

North Carolina Department of Commerce

Raleigh, North Carolina

Statewide Federal Compliance Audit Procedures

For the Year Ended June 30, 2023

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A Department of the
State of North Carolina



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Chapter 147, Article 5A of the North Carolina General Statutes gives the Auditor broad powers to examine all books, records, files, papers, documents, and financial affairs of every state agency and any organization that receives public funding. The Auditor also has the power to summon people to produce records and to answer questions under oath.



North Carolina Office of the State Auditor

Jessica N. Holmes, J.D., State Auditor

Auditor's Transmittal

The Honorable Roy Cooper, Governor
The General Assembly of North Carolina
Machelle B. Sanders, Secretary
North Carolina Department of Commerce

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 federal programs, we have completed certain audit procedures at the North Carolina Department of Commerce (Department) for the year ended June 30, 2023.

We conducted our audit of federal compliance in accordance with the 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). Our audit objective was to express an opinion on the State of North Carolina's compliance for each of its major federal programs. However, 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. The State Auditor expresses an opinion on the State of North Carolina's compliance with requirements applicable to its major federal programs in the State's *Single Audit Report*.

Our federal compliance audit scope at the Department included the following:

- Community Development Block Grant/State's Program and Non-Entitlement Grants in Hawaii (ALN 14.228)
- Workforce Innovation and Opportunity Act (WIOA) Cluster (ALN 17.258, 17.259, 17.278)
- Coronavirus State and Local Fiscal Recovery Funds (ALN 21.027)
- State Small Business Credit Initiative Technical Assistance Grant Program (ALN 21.031)

Our audit was performed by authority of Chapter 147, Article 5A of the North Carolina General Statutes.

Compliance

The results of our audit procedures at the North Carolina Department of Commerce disclosed instances of noncompliance that are required to be reported in accordance with the Uniform Guidance and which are described in findings 1 and 4 in the Findings, Recommendations, and Views of Responsible Officials of the Auditee section.

Internal Control Over Compliance

In planning and performing our audit of federal compliance, we considered the Department's 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 the Department's internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the Department's 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 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. Therefore, material weaknesses may exist that have not been identified. However, as discussed in the Findings, Recommendations, and Views of Responsible Officials of the Auditee section, we did identify certain deficiencies in internal control over compliance that we consider to be material weaknesses and significant deficiencies. The deficiencies described in findings 1 and 4 are considered to be material weaknesses in internal control over compliance. Furthermore, the deficiencies described in findings 2 and 3 are considered to be significant deficiencies in internal control over compliance.

North Carolina Department of Commerce's Response to Findings

The Department's responses to the findings identified in our audit are included in the Findings, Recommendations, and Views of Responsible Officials of the Auditee section of this transmittal. The Department's responses were not subjected to the auditing procedures applied in the audit of compliance, and accordingly, we express no opinion on the responses.

Purpose of This Transmittal

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

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 transmittal.



Jessica N. Holmes, J.D.
State Auditor

Raleigh, North Carolina

March 18, 2024



Findings, Recommendations, and Views of Responsible Officials of the Auditee

Matters Related to Federal Compliance Audit Objectives

ALN 14.228 - Community Development Block Grant/State's Program and Non-Entitlement Grants in Hawaii

1. Inadequate Monitoring of Subaward Expenditures

The Department of Commerce (Department) did not adequately monitor \$19.6 million in federal funds used to support community development activities. Specifically, the Department did not:

- Perform risk assessments.
- Complete monitoring activities.
- Adequately review reimbursement requests.

Auditors reviewed the Department's monitoring plan over subaward expenditures. The Department's monitoring plan required risk assessments over all subawards when funding is initially provided and then again after 20 months to determine which subawards to monitor. However, auditors reviewed the 50 subawards that required a risk assessment during the audit and found that none of the risk assessments were performed.

In addition, auditors reviewed the monitoring activities over all subawards open during the audit period. The Department's monitoring plan included various monitoring activities, such as on-site monitoring or desk reviews. Auditors reviewed the monitoring activities over all 152 open subawards and found that 148 (97%) subawards did not have monitoring activities completed during the year.

Lastly, auditors reviewed a sample of 60 reimbursement requests, totaling \$5.1 million, that were paid during the audit period and found eight (13%) requests totaling \$426,260 that were paid outside the subaward period.

As a result, the Department may be required to pay \$426,260 back to the federal government. Furthermore, inadequate monitoring increases the risk that federal funds may not be used in accordance with federal requirements, which may reduce funding available to communities for providing housing and expanding economic opportunities for low- and moderate-income families.

According to the Department management, reviews of the reimbursement requests were not detailed enough to ensure that payments were within the subaward period. In addition, staff turnover resulted in incomplete monitoring procedures.

Federal regulations¹ require the Department to:

- Establish and maintain effective internal control over the federal award that provides reasonable assurance that the entity is managing the award in compliance with federal statutes, regulations, and the terms and conditions of the federal award.

¹ 2 CFR 200.303(a) and 2 CFR 200.332(b),(d).

Findings, Recommendations, and Views of Responsible Officials of the Auditee

- Evaluate each subrecipient's risk of noncompliance with federal statutes, regulations, and the terms and conditions of the subaward to determine the appropriate subrecipient monitoring.
- Monitor the activities of the subrecipient as necessary to ensure that the subaward is used for authorized purposes, in compliance with federal statutes, regulations, and the terms and conditions of the subaward.

Federal Award Information: U.S. Department of Housing and Urban Development; Assistance Listing Numbers (titles): 14.228 (Community Development Block Grants/State's Program and Non-Entitlement Grants in Hawaii); Federal Award Identification Number(s) (award period(s)): B-15-DC-37-0001 (August 20, 2015 - September 1, 2022), B-16-DC-37-0001 (July 22, 2016 - September 1, 2023), B-17-DC-37-0001 (September 22, 2017 - September 1, 2024), B-18-DC-37-0001 (December 20, 2018 - September 1, 2025), B-19-DC-37-0001 (August 27, 2019 - September 1, 2026), B-20-DC-37-0001 (September 2, 2020 - September 1, 2027), B-20-DW-37-0001 (July 8, 2020 - July 8, 2026), B-21-DC-37-0001 (January 1, 2021 - September 1, 2028).

Recommendation: Department management should develop and implement detailed review procedures over expenditures to ensure they are within the subaward period.

In addition, Department management should establish contingency plans to ensure monitoring procedures are completed during times of employee turnover.

Views of Responsible Officials of the Auditee: The Department of Commerce, Rural Economic Development Division (REDD) recognizes its responsibility to adequately monitor subrecipient expenditures. Also, REDD CDBG staff consistently strives to adhere to federal requirements and ensure funding is available to communities to provide housing and expand economic opportunities for low- and moderate-income families.

Performance of Risk Assessments

The OSA finding notes that REDD's CDBG staff did not perform risk assessments. REDD CDBG staff assesses risk and performs monitoring at multiple points. To determine risk, an assessment is included at three critical points: (1) in the project selection process, (2) prior to the release of programmatic funds, and (3) the ongoing weekly monitoring of expenditure rates to address slow drawdown of funds.

REDD CDBG staff acknowledges and agrees that the finding notes the omission of the formal risk assessment at the second and third points noted above. The risk assessment is an ongoing process throughout the grant life and steps were modified to expedite funding during the public health emergency due to COVID-19. The monitoring plan, however, due to this unprecedented time was not updated to reflect the changes.

As a corrective action, REDD CDBG staff will modify the monitoring plan and risk assessment process to account for these extenuating situations. This will be completed by June 30, 2024 with an effective date of July 1, 2024.

Monitoring of Sub-Awardee Activities

The OSA report states that 148 of 152 sub-awardees were not monitored for allowable costs during Fiscal Year 2023. REDD CDBG agrees with the finding.

REDD CDBG current policy permits grantees to submit requisitions for payment without supporting documentation in most instances. The staff reviews allowable expenditures during desk reviews and on-site monitoring. When concerns arise, staff also request documentation to determine whether expenditures are appropriate.

As a corrective action, REDD CDBG staff will review current practices, revise where needed, and update the monitoring plan to reflect changes by June 30, 2024 and effective July 1, 2024.

Review of Sub-Awardee Requisition Requests

OSA auditors reviewed a sample of 60 reimbursement requests, totaling \$5.1 million, that were paid during the audit period and found eight (13%) requests totaling \$426,260 that were paid outside the subaward period.

The REDD CDBG staff acknowledges and agrees with the OSA finding. The identified subawards will be reviewed and actions will be taken to extend the grant period to ensure program compliance or recapture the funds for non-compliance from sub-awardees. Should the Department have to repay funds, the federal government will require a repayment using State funds. REDD CDBG staff will make every effort to prevent this situation.

CDBG REDD management has developed and implemented procedures to ensure that sub-awardee's requisitions are paid within the subaward grant period and corrective action will be taken for the ones identified by OSA by June 30, 2024.

2. Inaccurate Annual Reporting

The Department of Commerce (Department) did not accurately report Community Development Block Grant (CDBG) program data to the U.S. Department of Housing and Urban Development.

Auditors reviewed the obligation, expenditure, and program performance data² reported in the annual Financial Summary Report³ and found that amounts reported did not agree to the Department's accounting records. Specifically, auditors found differences in the following reported amounts:

- Obligated amounts ranged from an underreported amount of \$4.2 million to an overreported amount of \$7.5 million.

² Program performance data represents the expenditures used on activities that benefit low- and moderate-income families, for the prevention of slum and blight, and to meet urgent community development needs.

³ The annual Financial Summary Report includes cumulative reporting of obligated amounts, expenditure amounts, and program performance data for each open CDBG allocation. During the period, the report included award years 2002 through 2021.

- Expenditure amounts ranged from an underreported amount of \$8.3 million to an overreported amount of \$6.1 million.
- Program performance data ranged from an underreported amount of \$8.6 million to an overreported amount of \$13.1 million.

Inaccurate reporting of CDBG program data prevents the U.S. Department of Housing and Urban Development from monitoring the state's progress in helping communities provide housing and expand economic opportunities for low- and moderate-income families. In addition, citizens do not have complete and accurate information to provide feedback on how funds are being used in their communities.

According to Department management, the Financial Summary Report was prepared using amounts from the U.S. Department of Housing and Urban Development's reporting system, and the amounts were not reconciled to the Department's records to ensure accuracy.

Federal regulations⁴ require that the Department submit an annual report concerning the use of CDBG funds, known as the Consolidated Annual Performance and Evaluation Report (CAPER). The Financial Summary Report is a supplement to the CAPER.

Federal regulations⁵ also require the Department to establish and maintain effective internal control over federal awards that provide reasonable assurance that the Department is managing the program in compliance with federal statutes, regulations, and the terms and conditions of the federal award. The federal regulations define internal control to include the processes for achieving reliable reporting.

Federal Award Information: U.S. Department of Housing and Urban Development; Assistance Listing Numbers (titles): 14.228 (Community Development Block Grants/State's Program and Non-Entitlement Grants in Hawaii); Federal Award Identification Number(s) (award period(s)): B-15-DC-37-0001 (August 20, 2015 – September 1, 2022), B-16-DC-37-0001 (July 22, 2016 - September 1, 2023), B-17-DC-37-0001 (September 22, 2017 - September 1, 2024), B-18-DC-37-0001 (December 20, 2018 - September 1, 2025), B-19-DC-37-0001 (August 27, 2019 - September 1, 2026), B-20-DC-37-0001 (September 2, 2020 - September 1, 2027), B-21-DC-37-0001 (January 1, 2021 - September 1, 2028).

Recommendation: Department management should develop and implement detailed reconciliation and review procedures over the annual Financial Summary Report to ensure accuracy.

Views of Responsible Officials of the Auditee: The Department of Commerce, Rural Economic Development Division (REDD) acknowledges that there is currently not a process in place that reconciles the data in Commerce's Grants Management System (GMS) to the data in the federal Integrated Disbursement and Information System (IDIS). REDD acknowledges its responsibility to provide accurate and timely reconciled data for the annual financial reports required by the US Department of Housing and Urban Development (HUD). Due to outdated functionality of the aged (over 25 years old) internal database (GMS) CDBG staff has a tremendous challenge to reconcile the data to the federal system, IDIS. GMS has very limited configurability to conduct adequate automated financial reconciliation processes

⁴ 24 CFR 91.520.

⁵ 2 CFR 200.303 - Internal Controls.

and perform grant deliverables throughout the grant lifecycle for annual federal funding allocations.

Expenditure amounts ranged from an underreported amount of \$8.3 million to an overreported amount of \$6.1 million.

REDD CDBG staff acknowledges and agrees with the OSA. In February of 2021, the REDD CDBG leadership team was notified that a US Treasury bulletin whose requirements had not been enforced previously, would be beginning with the 2014 allocation. At the recommendation of HUD Small Cities Office, staff utilized a methodology of de-obligating newer grant awards and substituting these for older funds in our line of credit. These changes were tracked manually using Excel workbooks and reconciled monthly. This information was not attached to the PR28 report but has been maintained by REDD CDBG.

Obligated amounts ranged from an underreported amount of \$4.2 million to an overreported amount of \$7.5 million.

REDD CDBG staff acknowledges and agrees with this finding.

Program performance data ranged from an underreported amount of \$8.6 million to an overreported amount of \$13.1 million.

REDD CDBG staff acknowledges and agrees with the OSA.

Correction Action Plan: By October 1, 2024, REDD CDBG staff will work with Commerce Information Technology staff to explore and implement interim solutions until a replacement of the current Grants Management System (GMS) is available.

3. Errors in FFATA Reporting

The Department of Commerce (Department) did not submit complete, accurate, and timely subaward information for subrecipients of the Community Development Block Grant (CDBG) program to the Federal Funding Accountability and Transparency Act (FFATA) Subaward Reporting System (FSRS).

Auditors reviewed all 39 subawards totaling \$50.4 million that were required to be reported to the FSRS during the audit period and found the following errors:

- 34 subawards totaling \$49.1 million were reported 29 to 180 days late. In addition, one subaward totaling \$5.0 million was reported with the incorrect subaward number.
- Four subawards totaling \$1.3 million were not reported at all.
- One subaward totaling \$950,000 was reported although the subaward was canceled prior to report submission.

The FFATA was enacted to help reduce wasteful spending in government by empowering every American citizen with the ability to hold the government accountable for each spending decision. When subaward information is not reported to the FSRS, citizens do not have complete and accurate information about how federal funds are being used in their communities.

According to Department management, the required FFATA reporting for the CDBG program was not completed because staff responsible for FFATA reporting misunderstood the applicability of the requirement to CDBG subaward allocations.

The FFATA⁶ requires direct recipients of grants or cooperative agreements to report first-tier subawards of \$30,000 or more to the FSRS no later than the end of the month following the month in which the obligation was made.

Federal Award Information: Federal Awarding Agency: U.S. Department of Housing and Urban Development; Assistance Listing Numbers (titles): 14.228 (Community Development Block Grants/State's Program and Non-Entitlement Grants in Hawaii); Federal Award Identification Number(s) (award period(s)): B-15-DC-37-0001 (August 20, 2015 - September 1, 2022), B-18-DC-37-0001 (December 20, 2018 - September 1, 2025), B-21-DC-37-0001 (January 1, 2021 - September 1, 2028), B-22-DC-37-0001 (January 1, 2022 - September 1, 2029).

Recommendation: Department management should ensure that the staff responsible for FFATA reporting have a clear understanding of the reporting requirements applicable to the CDBG program.

Views of Responsible Officials of the Auditee: The Department of Commerce, Rural Economic Development Division (REDD) recognizes its responsibility to comply with the Federal Funding Accountability and Transparency Act (FFATA) requirements.

Pursuant to the requirements of the Federal Funding Accountability and Transparency Act (Pub. L. No. 109-282), as amended by Section 6202 of Pub. L. No. 110-252, hereafter referred as the "Transparency Act" that are codified in 2 CFR Part 170, all required Community Development Block Grant subawards have been put into the Federal Subaward Reporting System (FSRS). Based on the reporting requirements outlined in the "Transparency Act", all future awards will be put into FSRS by the end of the month following the month of the fully executed subaward agreement. To ensure data entry accuracy, all subaward information put into FSRS will have two review and concurrence cycles before final submission.

To provide timely and accurate information within the system, if a sub-awardee de-obligates or receives additional grant funds, updates to the information previously entered in the system will be updated to reflect any increase or decrease in the subaward. If a new subaward is made from de-obligated funding, the report will be updated with the information of the sub-awardee within the allotted timeframe specified in the reporting requirements. Prior to submission, these changes will also be required to have two review and concurrence cycles before final submission.

⁶ 2 CFR 170 Appendix A.

ALN 17.258, 17.259, 17.278 - Workforce Innovation and Opportunity Act Cluster

4. Inadequate Subrecipient Monitoring

The Department of Commerce (Department) did not adequately monitor \$58 million in federal funds passed to subrecipients to provide employment and training programs for adults, dislocated workers, and youth who face barriers to employment.

Auditors reviewed the monitoring procedures over all 22 subrecipients that received Workforce Innovation and Opportunity Act (WIOA) Cluster funds during the audit period. The Department's monitoring procedures required annual, onsite financial and programmatic monitoring for all subrecipients. However, auditors found no evidence that monitoring was completed as required.

Additionally, auditors reviewed the monitoring procedures for all 22 subrecipients that were required to have an audit in accordance with Uniform Guidance and found that the Department did not obtain or review the audit reports for 17 subrecipients (77%).

Inadequate monitoring increases the risk that federal funds may not be used in accordance with federal requirements, which may reduce funding available to provide services to individuals seeking employment and training assistance.

According to Department management, employee turnover in positions responsible for overseeing the monitoring process prevented the completion of monitoring during the year.

Federal regulations⁷ require the Department to:

- Perform annual onsite monitoring of all subrecipients to ensure that the subaward is used for authorized purposes in compliance with federal statutes, regulations, and the terms and conditions of the subaward; and that subaward performance goals are achieved.
- Verify that every subrecipient is audited as required.

Federal Award Information: Federal Awarding Agency: U.S. Department of Labor; Assistance Listing Numbers (titles): 17.258 (WIOA Adult Program), 17.259 (WIOA Youth Activities), 17.278 (WIOA Dislocated Worker Formula Grants); Federal Award Identification Number(s) (award period(s)): AA-38547-22-55-A-37 (April 1, 2022 - June 30, 2025), AA-36337-21-55-A-37 (April 1, 2021 - June 30, 2024), AA-34786-20-55-A-37 (April 1, 2020 - June 30, 2023), AA-33241-19-55-A-37 (April 1, 2019 - June 30, 2022).

Recommendation: The Department should prioritize the development of a contingency plan to ensure annual monitoring is completed when employee turnover occurs

Views of Responsible Officials of the Auditee: The Department of Commerce, Division of Workforce Solutions (DWS) understands its responsibility to monitor subrecipients annually in a timely manner and acknowledges that it is catching up on monitoring local workforce development boards after being delayed due to a combination of the operational disruptions

⁷ 200 CFR 200.332(d)-(f) and 20 CFR 683.410(b).

of the COVID-19 pandemic, restructuring of the monitoring unit due to staff vacancies, and an identified need to create new internal training and updated procedures before resuming monitoring. DWS has historically completed monitoring timely, prior to March 2020, the start of the COVID-19 pandemic.

Since the end of the audit period, DWS has issued 13 programmatic or financial monitoring reports for the period of the audit - State Fiscal Year (SFY) 2023 that corresponds to WIOA Program Year (PY) 2022 (July 1, 2022 - June 30, 2023). In the last year, DWS programmatic and financial monitors have conducted concurrent onsite reviews of three program years, substantially catching up on monitoring activities and has a plan in place to complete the period of the audit and the subsequent SFY 2024/WIOA PY 2023 monitoring activities by December 31, 2024.

DWS is submitting with this response a Corrective Action Plan to ensure that local areas' compliance with the Uniform Guidance is monitored on an annual basis, as well as a Monitoring Plan that includes a contingency plan to ensure annual monitoring is completed when employee turnover occurs. DWS estimates that all monitoring activities for the period of the year of the audit, as well as the following year, will be complete by December 31, 2024. DWS will be on schedule for monitoring activities going forward effective January 1, 2025.

Ordering Information

Copies of this report may be obtained by contacting:

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919-807-7666



This audit required 2,495 hours at an approximate cost of \$339,320.