



STATE OF NORTH CAROLINA

NORTH CAROLINA STATE BOARD OF ELECTIONS FISCAL CONTROL AUDIT

OFFICE OF THE STATE AUDITOR

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NORTH CAROLINA STATE BOARD OF ELECTIONS

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AUDITOR'S TRANSMITTAL

October 12, 2011

The Honorable Beverly Eaves Perdue, Governor
The General Assembly of North Carolina
Mr. Gary Bartlett, Executive Director
North Carolina State Board of Elections

This report presents the results of our fiscal control audit at the North Carolina State Board of Elections. Our work was performed by authority of Article 5A of Chapter 147 of the *North Carolina General Statutes* and was conducted in accordance with the performance audit standards contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. The objective of a fiscal control audit is to identify improvements needed in internal control over selected fiscal matters, such as financial accounting and reporting; compliance with finance-related laws, regulations, and provisions of contracts or grant agreements; and/or management of financial resources.

The results of our audit disclosed deficiencies in internal control and/or instances of noncompliance or other matters that are considered reportable under *Government Auditing Standards*. These items are described in the Audit Findings and Responses section of this report.

North Carolina General Statutes require the State Auditor to make audit reports available to the public. Copies of audit reports issued by the Office of the State Auditor may be obtained through one of the options listed in the back of this report.

A handwritten signature in cursive script that reads "Beth A. Wood".

Beth A. Wood, CPA
State Auditor

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OBJECTIVES, SCOPE, METHODOLOGY, AND RESULTS

OBJECTIVES, SCOPE, AND METHODOLOGY

As authorized by Article 5A of Chapter 147 of the *North Carolina General Statutes*, we have conducted a fiscal control audit at the North Carolina State Board of Elections. There were no special circumstances that caused us to conduct the audit, but rather it was performed as part of our effort to periodically examine and report on the financial practices of state agencies and institutions.

The objective of a fiscal control audit is to identify improvements needed in internal control over selected fiscal matters, such as financial accounting and reporting; compliance with finance-related laws, regulations, and provisions of contracts or grant agreements; and/or management of financial resources. Our audit does not provide a basis for rendering an opinion on internal control, and consequently, we have not issued such an opinion.

Management is responsible for establishing and maintaining effective internal control. Internal control is a process designed to provide reasonable assurance that relevant objectives are achieved. Because of inherent limitations in internal control, errors or fraud may nevertheless occur and not be detected. Also, projections of any evaluation of internal control to future periods are subject to the risk that conditions may change or compliance with policies and procedures may deteriorate.

To accomplish our audit objectives, we gained an understanding of internal control over matters described below and evaluated the design of the internal control. We then performed further audit procedures consisting of tests of control effectiveness and/or substantive procedures that may reveal significant deficiencies in internal control. Specifically, we performed procedures such as interviewing personnel, observing operations, reviewing policies, analyzing accounting records, and examining documentation supporting recorded transactions and balances. Whenever sampling was used, we applied a nonstatistical approach but chose sample sizes comparable to those that would have been determined statistically. As a result, we were able to project our results to the population but not quantify the sampling risk.

As a basis for evaluating internal control, we applied the internal control guidance contained in *Internal Control Integrated Framework*, published by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). As discussed in the framework, internal control consists of five interrelated components, which are (1) control environment, (2) risk assessment, (3) control activities, (4) information and communication, and (5) monitoring.

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions

OBJECTIVES, SCOPE, METHODOLOGY, AND RESULTS (CONTINUED)

based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Our audit scope covered the period July 1, 2010 through December 31, 2010 and included selected internal controls in the following organizational units:

State Board of Elections Administration Division

This Division is responsible for the day-to-day operations and the representation of the financial statements of the Board. Additionally, the administration division provides all accounting information to the Department of Administration who performs the accounting function for the Board.

State Board of Elections Campaign Finance Division

This Division is responsible for compliance with laws and regulations regarding campaign finance reporting by individual candidates, candidate campaign committees and political party campaign organizations at the local and state level. In addition, the campaign finance division administers the North Carolina Public Campaign Financing Fund and the North Carolina Political Parties Financing Fund.

During our audit, we considered internal control related to the following accounts and control objectives:

Fees, Licenses, and Fines - This classification includes candidate filing fees, forfeitures of unallowable campaign contributions, fines and penalties for delinquent campaign finance reports and registration fees for county board staff training. We examined internal control designed to ensure that the Board properly assesses and accounts for these revenues, which included recognizing the accrued receivable at year-end. We also examined evidence to support compliance with related laws and regulations over these revenues. These laws and regulations establish the amount of fees, timing of fee assessments and action to be taken regarding delinquent and noncompliant campaign finance reporting. As of December 31, 2010, the Board reported fees, licenses and penalties of \$524,956 in the general fund.

Tax Distributions In - This classification includes receipts from the Department of Revenue based on individual tax return designations for contributions to the North Carolina Public Campaign Financing Fund and North Carolina Political Parties Financing Fund. We examined internal control designed to ensure the Board properly receipts and accounts for these revenues, which included recognizing the accrued receivable at year-end. We also examined evidence to support compliance with related laws and regulations over these revenue receipts. These laws and regulations set guidelines for the timing and amount of distributions to public candidates and political parties. As of December 31, 2010, the Board reported tax distributions in of \$777,045 in the special revenue fund.

OBJECTIVES, SCOPE, METHODOLOGY, AND RESULTS (CONCLUDED)

Noncapital Gifts - This classification includes receipts collected from the State Bar Association for a surcharge on attorney license renewals to be used to provide contributions to qualified candidates and to produce and distribute the voter guide in connection with the statewide judicial elections. We examined internal control designed to ensure the Board properly receipts and accounts for these revenues, which included recognizing the accrued receivable at year-end. We also examined evidence to support compliance with related laws and regulations over the allowable use of these revenues. As of December 31, 2010, the Board reported noncapital gifts of \$675,632 in the special revenue fund.

Grants, State Aid and Subsidies - This classification includes expenditures for the distributions in the special revenue fund to public candidates and statewide political parties. We examined internal control designed to ensure the Board properly distributes and accounts for these expenditures. We also examined evidence to support compliance with related laws and regulations over these distributions. These laws and regulations include guidelines on the timing and limitation of distributions and the qualification of candidates and political parties. As of December 31, 2010, the Board reported total distributions of \$819,066 which included \$214,613 to public candidates and \$604,453 to statewide political parties.

Other Services - This classification within the special revenue fund includes expenditures for the cost of printing, binding and distributing the voter guide for the statewide judicial election. We examined internal control designed to ensure the Board properly uses and accounts for these expenditures. We also examined evidence to support compliance with related laws and regulations over these expenditures. These laws and regulations include guidelines for the selection of a vendor to produce and distribute the voter guide. As of December 31, 2010, the Board reported printing and postage expenditures of \$1,023,761.

RESULTS

The results of our audit disclosed deficiencies in internal control and/or instances of noncompliance or other matters that are considered reportable under generally accepted government auditing standards. These items are described in the Audit Findings and Responses section of this report.

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AUDIT FINDINGS AND RESPONSES

1. FORFEITURES, FINES AND PENALTIES NOT TRANSFERRED TO THE CIVIL PENALTY AND FORFEITURE FUND

The State Board of Elections did not transfer forfeitures, fines, and penalties to the Civil Penalty and Forfeiture Fund at the Office of State Budget and Management (OSBM) as required by *North Carolina General Statute*. During the 2010 fiscal year the Board collected \$199,160 in forfeitures of anonymous contributions or contributions that were unlawfully collected by campaign or political committees, fines, and penalties. These funds were transferred to the Office of State Controller in July 2010 and were deposited in the State's general fund instead of being transferred to OSBM. No transfers had been made for the forfeitures, fines, and penalties collected during the 2011 fiscal year. At December 2010 this balance totaled \$452,665.

North Carolina General Statute 115C-457.2 requires the Board to transfer the forfeitures, fines, and penalties collected to the Civil Penalty and Forfeiture Fund within 10 days after the close of the calendar month in which the revenues were received or collected.

Recommendation: The Board should implement procedures to ensure that forfeitures, fines, and penalties collected are properly and timely transferred to the Civil Penalty and Forfeiture Fund at the Office of State Budget and Management.

Agency Response: \$493,130.16 of forfeitures, fines and penalties were transferred to Office of State Budget and Management at the end of FY 2010-2011. Without a dedicated staff person with governmental accounting background, the State Board has relied on the expertise of Department of Administration and prior to that, the Office of State Controller. Both agencies provided valuable service without a great deal of input from Board staff. In order to ensure this does not occur in the future, the Board will submit a monthly request to DOA Fiscal Management of amounts collected to transfer Civil Penalty and Forfeiture funds to the Office of State Budget and Management within 10 days after the close of the calendar month.

2. DEFICIENCIES IN RECORDING ACCOUNTS RECEIVABLE

The State Board of Elections did not properly record its accounts receivable. Therefore, management and other users of the Board's accounting information did not have available the correct amount owed to the Board. Specific misstatements noted in our audit included the following:

- No entry was made to record a receivable for the monies collected by the Department of Revenue for the quarter ended June 2010 for the North Carolina Political Parties Fund. This amount totaled \$519,525.

AUDIT FINDINGS AND RESPONSES (CONTINUED)

- The accounts receivable for the North Carolina Public Campaign Financing Fund, representing monies collected by the Department of Revenue by taxpayer designation and from the North Carolina Bar license renewal surcharge, was overstated by \$169,456 due to using amounts from the wrong months to prepare the financial statements.
- No entry was made for the \$220,432 in outstanding forfeitures, fines, and penalties levied by the Board. Of this outstanding amount, \$92,600 was under appeal by the affected parties dating back to January 2009, making it doubtful that this amount would be collected. This would have resulted in a net receivable understatement of \$127,832.

These misstatements resulted in accounts receivable being understated by a total of \$477,901.

Recommendation: The State Board of Elections should place greater emphasis on the year-end financial reporting process and strengthen internal controls to ensure the accuracy and completeness of the financial statements.

Agency Response: The State Board of Elections has strengthened internal controls and reviews to ensure accuracy and completeness of the financial statements.

3. NONCOMPLIANCE WITH CAMPAIGN FINANCE REPORTING REQUIREMENTS

The State Board of Elections did not comply with requirements regarding assessing and collecting penalties, accepting and adjudicating appeals, or terminating and reactivating campaign status when campaign reports are delinquent. The noncompliance results in untimely collection of penalties and in some cases, penalties were not assessed at all.

Title 08 Section 1.0104(d) of the North Carolina Administrative Code requires termination notices to be sent to committees that do not file their campaign reports within 20 days of the issuance of the “Notice of Noncompliance” and only reactivate the committees’ status after reports are filed and penalties satisfied. Additionally, *North Carolina General Statute* 163-278.34(e) requires penalties to be paid or appealed within 30 days and if not, the account is to be turned over to the State Attorney General’s office for collection.

During our review of the Board’s compliance with handling delinquent campaign reports, we noted several areas of noncompliance as follows:

- Five of the 48 committees that were sent a termination letter between July 1, 2010 and March 8, 2011 were returned to active status on the Board’s website once the reports were filed without satisfying the penalties. As of March 8, 2011, three of the five had not been assessed penalties and two were returned to active status prior to the payment or appeal of penalties.

AUDIT FINDINGS AND RESPONSES (CONTINUED)

- Tests of the 106 committees assessed a penalty during the audit period revealed that 36 had not paid or appealed the penalty within 30 days and had not been turned over to the Attorney General's office for collection. There was \$11,550 in uncollected penalties related to these 36 assessments as of December 2010. The Board's position is to make multiple attempts to collect the penalties and only involve the Attorney General after two years since they have three years to file civil action.
- Based on our review of the Board minutes, appeals have not been heard since December 11, 2008. Of the 106 penalties assessed during the audit period, 53 were appealed with a total balance of \$48,450.

Recommendation: The Board should enhance procedures to ensure compliance with statutory requirements regarding the handling of delinquent or noncompliant campaign finance reporting. The Board should take steps to adjudicate the backlog of appeals and handle future appeals timely. Additionally, efforts should be made to review the statutory requirements to evaluate and consider the need for technical revisions.

Agency Response: The Board will enhance procedures to ensure compliance with statutory requirements regarding the handling of delinquent or noncompliant campaign finance reporting and will take steps to adjudicate the backlog of appeals and handle future appeals timely.

4. CAMPAIGN FINANCE REPORT AUDITS NOT PERFORMED TIMELY

The State Board of Elections did not perform the required audits of campaign finance reports within the time stated in State law. *North Carolina General Statutes* 163-278.23 and .24 requires that campaign finance reports be reviewed within 30 days of receipt and audited within four months of the election for conformance with law and truthfulness. If reports are not audited timely, the likelihood of collecting forfeitures and penalties assessed decreases.

At the time of our audit there were over 30,000 reports that had not been audited. Some of these unaudited reports date back to the 2000 election. The receipts and expenditures for approximately 10,000 of those reports had not been entered in the campaign finance database, which is necessary before an audit can be performed since many of the audit procedures are performed electronically.

For the 2010 election cycle, 10,931 campaign finance reports were filed. At the completion of our audit, 6,578 of the 10,931 reports still had not been entered in the database and therefore had not been audited within the timeframe required.

The Board does perform cursory reviews of campaign reports when they are received and placed on the public web site. Electronically filed reports are subjected to various computer based edit and consistency checks when received. Manual reports are scanned into the system within days of receipt and are visually checked by the Board's staff.

AUDIT FINDINGS AND RESPONSES (CONCLUDED)

Recommendation: The Board should implement procedures to ensure information contained in the manual reports is entered in the campaign finance database and all campaign reports are audited timely in accordance with statute. Efforts should be made to obtain the necessary resources to eliminate the data entry and audit backlog and if considered necessary, seek further guidance from legislature on the intention and purpose of the statute as it relates to the extent and timing of audits to be performed.

Agency Response: Since implementation of the Campaign Finance Reporting Article 40 years ago, the four month audit requirement has never been accomplished. There is a cursory review of each report received by the Board whether by electronic, in person or mail delivery with a more formal audit done later.

Until electronic filing is mandated and Campaign Finance receives additional resources, this deadline will always be a challenge. We will continue to seek the General Assembly's review of the statutes for any practical changes or amendments to the Campaign Reporting Act.

ORDERING INFORMATION

Audit reports issued by the Office of the State Auditor can be obtained from the web site at www.ncauditor.net. Also, parties may register on the web site to receive automatic email notification whenever reports of interest are issued. Otherwise, copies of audit reports may be obtained by contacting the:

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