



STATE OF NORTH CAROLINA

GOLDEN LONG-TERM ECONOMIC ADVANCEMENT FOUNDATION (GOLDEN LEAF FOUNDATION)

FINANCIAL RELATED AUDIT

AUGUST 2012

OFFICE OF THE STATE AUDITOR

BETH A. WOOD, CPA

STATE AUDITOR

**GOLDEN LONG-TERM ECONOMIC ADVANCEMENT FOUNDATION
(GOLDEN LEAF FOUNDATION)**

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BOARD OF DIRECTORS

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State Auditor

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AUDITOR'S TRANSMITTAL

August 27, 2012

The Honorable Beverly Eaves Perdue, Governor
The General Assembly of North Carolina
Board of Directors, Golden LEAF
Dan Gerlach, President

This report presents the results of our financial related audit at the Golden Long-term Economic Advancement Foundation (Golden LEAF Foundation). 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 results of our audit disclosed a deficiency in internal control that is considered reportable under *Government Auditing Standards*. This matter is 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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BACKGROUND

As authorized by Article 5A of Chapter 147 of the *North Carolina General Statutes*, we have conducted a financial related audit at the Golden Long-term Economic Advancement Foundation (Golden LEAF Foundation). 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 organizations within the State of North Carolina reporting entity.

In 1999, the North Carolina legislature created a nonprofit organization, commonly referred to as the Golden LEAF Foundation, to receive and distribute 50 percent of the State's share of a legal settlement with cigarette manufacturers. The purpose of the Golden LEAF Foundation (the Foundation) is to promote the social welfare and lessen the burdens of government by receiving and distributing funds to provide economic impact assistance to economically affected or tobacco-dependent regions of North Carolina. The Foundation awards grants to nonprofit and governmental entities across North Carolina to support activities that include:

- a. Educational assistance for tobacco farmers and other workers affected or projected to be affected by a decline in production of tobacco products.
- b. Job training and employment assistance for tobacco farmers and other workers dependent on tobacco farming, production, and sales to transition to other sources of income.
- c. Scientific research to develop new uses for tobacco or for the development of alternative cash crops.
- d. Economic hardship assistance experienced by tobacco farmers, quota owners, their families and others as a result of decline in quota and/or production of tobacco or tobacco products.
- e. Public works and industrial recruitment to local governments for upgrading utilities, transportation, and other public service infrastructure to attract new businesses or for more general economic development purposes.
- f. Health and human services to improve health care and other social services needed to maintain the stability of tobacco-dependent communities.
- g. Community assistance in the form of grants and/or loans to economically depressed and deteriorating tobacco-dependent communities, to be used exclusively for public purposes.

AUDIT SCOPE AND OBJECTIVES

The general objective of this financial related audit was to identify improvements needed in internal control over selected fiscal matters. 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. Our audit does not provide a basis for rendering an opinion on internal control, and consequently, we have not issued such an opinion.

Our audit scope covered the period July 1, 2011 through December 31, 2011 and included the following transaction types and control objectives:

Investments and Investment Income – The Foundation contracts with an investment consultant and external investment managers to help oversee and manage its investment assets. We examined the Foundation’s procedures for selecting and contracting with external investment managers and monitoring the investment activity for compliance with investment policies and contract guidelines. The investments held by the Foundation include long-term fixed income investments, equity investments, money market funds, certificates of deposit, limited partnerships, real estate, and obligations of government agencies. Investment income includes dividends and interest earned, realized gains and losses from trading of investments, and net unrealized gains and losses from the change in market value. The Foundation reported investment losses of approximately \$45.8 million during our audit period and held approximately \$728.9 million in investments assets at December 31, 2011.

Grant Commitments – The Foundation awards grants to nonprofit and governmental entities across the State. We examined the Foundation’s procedures for reviewing grant applications and ensuring that only those that align with the Foundation’s purpose received awards. In addition, we reviewed the Foundation’s procedures for ensuring that the awarded amount was reasonable and the grant agreement included clear expectations and a method for determining if the grant achieves proposed outcomes. The Foundation reported approximately \$94.7 million in grant commitments at December 31, 2011.

Grant Distributions – This represents the amount of funds paid to grantees. We examined the Foundation’s procedures for grant disbursements and monitoring grantees. This included evaluating if the Foundation’s procedures were sufficient to assess whether the grantee’s costs and activities were in accordance with the grant agreement, whether grants achieved proposed outcomes, whether grantees complied with reporting requirements, and whether grantees corrected noted issues timely. The Foundation reported approximately \$18.6 million of grant distributions during our audit period.

METHODOLOGY

To accomplish our audit objective, we gained an understanding of internal control over matters described in the *Audit Scope and Objectives* section of this report 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 provide evidence about our audit objectives. 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 professional auditing standards. As discussed in the standards, 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 audit in accordance with generally accepted government auditing standards applicable to performance audits. 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 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.

RESULTS AND CONCLUSIONS

The results of our audit disclosed a deficiency in internal control that is considered reportable under generally accepted government auditing standards. This matter is described in the *Audit Findings and Responses* section of this report. Management's response is presented after the audit finding. We did not audit the response, and accordingly, we express no opinion on the response.

AUDIT FINDINGS AND RESPONSES

MONITORING OF GRANTEE ACTIVITIES AND OUTCOMES NEEDS IMPROVEMENT

The Golden LEAF Foundation (the Foundation) can improve its monitoring of grant recipients. The *North Carolina Administrative Code* requires that state-funded grants be monitored for compliance with grant requirements. Monitoring should also include a comparison of actual program results and outcomes to pre-established performance goals. Inadequate monitoring increases the risk of waste and/or misuse of funds.

Review of Reports and Supporting Documentation is Inconsistent

The Foundation's primary monitoring procedure is a review of grantee reports and related supporting documentation, typically submitted every six months (starting six months from the award date). However, we found that sufficient documentation is not always submitted to validate reported uses of funds, and information is often not provided to substantiate the attainment of performance goals.

We examined the Foundation's monitoring documentation for a sample of 47 grant awards, totaling \$20.2 million, that were active during the period of July 1, 2011 through December 31, 2011. Our sample focused on grants from the three major grant types: the Open Grant program, the Economic Catalyst Grant program, and the Community Assistance Initiative grant program. The following deficiencies were identified:

- The Foundation does not consistently obtain support for grant expenditures. Invoices, canceled checks, and detailed payroll data were typically obtained from grantees to support the reported use of funds. However, we noted six instances where the only support provided was summary reports or printouts from the grantee's accounting system.
- The Foundation does not obtain enough information to determine if the grants actually achieve the desired outcomes stated in the grant application. The Foundation requests a summary of the outcomes and results, but specific support for the project's impact, such as new jobs created, worker skills upgraded, or total number served, are often not provided. We noted the Foundation typically receives job creation documentation for Economic Catalyst Grants, but not for Open Grant programs. We identified 16 instances when the detailed support for outcomes was not obtained.
- The grantees do not always submit their reports timely, and the Foundation does not consistently send reminders for past due reports. We noted 16 instances when the grantee did not submit a report timely and there was no evidence the Foundation conducted a follow-up.

On-site Monitoring of Grantees Generally Not Performed

We also noted that site visits are not part of the Foundation's standard monitoring procedures. Although we saw evidence that the Foundation has visited some locations, no standard

AUDIT FINDINGS AND RESPONSES (CONCLUDED)

protocol has been developed for monitors to use when they do visit grantees. A form is available to document an onsite assessment of the grantee's work plan and evaluation plan; however, of those we saw the procedures actually performed and documented for each visit varied.

On-site monitoring is generally considered more effective and efficient than desk reviews of documentation. During a site visit, monitors have the opportunity to interview personnel and observe operations first-hand. Furthermore, monitors could inspect original documentation supporting uses of funds and performance outcomes, which is more reliable and less costly than having grantees copy and mail documentation.

The Foundation has indicated that monitoring visits to all grantees is difficult given the current staffing levels and job duties. The Foundation has seven staff members whose main duties include monitoring active grants. However, these staff members are also responsible for conducting the Foundation's review and evaluation of grant applications, which is generally a rather involved process. In addition, some staff actively work with communities across the State to identify potential community assistance projects. We noted that the Foundation reviewed over 100 grant applications and had over 230 active grants to monitor during our audit period.

We visited three active grantees and examined documentation supporting reported expenditures and performance outcomes. In all cases, the grantee was able to provide support that validated its reports. Our procedures were limited to determining whether documentation supported the reports. We did not attempt to determine whether desired performance outcomes were actually achieved.

Recommendation: The Foundation should develop a comprehensive plan for monitoring grant recipients that includes: (1) assessing grantee risk and adapting monitoring procedures based on the assessment (which may assist with the allocation of staff resources); (2) standardized procedures for grantee reporting and providing support for reports; and (3) standardized procedures for performing site visits when such visits are required. Procedures should be effectively and consistently performed to validate reported uses of funds and attainment of performance outcomes. We believe that site visits generally are more effective and efficient than desk review procedures and should at least be considered for high risk grantees.

Foundation Response: The Foundation agrees with the recommendation. Foundation staff has designed a comprehensive policy for grants management, which incorporates a risk assessment to guide levels of oversight including site visits, and outcome and expense verification. The Foundation Board reviewed and endorsed these changes at its August 2012 Board meeting. The Foundation is in the process of hiring an additional program staff position to help strengthen performance and carry out some of these additional tools for grants oversight, while keeping its administrative budget below the 2007 levels. Many of these changes were in development during and after the audit period but are now being implemented.

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This audit required 1,035 audit hours at an approximate cost of \$74,520 and included site visits to three grantees. The cost represents 0.12% of the \$64,358,982 in total revenues and expenditures subjected to audit.