 3. DEFICIENCIES IN FEDERAL REPORTING

For the Weatherization Assistance for Low-Income Persons grant, the Department of Commerce did not have effective internal controls to ensure compliance with federal reporting requirements. As a result, the Department did not present the quarterly SF-425 reports or the American Recovery and Reinvestment Act (ARRA) Section 1512 reports in accordance with federal reporting requirements.

During our review of the federal reports, we noted the following deficiencies:

- The Department did not review the SF-425 report and its supporting documentation to ensure the report was properly prepared prior to submitting the report. The SF-425 report for the third quarter, which covers the activity period of January 1, 2010 to March 31, 2010, was submitted, but the Department later determined there were errors in the reported expenditures. The report was not corrected and approved by the federal agency until January 24, 2011. In addition, the fourth quarter SF-425, which covers the activity period of April 1, 2010 to June 30, 2010, could not be submitted until the third quarter report was corrected.
- The Department did not review the data or supporting documentation to ensure the accuracy of the information in the ARRA Section 1512 report prior to its submission. In addition, those responsible for compiling the financial data for the report are not fully aware of the reporting requirements or their responsibilities for compiling the report data. As a result, during our tests we found that the fourth quarter report contained misstatements. The amount of funds disbursed to subrecipients was overstated by \$962,915 because the Department incorrectly used disbursements for the period of April 6, 2010 to July 12, 2010, which was not the correct period for the report.

The *OMB Circular A-133 Compliance Supplement* states that recipients of federal awards are expected to have controls in place to ensure compliance with the following reporting requirements: reports for federal awards are required to include all activity of the reporting period, be supported by applicable accounting or performance records, and be fairly presented in accordance with program requirements.

*Federal Award Information:* This finding affects CFDA 81.042 Weatherization Assistance for Low-Income Persons award DE-FG26-07NT43134 for the award period July 1, 2007 - June 30, 2010 and ARRA award DE-EE0000118 for the award period April 1, 2009 - March 31, 2012.

## AUDIT FINDINGS AND RESPONSES (CONTINUED)

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*Recommendation:* The Department should strengthen internal controls to ensure federal reports are prepared in accordance with federal reporting requirements.

*Agency Response:* The Department has assigned staff with reporting knowledge to prepare and submit the reports.

Anticipated Completion Date: March 31, 2011.

#### 4. FEDERAL AWARD NUMBER NOT COMMUNICATED TO ARRA SUBRECIPIENTS

For the Weatherization Assistance for Low-Income Persons grant funded by the American Recovery and Reinvestment Act (ARRA), the Department of Commerce did not communicate the federal award number to each subrecipient at the time of the ARRA award and at the time ARRA funds were disbursed. As a result, the Department did not comply with federal requirements specific to ARRA funds. This increases the risk that subrecipients will not properly identify the ARRA awards and expenditures in their Schedule of Expenditures of Federal Awards and Data Collection Form.

The Department's ARRA awards to subrecipients identify the award as ARRA, the amount of the ARRA funds, and the Catalog of Federal Domestic Assistance (CFDA) number for the Weatherization Assistance for Low-Income Persons grant. However, the federal award number was not included in the award documents. The Department disburses funds based on standard forms that identify the disbursement as ARRA funds, the amount, and the CFDA number, but do not identify the federal award number.

The *OMB Circular A-133 Compliance Supplement* requires the State to separately identify to each subrecipient, and document at the time of the subaward and disbursement of funds, the federal award number, CFDA number, and the amount of ARRA funds; and require their subrecipients to provide similar identification in their Schedule of Expenditures of Federal Awards and Data Collection Form.

*Federal Award Information:* This finding affects CFDA 81.042 Weatherization Assistance for Low-Income Persons ARRA award DE-EE0000118 for the award period April 1, 2009 - March 31, 2012.

*Recommendation:* The Department should ensure the federal award number is communicated to subrecipients of ARRA funds.

*Agency Response:* Effective March 2011, the Department has placed the ARRA award number on the monthly financial status report and the award number and CFDA number will be added to the Cash Disbursement Code Sheet and transmitted to the subrecipients in the Notification of Funds transfer e-mail.

Anticipated Completion Date: March 31, 2011.

## AUDIT FINDINGS AND RESPONSES (CONTINUED)

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### COMMUNITY DEVELOPMENT BLOCK GRANT (CDBG) – STATE-ADMINISTERED SMALL CITIES PROGRAM CLUSTER – CFDA 14.228 AND 14.255

#### 5. SUBRECIPIENT MONITORING NEEDS IMPROVEMENT

For projects funded by the Community Development Block Grant, the Department of Commerce did not establish adequate monitoring procedures to ensure that the subrecipients were in compliance with all federal requirements. As a result, there is an increased risk that noncompliance with federal requirements could occur at the subrecipient level and not be detected by the Department.

During our review of the Department's on-site monitoring procedures and inspection documentation, we noted the following deficiencies:

- The Department's procedures do not include monitoring their subrecipients' activities to ensure that the subrecipients are not entering into transactions with suspended or debarred entities. Although the Department obtains a certification from the subrecipients stating they are not contracting with or making sub-awards to suspended or debarred parties, the Department does not have effective procedures in place to ensure the subrecipients have evidence to support this certification.
- The Department's procedures do not include monitoring the subrecipients for compliance with the requirements associated with equipment purchased with federal funds. As a result, the Department did not ensure that subrecipients maintained proper equipment records, safeguarded the equipment, and properly maintained and disposed of the equipment.

The Department uses a monitoring tool to help ensure all federal compliance requirements are covered. However, the monitoring tool prepared and used by the Department did not include provisions to monitor subrecipients for the suspension and debarment or equipment compliance requirements.

The *OMB Circular A-133 Compliance Supplement* states that subrecipients should be monitored to provide reasonable assurance that the subrecipient administers federal awards in compliance with laws, regulations, and the provisions of contracts or grant agreements.

*Federal Award Information:* This finding affects CFDA 14.228 Community Development Block Grant award B-10-DC-37-0001 awarded January 1, 2010; award B-09-DC-37-0001 awarded January 1, 2009; award B-08-DC-37-0001 awarded January 1, 2008; and award B-07-DC-37-0001 awarded January 1, 2007.

*Recommendation:* The Department should strengthen internal controls to ensure all applicable federal compliance requirements are included in their subrecipient monitoring procedures.

## AUDIT FINDINGS AND RESPONSES (CONTINUED)

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*Agency Response:* Suspension/debarment requirements are included in the Grant Agreements (contracts) with division subrecipients. Additionally, division staff conducts on-site monitoring of the contracts. There were no instances where subrecipients entered into transactions with suspended or debarred entities. The division has implemented the Auditor's recommendation to include additional provisions on the monitoring tool related to suspension and debarment.

Requirements regarding equipment purchases using Federal funds are included in the Grant Agreement (contract) and in 4 NCAC 19 L. There were no instances found where regulations covering equipment purchases were violated; and the division has incorporated the Auditor's recommendation to enhance the monitoring checklist related to equipment compliance.

Anticipated Completion Date: May 1, 2011.

### 6. DEFICIENCIES IN FEDERAL REPORTING

For the Community Development Block Grant, the Department of Commerce did not implement effective internal control procedures to ensure compliance with the federal reporting requirements described in the *OMB Circular A-133 Compliance Supplement*. As a result, there is an increased risk that reports submitted to the federal agency could be misstated.

During our test of the federal reports for the Community Development Block Grant (CDBG) and the National Stabilization Program (NSP), we noted the following deficiencies:

- The 2009 CDBG Annual Performance Report, *Section 3 Summary Report*, was not submitted to the U.S. Department of Housing and Urban Development (HUD) by March 31, 2010 in accordance with federal requirements. It is the Department's procedure to submit this annual report in November, which according to HUD is an outdated reporting requirement. The Department has not updated their procedures to comply with changes in the federal reporting requirements that have been in place for over a year.
- While testing documentation supporting the annual *Section 3 Summary Report*, we reviewed a sample of 28 subrecipient Annual Performance Reports and found that six did not agree to the information contained in the 2008 *Minority Business Enterprise Report* submitted to HUD. As a result, not all activity was included in the annual report that was submitted to HUD. Internal controls were not effectively implemented to ensure that the information collected from the subrecipients was accurately documented by the Division of Community Assistance in the Division's subsystem (i.e. in the Grants Management System (GMS)). For the six errors in our test, the data submitted by the subrecipients were reviewed by Division staff for reasonableness; however it was not accurately entered into GMS. Therefore, the annual report to HUD, which is generated directly from GMS, was incorrect.

## AUDIT FINDINGS AND RESPONSES (CONTINUED)

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- The reconciliation control that was designed to ensure the completeness and accuracy of the *NSP Quarterly Performance Report* was not consistently performed. The reconciliation was not performed for the fourth quarter *NSP Quarterly Performance Report* until after the auditor inquired about the procedure. Without the execution of proper control procedures, there is an increased risk that inaccurate data could be accumulated and not detected prior to submitting the report to HUD.

The *OMB Circular A-133 Compliance Supplement* requires recipients of federal awards to have controls in place to ensure compliance with the following reporting requirements: reports for federal awards are required to include all activity of the reporting period, be supported by applicable records, and be fairly presented in accordance with program requirements.

*Federal Award Information:* This finding affects the following:

- CFDA 14.228 Community Development Block Grant award B-09-DC-37-0001 awarded January 1, 2009; award B-08-DC-37-0001 awarded January 1, 2008; award B-07-DC-37-0001 awarded January 1, 2007; award B-06-DC-37-0001 awarded January 1, 2006; award B-05-DJ-37-0001 awarded May 25, 2005; award B-05-DC-37-0001 awarded January 1, 2005; award B-04-DC-37-0001 awarded January 1, 2004; award B-03-MC-37-0001 awarded January 1, 2003; award B-02-DC-37-0001 awarded January 1, 2002; award B-01-DC-37-0001 awarded January 1, 2001; award B-00-DC-37-0001 awarded January 1, 2000; and
- CFDA 14.228 National Stabilization Program award B-08-DN-37-0001 for the award period March 9, 2009 - March 9, 2013.

*Recommendation:* The Department should strengthen internal controls to ensure reports are prepared in accordance with federal reporting requirements.

*Agency Response:* 13 of 14 sections of the 2009 Annual Performance Report were submitted to U.S. HUD by the March 31, 2010 deadline as required. The Section 3 Report has since been completed and submitted. All previous and subsequent NSP Quarterly Performance Reports were reconciled. Due to office relocation during this time period, the reconciliation occurred after submission. As of this date, the NSP (Fourth) Quarterly Performance Report has been reconciled and will be corrected in the subsequent quarterly submission per recommendation by U.S. HUD staff. The division staff is in the process of developing internal control procedures to ensure timely and accurate reporting as required for both reports.

Anticipated Completion Date: July 1, 2011.



## AUDIT FINDINGS AND RESPONSES (CONTINUED)

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### WORKFORCE INVESTMENT ACT OF 1998 (WIA) CLUSTER - CFDA 17.258, 17.259 AND 17.260

#### 7. DEFICIENCIES IN FEDERAL REPORTING

For the Workforce Investment Act (WIA) Cluster, the Department of Commerce (Department) did not have effective internal controls to ensure compliance with federal reporting requirements. As a result, there is an increased risk that federal reports could contain errors and not be detected and corrected timely by the Department.

During our test of the WIA Annual Performance Report (ETA-9091), we noted the following deficiencies that indicate the Department's controls were not adequate to ensure that the report was supported by the applicable records or included all activity of the period:

- The annual report is created from a subsystem that was designed to track individual participant data needed to verify compliance with the federal requirements. Participant data are entered by the subrecipients and certain data are monitored by the Department. However, we noted that the Department's monitoring procedures were not designed to ensure that all the data elements needed for the federal reports were in the subsystem.
- After the annual report is submitted, the federal agency requires the Department to agree a sample of data in the annual report to information in the participants' files that reside at the subrecipients. There are numerous data items for each participant and the items vary by participant and program. We examined a sample of documents from the Department's verification procedures and found that, based on the Department's documents, the data submitted in the Annual Performance Report did not agree to the participants' files. We identified one to nine inaccurate data items per participant for 33 of the 40 participants that we examined. As a result, we concluded that the annual report was not properly supported.
- The Department is required to report the results of their participant data verification to the federal awarding agency in the WIA Summary/Analytical Report. We compared this summary report to supporting documents for 40 participants and noted four instances where the WIA Summary/Analytical Report did not match the support. Although the Department had procedures in place to review this summary report, we found this review was not completed in time to ensure that all errors noted by the Department are corrected prior to submitting the report.

The Department's controls were not adequate to ensure that the Monthly Youth Served with WIA Recovery Act Resources Reports (ETA-9149) were prepared in accordance with all federal requirements. A computer program was used to extract data from a subsystem to create the monthly reports. However, neither the program source code nor other support was maintained and the Department was not able to produce the detail to support the reports for our audit. Also, while controls over the accuracy of data in the

## AUDIT FINDINGS AND RESPONSES (CONTINUED)

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supporting subsystem may have been adequate, internal control to ensure data were properly extracted and summarized in the reports was lacking.

In addition, there was no evidence to support that the Quarterly WIA Financial Reports (ETA-9130) were prepared in accordance with all federal requirements. We were unable to test the reports because the Department did not maintain the support nor were they able to reproduce the support.

The *OMB Circular A-133 Compliance Supplement* states that recipients of federal awards are expected to have controls in place to ensure that reports for federal awards include all activity of the reporting period, are supported by applicable accounting or performance records, and are fairly presented in accordance with program requirements.

*Federal Award Information:* This finding affects the following:

- CFDA 17.259 WIA Youth Activities award AA-16040-07-55-A-37 for the award period April 1, 2007 - June 30, 2010, award AA-17133-08-55-A-37 for the award period April 1, 2008 - June 30, 2011, award AA-18653-09-55-A-37 for the award period April 1, 2009 - June 30, 2012, and award AA-20205-10-55-A-37 for the award period April 1, 2010 - June 30, 2013.
- CFDA 17.258 WIA Adult Program and CFDA 17.260 WIA Dislocated Workers award AA-16040-07-55-A-37 for the award period July 1, 2007 - June 30, 2010, award AA-17133-08-55-A-37 for the award period July 1, 2008 - June 30, 2011, and award AA-18653-09-55-A-37 for the award period July 1, 2009 - June 30, 2012.
- CFDA 17.258 ARRA WIA Adult Program, CFDA 17.259 ARRA WIA Youth Activities, and CFDA 17.260 ARRA WIA Dislocated Workers award AA-17133-08-55-A-37 for the award period February 17, 2009 - June 30, 2011.

*Recommendation:* The Department should strengthen internal controls to ensure reports are prepared in accordance with federal requirements, including maintaining supporting details for the reports. Also, copies of program code should be maintained to ensure that results can be reproduced if needed.

*Agency Response:* As indicated in the findings, the annual report (ETA-9091) was designed to track individual participant data to verify compliance with federal requirements and that monitoring procedures were not designed to ensure that all data elements needed for the federal reports were in the subsystem. The Division has made changes to the sampling report used by monitoring staff to increase the numbers of records reviewed. The number of records reviewed is based on current enrollment and now can be up to 35%.

Anticipated Completion Date: March 4, 2011

The Division acknowledges that error rates in the validation of participant information are higher than acceptable. Clarifying policy guidance, training and technical assistance

## AUDIT FINDINGS AND RESPONSES (CONTINUED)

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has been, and will continue to be provided to all sub recipients in order to reduce the error rate.

Anticipated Completion Date: The provision of local technical assistance and training is an ongoing effort.

In the next data validation review (October 2011 into January 2012), the Division will establish a procedure to ensure that there is an additional review, comparing all of the worksheet results to the data entered in the DRVS software. This will be prior to the submission of the data validation report to the U.S. Department of Labor.

Anticipated Completion Date: February 3, 2012

The ETA-9149 report lists the total number of youth participants served during the most recent month. The programs that create this report have been changed to allow it to run against previous months' data. The source code is now captured as part of the monthly copy so that it will reference the program that was used to create a specific months report. Two additional programs have been created that will create detail snapshots of all data used in the summary reports, and will be kept to support the report. The step-by-step processes for all reports will be fully documented, and cross-training will be provided to create a check-and-balance to ensure that more than one person is able to generate the reports.

Anticipated Completion Date: February 1, 2012

A procedure has been implemented requiring that at the time of 9130 preparation screen prints of FMIS system data are maintained in the files. Also included are related reconciliation worksheets and signed copies of the 9130 reports.

Anticipated Completion Date: December 31, 2010

### 8. FAILURE TO COMPLY WITH FEDERAL SUSPENSION AND DEBARMENT REQUIREMENTS

The Department of Commerce did not ensure that subrecipients funded by the Workforce Investment Act (WIA) Cluster were not suspended or debarred at the time of the annual award. The failure to comply with these requirements increases the risk that the Department may contract with suspended or debarred parties.

For the fiscal year ending June 30, 2010, the Department disbursed \$113.5 million of federal WIA funds to 24 local Workforce Development Boards (local areas), but did not verify that these local areas were not suspended or debarred. Instead, the Department has been relying on suspension and debarment certifications that were signed by the local areas in 2003. Although the original grant award was in 2003, a local area's receipt of subsequent awards is not automatic. Each year, the local areas must submit an updated plan to the State before being awarded additional WIA funds, but the Department has not required annual suspension and debarment certifications.

## AUDIT FINDINGS AND RESPONSES (CONTINUED)

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Based on our tests, we did not identify any subrecipients that were suspended or debarred.

The *OMB Circular A-133 Compliance Supplement* requires a non-federal entity that makes a subaward to an entity at a lower tier to verify that the subrecipient is not suspended or debarred or otherwise excluded.

*Federal Award Information:* This finding affects the following:

- CFDA 17.259 WIA Youth Activities award AA-16040-07-55-A-37 for the award period April 1, 2007 - June 30, 2010, award AA-17133-08-55-A-37 for the award period April 1, 2008 - June 30, 2011, award AA-18653-09-55-A-37 for the award period April 1, 2009 - June 30, 2012, and award AA-20205-10-55-A-37 for the award period April 1, 2010 - June 30, 2013.
- CFDA 17.258 WIA Adult Program and CFDA 17.260 WIA Dislocated Workers award AA-16040-07-55-A-37 for the award period July 1, 2007 - June 30, 2010, award AA-17133-08-55-A-37 for the award period July 1, 2008 - June 30, 2011, and award AA-18653-09-55-A-37 for the award period July 1, 2009 - June 30, 2012.
- CFDA 17.258 ARRA WIA Adult Program, CFDA 17.259 ARRA WIA Youth Activities, and CFDA 17.260 ARRA WIA Dislocated Workers award AA-17133-08-55-A-37 for the award period February 17, 2009 - June 30, 2011.

*Recommendation:* The Department should strengthen internal controls to ensure compliance with the federal suspension and debarment requirements.

*Agency Response:* Sub recipients will be required on an annual basis to submit a signed Suspension and Debarment Certification form. The division has implemented the Auditor's recommendation to include additional provisions on the monitoring tool related to suspension and debarment.

Anticipated Completion Date: June 30, 2011

### 9. FAILURE TO COMMUNICATE ARRA FEDERAL AWARD INFORMATION TO SUBRECIPIENTS

The Department of Commerce did not communicate at the time of award and disbursement all the required American Recovery and Reinvestment Act (ARRA) federal award information to subrecipients of the Workforce Investment Act (WIA) Cluster. As a result, the Department did not comply with federal requirements specific to ARRA funds. This increases the risk that subrecipients will not properly account for ARRA funds or identify the ARRA awards and expenditures in their Schedule of Expenditures of Federal Awards and Data Collection Form.

The Department provided the amount of ARRA funds at the time of the award; however, the federal award number and Catalog of Federal Domestic Assistance (CFDA) number

## AUDIT FINDINGS AND RESPONSES (CONTINUED)

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were not provided. In addition, the Department did not provide the federal award number, CFDA number, or the amount of ARRA funds at the time of disbursement.

The *OMB Circular A-133 Compliance Supplement* requires the State to separately identify to each subrecipient, and document at the time of the subaward and disbursement of funds, the federal award number, CFDA number, and the amount of ARRA funds. It also requires subrecipients to separately account for ARRA funds and separately identify the funds in their Schedule of Expenditures of Federal Awards and Data Collection Form.

*Federal Award Information:* CFDA 17.258 ARRA WIA Adult Program, CFDA 17.259 ARRA WIA Youth Activities, and CFDA 17.260 ARRA WIA Dislocated Workers award AA-17133-08-55-A-37 for the award period February 17, 2009 - June 30, 2011.

*Recommendation:* The Department should ensure all applicable federal award information is communicated to subrecipients of ARRA funds.

*Agency Response:* Documents to subrecipients that communicate funding information at time of award will include CFDA numbers, federal grant award number, and an ARRA identification number. Also, CFDA numbers, federal grant award numbers, and the amount will be added to the Cash Disbursement Code Sheet transmitted to the subrecipients in the Notification of Funds transfer e-mail.

Anticipated Completion Date: June 30, 2011.

### 10. SUBRECIPIENT MONITORING NEEDS IMPROVEMENT

The Department of Commerce did not adequately monitor subrecipients of the Workforce Investment Act (WIA) Cluster for compliance with all applicable federal requirements. As a result, there is an increased risk that noncompliance with federal requirements could occur at the subrecipient level and not be detected by the Department.

During our review of the Department's monitoring procedures, we identified the following deficiencies:

- The Department did not adequately monitor WIA subrecipients funded by American Recovery and Reinvestment Act (ARRA) to ensure they were registered in the Central Contractor Registration (CCR), and the Department did not perform periodic reviews to ensure that subrecipients were updating this information. We reviewed the CCR database for five local Workforce Development Boards (local areas) and found that one had a CCR registration that expired on January 16, 2010. We also found that two of the five local areas were not listed in the CCR database. The Department claimed these local areas were registered but not publicly listed. Additional evidence to validate their registration was requested but not provided because the Department stated that it had only inquired of the local areas to ensure they were registered.
- The Department did not adequately monitor subrecipients of the WIA Youth Activities grant to ensure compliance with the earmarking requirement, which

## AUDIT FINDINGS AND RESPONSES (CONTINUED)

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states that at least 95% of eligible participants in youth activities must meet the criteria of disadvantaged low-income youth. During the fiscal year, one of the Department's three field representatives did not monitor for this requirement, thus 33% of the subrecipients were not monitored for earmarking compliance. As a result, there is an increased risk that the percentage of the disadvantaged low-income youth served by a subrecipient could fall below the required threshold and not be detected by the Department.

The *OMB Circular A-133 Compliance Supplement* states that a pass-through entity is responsible for identifying to first-tier subrecipients the requirement to register in the Central Contractor Registration, including obtaining a Dun and Bradstreet Data Universal Numbering System (DUNS) number, and for maintaining the currency of that information. In addition, the OMB guidance and Title 20 CFR section 667.400(c) requires each recipient and subrecipient to conduct regular compliance oversight and monitoring of its WIA activities and those of its subrecipients and contractors and to provide them technical assistance as necessary and appropriate.

*Federal Award Information:* This finding affects the following:

- CFDA 17.259 WIA Youth Activities award AA-16040-07-55-A-37 for the award period April 1, 2007 - June 30, 2010, award AA-17133-08-55-A-37 for the award period April 1, 2008 - June 30, 2011, award AA-18653-09-55-A-37 for the award period April 1, 2009 - June 30, 2012, and award AA-20205-10-55-A-37 for the award period April 1, 2010 - June 30, 2013.
- CFDA 17.258 ARRA WIA Adult Program, CFDA 17.259 ARRA WIA Youth Activities, and CFDA 17.260 ARRA WIA Dislocated Workers award AA-17133-08-55-A-37 for the award period February 17, 2009 - June 30, 2011.

*Recommendation:* The Department should strengthen internal controls to ensure all applicable federal compliance requirements are included in their subrecipient monitoring procedures.

*Agency Response:* All sub recipients will be required to submit information that documents their registration in the CCR database, as well as their active status. A schedule of CCR active status expiration dates will be maintained and subrecipients will be reminded to re-enroll prior to the expiration date of the active status.

Anticipated Completion Date: April 30, 2011.

Each of the field representatives will receive additional training and technical assistance related to the oversight of the 5% earmarking requirement. Additionally, reports from the state's Workforce Investment Act participant tracking database will be enhanced to allow improved oversight of this requirement.

Anticipated Completion Date: April 30, 2011

## AUDIT FINDINGS AND RESPONSES (CONTINUED)

### WIA CLUSTER (CFDA 17.258, 17.259 AND 17.260), WEATHERIZATION ASSISTANCE FOR LOW-INCOME PERSONS (CFDA 81.042), AND CDBG (CFDA 14.228 AND 14.255)

#### 11. ERRORS NOTED IN THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS (SEFA)

The Department of Commerce did not prepare the Schedule of Expenditures of Federal Awards (SEFA) in accordance with guidelines prescribed by OMB Circular A-133. Errors in the SEFA reduce the usefulness of the report.

OMB Circular A-133 requires the reporting of all actual expenditures for the year by federal program and separate identification of ARRA funds. During our review of the Department's SEFA, we noted the following deficiencies:

- a. The expenditure amounts reported on the SEFA for the Workforce Investment Act (WIA) Cluster were not supported by the expenditures reported in the accounting records and were not properly reported on a cash basis in accordance with state policy. The Department misstated the total federal awards expended and the total amount provided to subrecipients of the WIA Cluster. We found that the total federal awards expended were misstated by \$7.2 million and the total amount provided to subrecipients were misstated by \$7.6 million as follows:
  - For the WIA Adult Programs, the federal awards expended from ARRA were understated by \$2 million and overstated by \$1.3 million for the regular grant. For the amounts provided to subrecipients, the ARRA grant was understated by \$1.9 million and the regular grant was overstated by \$992,000.
  - For the WIA Youth Activities, the federal awards expended from ARRA were understated by \$933,000 and overstated by \$1.2 million for the regular grant. For the amounts provided to subrecipients, the ARRA grant was understated by \$809,700 and the regular grant was overstated by \$128,500.
  - For the WIA Dislocated Workers, the federal awards expended from ARRA were overstated by \$4 million and overstated by \$2.1 million for the regular grant. For the amounts provided to subrecipients, the ARRA grant was overstated by \$4.2 million and the regular grant was overstated by \$3.4 million;
  - In addition, the ARRA Health Coverage Tax Credit (HCTC) grant was classified as part as the Workforce Investment Act Cluster in CFDA 17.260 for ARRA WIA Dislocated Workers, thus overstating the federal awards expended and amounts provided to subrecipients from this grant by an additional \$1.6 million. The HCTC expenditures should be classified under CFDA 17.276 as ARRA.
- b. The amount reported on the SEFA for the Community Development Block Grant (CDBG) program was not supported by the accounting records. The total federal awards expended were understated by \$1.4 million.

## AUDIT FINDINGS AND RESPONSES (CONTINUED)

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- c. The amounts reported on the SEFA for the ARRA Weatherization Assistance grant and the regular Weatherization Assistance grant were not supported by the accounting records. The total federal awards expended for the ARRA Weatherization Assistance grant were overstated by \$615,585. The total federal awards expended for the regular Weatherization Assistance grant were understated by \$1,000. The amount provided to subrecipients for the regular Weatherization Assistance grant was understated by \$135,680.
- d. In addition, the accounting subsystem for WIA was used to prepare the SEFA for its applicable grants. This subsystem did not reconcile to the North Carolina Accounting System (NCAS) by a net value of \$4.9 million. The Department was unable to identify and resolve the discrepancies, thus increasing the risk of errors reported on the SEFA.

It is essential that effective internal control over the preparation of the SEFA be established to provide reasonable assurance that expenditures are accurate and presented in accordance with federal guidelines.

*Federal Award Information:* This finding affects the following:

- a. CFDA 17.259 WIA Youth Activities award AA-16040-07-55-A-37 for the award period April 1, 2007 - June 30, 2010, award AA-17133-08-55-A-37 for the award period April 1, 2008 - June 30, 2011, award AA-18653-09-55-A-37 for the award period April 1, 2009 - June 30, 2012, and award AA-20205-10-55-A-37 for the award period April 1, 2010 - June 30, 2013.
- b. CFDA 17.258 WIA Adult Program and CFDA 17.260 WIA Dislocated Workers award AA-16040-07-55-A-37 for the award period July 1, 2007 - June 30, 2010, award AA-17133-08-55-A-37 for the award period July 1, 2008 - June 30, 2011, and award AA-18653-09-55-A-37 for the award period July 1, 2009 - June 30, 2012.
- c. CFDA 17.258 ARRA WIA Adult Program, CFDA 17.259 ARRA WIA Youth Activities, and CFDA 17.260 ARRA WIA Dislocated Workers award AA-17133-08-55-A-37 for the award period February 17, 2009 - June 30, 2011.
- d. CFDA 14.228 Community Development Block Grant award B-10-DC-37-0001 awarded January 1, 2010, award B-09-DC-37-0001 awarded January 1, 2009, award B-08-DC-37-0001 awarded January 1, 2008, and award B-07-DC-37-0001 awarded January 1, 2007.
- e. CFDA 81.042 Weatherization Assistance for Low-Income Persons award DE-FG26-07NT43134 for the award period July 1, 2007 - June 30, 2010, and ARRA award DE-EE0000118 for the award period April 1, 2009 - March 31, 2012.

*Recommendation:* The Department should strengthen internal controls over the preparation of the Schedule of Expenditures of Federal Awards to ensure federal expenditures are reported in accordance with federal guidelines.



## **AUDIT FINDINGS AND RESPONSES (CONCLUDED)**

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*Agency Response:*

- a. Procedures and controls will be installed so that the numbers reported will match financial records. The Access database that interfaces FMIS with the Cash Draw process and subsequently to NCAS had a programming issue that has been repaired. The reconciliation of FMIS and NCAS will be completed at year-end before preparation of the SEFA. CFDA numbers will be checked prior to submission of the SEFA.
- b. As stated in the finding the amount for the total awards expended did not match the accounting records. This error resulted from the accidental omission of the administrative expenses for the CDBG program. To ensure the accurate reporting of this and other numbers reported on the SEFA, Commerce will add an addition review once the values have been computed prior to the submission of the SEFA to the Office of State Controller.
- c. As stated in the finding, the amount for the ARRA Weatherization Assistance grant, and regular Weatherization Assistance grant were not supported by the accounting records. The overstatement of \$615,585 out of the total program budget of \$ 131,954,536.00 resulted from total non-salary item line value being entered on the SEFA rather than the expenditures line. The \$1,000.00 error reported for regular Weatherization was caused by a typo. To ensure the accurate reporting of this and other numbers reported on the SEFA, Commerce will add an addition review once the values have been computed prior to the submission of the SEFA to the Office of State Controller.
- d. FMIS will be reconciled with NCAS at year end before preparation of the SEFA report.

Anticipated Completion Date: August 30, 2011.

## **ORDERING INFORMATION**

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