

STATE OF NORTH CAROLINA

OFFICE OF THE STATE AUDITOR

BETH A. WOOD, CPA



DEPARTMENT OF PUBLIC INSTRUCTION

RALEIGH, NORTH CAROLINA

STATEWIDE FEDERAL COMPLIANCE AUDIT PROCEDURES

FOR THE YEAR ENDED JUNE 30, 2016



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STATE OF NORTH CAROLINA
Office of the State Auditor



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AUDITOR'S TRANSMITTAL

The Honorable Roy Cooper, Governor
Members of the North Carolina General Assembly
State Board of Education
Mr. Mark Johnson, State Superintendent
Department of Public Instruction

As part of our audit of the State of North Carolina's compliance with requirements applicable to its major federal programs, we have completed certain audit procedures at the Department of Public Instruction for the year ended June 30, 2016. We conducted our audit in accordance with the auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Governmental Auditing Standards*, issued by the Comptroller General of the United States; and the audit requirements of Title 2 U.S. *Code of Federal Regulations* Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance). Our audit was performed by authority of Article 5A of Chapter 147 of the *North Carolina General Statutes*.

Our audit objective was to render an opinion on the State of North Carolina's major federal programs 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 State Auditor expresses an opinion on the State's compliance with requirements applicable to its major federal programs in the State's *Single Audit Report*.

The audit finding in this 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



Beth A. Wood, CPA
State Auditor

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INDEPENDENT AUDITOR'S REPORT

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**INDEPENDENT AUDITOR'S 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 THE UNIFORM GUIDANCE**

Mr. William Cobey, Chairman, State Board of Education
and Management of the Department of Public Instruction

Report on Compliance

As part of our audit of the State of North Carolina's compliance with the types of requirements described in the *OMB Compliance Supplement* that could have a direct and material effect on each of its major programs for the year ended June 30, 2016, we have performed audit procedures at the Department of Public Instruction. 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 Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) is included in the State's *Single Audit Report*. Our federal compliance audit scope at the Department of Public Instruction included the following:

- CFDA 84.010: Title I Grants to Local Education Agencies
- CFDA 84.048: Career and Technical Education – Basic Grants to States
- CFDA 84.367: Improving Teacher Quality State Grants
- CFDA 84.395: State Fiscal Stabilization Fund (SFSF)-Race-to-the-Top Incentive Grants, Recovery Act
- Special Education Cluster
 - CFDA 84.027: Special Education – Grants to States
 - CFDA 84.173: Special Education – Preschool Grants

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.

Management's Responsibility

Management is responsible for compliance with federal statutes, regulation, and the terms and conditions of its federal awards applicable to its federal programs.

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for each of the State of North Carolina's major federal programs based on our audit of the types of compliance requirements referred to above, which we issue in the State's *Single Audit Report*. 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 the audit requirements of Title 2 U.S. *Code of Federal Regulations* Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance). Those standards and the Uniform Guidance 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. However, our audit does not provide a legal determination of the Department's compliance with those requirements.

Opinion on Each Major Federal Program

As stated above, our opinion on compliance for each of the State of North Carolina's major federal programs is included in the State's *Single Audit Report*.

Other Matters

The results of our audit procedures at the Department of Public Instruction disclosed an instance of noncompliance that is required to be reported in accordance with the Uniform Guidance and which is described in the finding in the Findings, Recommendations, and Responses section of this report.

Report on Internal Control Over Compliance

Management is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered internal control over compliance with the types of requirements that could have a direct and material effect on a major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major federal program and to test and report on internal control over compliance in accordance with the Uniform Guidance, 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 material weaknesses or significant deficiencies, and therefore, material weaknesses or significant deficiencies may exist that were not identified. However, we consider the deficiency described in the finding in the Findings, Recommendations, and Responses section of this report to be a material weakness in internal control over compliance.

Department of Public Instruction's Response to the Finding

The Department's response to the finding identified in our audit is included in the Findings, Recommendations, and Responses section of this report. The Department's response was not subjected to the auditing procedures applied in the audit of compliance, and accordingly, we express no opinion on the response.

Purpose of Report on Internal Control Over Compliance

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of the Uniform Guidance. Accordingly, this report is not suitable for any other purpose.



Beth A. Wood, CPA
State Auditor

Raleigh, North Carolina

March 16, 2017



FINDINGS, RECOMMENDATIONS, AND RESPONSES

Matters Related to Federal Compliance Objectives

The following audit finding was identified during the current audit and describes conditions that represent a deficiency in internal control or noncompliance with laws, regulations, contract, grant agreements, or other matters.

FISCAL MONITORING RESULTS WERE DELIVERED LATE

The Department did not report the results of its fiscal monitoring¹ visits to subrecipients within 60 business days after leaving the audit site, preventing subrecipients from taking timely corrective action.

The Department monitors subrecipients on a rotational basis. During fiscal year 2016, the Department monitored 38 subrecipients who spent \$182 million of the \$809 million in total federal funds that subrecipients spent.

A review of supporting documentation determined that 21 out of 38 (55%) fiscal monitoring reports were communicated between 61 and 170 days after the end date of the monitoring visit.

As a result, subrecipient corrective action was delayed, which allowed noncompliance with federal program regulations to continue. Examples of noncompliance noted in monitoring reports included:

- Procedures not in place to ensure contracts and service agreements are on file to support all expenditures for contracted services.
- Procedures not in place to ensure employee time and effort documentation is complete and accurate.
- Procedures not properly designed to ensure federal funds are spent within three days or returned to the Department.

The Division of School Business management was not reviewing the onsite monitoring log effectively to identify delays between the site visit completion dates and issuing the monitoring results. Additionally, a temporary delegation of duties resulted in the circumvention of the review control. Consequently, no follow-up actions were taken to discover why the reports were not being finalized for review and communicated to subrecipients within 60 days of completing the site visit.

The Department's Division of School Business policies and procedures manual requires communication of fiscal monitoring results within 60 business days.

Significant aspects of this finding were reported in the 2015 Statewide Single Audit as findings numbers 2015-026, 2015-028, 2015-032, 2015-049 and 2015-058.

Federal Award Information:

CFDA 84.027: Special Education – Grants to States

¹ Fiscal monitoring includes reviewing subrecipients' expenditures to ensure federal funds are used for allowable costs in accordance with approved budgets and program guidelines.

Award Number: H027A150092A
Federal Funding Period: July 1, 2015 – September 30, 2016

CFDA 84.173: Special Education – Preschool Grants

Award Number: H173A140096
Federal Funding Period: July 1, 2014 – September 30, 2015

Award Number: H173A140096
Federal Funding Period: July 1, 2015 – September 30, 2016

CFDA 84.010: Title I – Grants to LEAs

Award Number: S010A140033A
Federal Funding Period: July 1 2014 – September 30, 2015

Award Number: S010A150033A
Federal Funding Period: July 1 2015 – September 30, 2016

CFDA 84.367: Improving Teacher Quality State Grants

Award Number: S367A140032A
Federal Funding Period: July 1, 2014 – September 30, 2015

Award Number: S367A150032A
Federal Funding Period: July 1, 2015 – September 30, 2016

CFDA 84.048: Career and Technical Education

Award Number: V048A150033-12A
Federal Funding Period: July 1, 2015 – September 30, 2016

Recommendation: Division management should effectively review the onsite monitoring log and ensure all fiscal monitoring results are finalized for communication within 60 business days of completing the onsite visit. Division management’s delegation of duties should be designed to prevent the circumvention of controls, even in temporary situations.

Agency Response: The Department concurs with the Auditor’s finding related to fiscal monitoring results being communicated late. The audit finding is the result of a former management level employee’s intentional circumvention of existing internal controls related to the fiscal monitoring process. The employee in question had direct supervisory responsibility for oversight of the fiscal monitoring process and staff. Division management reviewed the fiscal monitoring tracking log on a regular basis as established by internal procedures; however, date-related information entered into the log was intentionally deceptive. As soon as management became aware of the potential circumvention of existing internal controls related to the fiscal monitoring process, an internal investigation was conducted and documented. The employee in question is no longer employed by the Department.

Ongoing oversight activities by section and division management, as well as clarification of roles and responsibilities of fiscal monitoring staff, regular status update meetings and the hiring of a new Section Chief should prevent recurrence of the finding. The Assistant Director of School Business, in conjunction with the Director, will continue to monitor the fiscal monitoring process to improve the efficiency and effectiveness of existing controls.

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For additional information contact:
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This audit was conducted in 3,113 hours at an approximate cost of \$320,639.