

STATE OF NORTH CAROLINA

OFFICE OF THE STATE AUDITOR

BETH A. WOOD, CPA

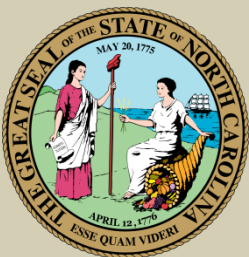


ORANGE COUNTY CLERK OF SUPERIOR COURT

HILLSBOROUGH, NORTH CAROLINA

PERFORMANCE AUDIT

JULY 2022



NCOSA
The Taxpayers' Watchdog

STATE OF NORTH CAROLINA
Office of the State Auditor



Beth A. Wood, CPA
State Auditor

2 S. Salisbury Street
20601 Mail Service Center
Raleigh, NC 27699
Telephone: (919) 807-7500
Fax: (919) 807-7647
www.auditor.nc.gov

AUDITOR'S TRANSMITTAL

The Honorable Roy Cooper, Governor
The General Assembly of North Carolina
The Honorable Mark Kleinschmidt, Orange County Clerk of Superior Court

Ladies and Gentlemen:

We are pleased to submit this performance audit report for the Orange County Clerk of Superior Court. The audit objective was to identify improvements needed in internal control over selected financial matters, as listed on pages 2-3.

This audit was conducted in accordance with Chapter 147, Article 5A of the North Carolina General Statutes.

The results of our audit identified deficiencies in internal control and instances of noncompliance that are considered reportable under *Government Auditing Standards*. These items are described in the FINDINGS, RECOMMENDATIONS, AND RESPONSES section of this report.

We appreciate the courtesy and cooperation received from management and the employees of the Orange County Clerk of Superior Court during our audit.

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 black ink, reading "Beth A. Wood".

Beth A. Wood, CPA
State Auditor

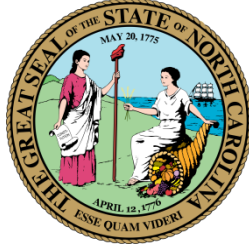


Beth A. Wood, CPA
State Auditor

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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.

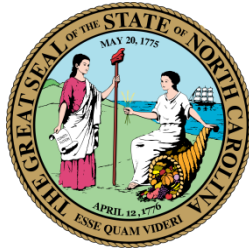


BACKGROUND

We have conducted a performance audit of the Orange County Clerk of Superior Court, as authorized by Chapter 147, Article 5A of the North Carolina General Statutes, which requires the Office of the State Auditor to periodically examine and report on the financial practices of state agencies.

The voters of each county elect a Clerk of Superior Court for a four-year term. Clerks are responsible for all clerical and record-keeping functions of the superior court and district court. The Clerks' offices collect, invest, and distribute assets in a fiduciary capacity. For example, the Clerks' offices collect fines and court costs, hold cash and property bonds, administer estates on behalf of minors, and distribute resources to governmental and private parties as required.

The North Carolina Administrative Office of the Courts (NCAOC) provides statewide support services for the courts, including court programs and management services; information technology; human resources services; financial, legal, and legislative support; and purchasing services. In addition, the NCAOC prepares and administers the court system's budget.



OBJECTIVES, SCOPE, AND METHODOLOGY

The objective of this performance audit was to identify improvements needed in internal control over selected financial 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. Errors or fraud may nevertheless occur and not be detected because of the inherent limitations of internal control. Also, projections of any evaluation of internal control to future periods are subject to the risk that conditions may change or that compliance with policies and procedures may deteriorate.

Our audit scope covered the period July 2021 through February 2022. In conducting our audit, we observed, documented, and evaluated the effectiveness of selected internal controls related to:

- *Cash* – The Clerk’s office collects various fines, fees, and court costs daily, as well as bonds, judgments, and other amounts. We examined internal controls to determine whether such controls were designed and implemented to ensure that the Clerk properly safeguarded and accounted for cash receipts. We also examined internal controls designed to ensure compliance with laws and regulations related to depositing cash receipts. During the audit period, the Clerk collected \$6,742,932 in cash.
- *Estates* – The Clerk’s office is to ensure that all estates are charged an application fee plus an assessment based on the value of each estate’s inventory. An estate inventory is to be filed by the representative of the estate. We examined internal controls to determine whether such controls were designed and implemented to ensure that the Clerk properly obtained an inventory for each estate in compliance with laws and regulations. We also examined internal controls designed to ensure compliance with laws and regulations related to the appropriate assessment and collection of estate fees. During the audit period, the Clerk collected \$238,681 in estate fees related to estates.

The Clerk’s office is to ensure that all estate guardians¹ are properly bonded based on the value of each annual estate inventory. An annual estate inventory is to be filed by the estate guardian of a minor or incapacitated adult. We examined internal controls designed to ensure that the Clerk properly obtained an inventory for each guardianship in compliance with laws and regulations. We also examined internal controls to determine whether such controls were designed and implemented to ensure that bonds assessed and collected were sufficient and in compliance with laws and regulations. During the audit period, auditors examined \$10,794,169 in estate guardian bonds retained by the Clerk related to 65 estates.

- *Escheats* – The Clerk’s office is to transfer abandoned property to the state. The transfer results when the person legally entitled to the property fails to make a valid claim on the property within a prescribed period of time. After that time, all abandoned property held by the Clerk is required to be transferred to the North Carolina Department of State Treasurer. We examined internal controls to determine whether such controls were designed and implemented to ensure that the Clerk properly identified escheatable funds. We also examined internal controls designed to ensure compliance with laws and regulations related to escheating unclaimed funds after a

¹ Guardianship is a legal relationship in which a person(s) or agency (the guardian) is appointed by the court to make decisions and act on behalf of a minor or incapacitated adult.

prescribed period of time. During the audit period, the Clerk transferred \$274,601 in escheats to the Department of State Treasurer.

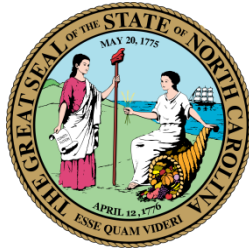
- *Trusts* – The Clerk’s office receives, administers, and disburses trust funds for minors and incapacitated adults. We examined internal controls to determine whether such controls were designed and implemented to ensure that disbursements from minor and incapacitated adult trust accounts were proper to ensure compliance with laws and regulations. During the audit period, the Clerk disbursed \$79,821 from minor and incapacitated adult trust accounts.

To accomplish the audit objective, auditors gained an understanding of the Clerk’s internal control over matters and evaluated the design of internal control. Auditors then performed further audit procedures consisting of tests of control effectiveness and/or substantive procedures that provide evidence about our audit objectives. Specifically, auditors interviewed personnel, observed operations, reviewed policies, analyzed accounting records, and examined documentation supporting recorded transactions and balances, as considered necessary in the circumstances. 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 as applicable but not quantify the sampling risk. This approach was determined to adequately support our audit conclusions.

Because of the test nature and other inherent limitations of an audit, together with limitations of any system of internal and management controls, this audit would not necessarily disclose all deficiencies in internal control or instances of noncompliance.

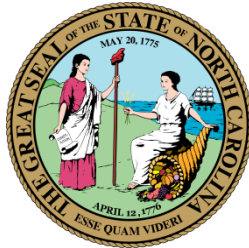
As a basis for evaluating internal control, we applied the internal control guidance contained in professional auditing standards. However, our audit does not provide a basis for rendering an opinion on internal control, and consequently, we have not issued such an opinion. See the Appendix for internal control components and underlying principles that were significant to our audit objectives.

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 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

Based on the results of audit procedures described in the OBJECTIVES, SCOPE, AND METHODOLOGY section of this report, auditors identified deficiencies in internal control and instances of noncompliance that are considered reportable under *Government Auditing Standards*. These items are described in the FINDINGS, RECOMMENDATIONS, AND RESPONSES section of this report. Management's responses are presented after each audit finding. We did not audit the responses, and accordingly, we express no opinion on them.



FINDINGS, RECOMMENDATIONS, AND RESPONSES

1. FAILURE TO COMPEL ESTATE INVENTORY FILINGS OR FEE COLLECTION

The Clerk's office did not compel the filing of estate inventories or collect estate fees in accordance with state law. The Clerk's office collected \$238,681 in estate fees during the audit period of July 2021 through February 2022.

Auditors examined 65 of the 104 estates in the audit period that required an inventory to be filed. For 16 (25%) estates, the inventories were not filed timely and the Clerk failed to issue written requests requiring the inventory filings.

Auditors also examined 65 of the 226 estates in the audit period in which a final inventory was filed. A total of \$457 in fees for four (6%) estates were not accurately assessed or collected when the final inventory was filed. Specifically,

- For three estates, fees were not accurately assessed. This resulted in the Clerk collecting a total of \$442 less than required for the estates.
- For one estate, fees totaling \$15 were not collected when the final inventory was filed and there was no evidence in the file to support subsequent collection efforts. These fees remained uncollected as of the time of our audit.

The Clerk's failure to compel the filing of inventories could allow unauthorized transactions to occur, such as removal of estate assets without the knowledge of qualified heirs. It could also delay the family of the deceased from finalizing the estate. Additionally, there were delays and potential loss in the collection of estate fees.

According to the Clerk, there were two reasons for the errors.

- The Clerk's office prioritized other duties over reviewing inventory reports for filing deadlines due to turnover of staff overseeing the compelling of estates.
- The Clerk's staff made unintentional mistakes in calculating the fees and not collecting the required amounts before finalizing due to a lack of review.

Chapter 28, Article 20 of the North Carolina General Statutes and the *North Carolina Clerk of Superior Court Procedures Manual*, Chapter 74, require the filing of an estate inventory within three months after the Clerk's appointment of the estate's personal representative. If an inventory is not filed, the Clerk must compel the inventory by issuing a written request requiring the personal representative to file the inventory or explain why the personal representative should not be replaced. Additionally, North Carolina General Statute 7A-307(a)(2) requires the Clerk to assess and collect the estate fees at the time the final inventory is filed.

Recommendation: The Clerk should develop contingency plans to ensure estates are compelled to file inventories in the event of personnel shortages.

In addition, the Clerk should implement monitoring procedures such as reviewing fee calculations for accuracy and identifying uncollected fees at the time of the final inventory filings.

Clerk's Response: See page 8 for the Clerk's response to this finding.

2. FAILURE TO COMPEL ESTATE INVENTORY FILINGS OR ASSESS AND COLLECT SUFFICIENT BONDS FOR ESTATES OF MINORS AND INCAPACITATED ADULTS

The Clerk's office did not compel the filing of guardianship estate inventories or assess and collect sufficient² bonds to protect wards (minors or incapacitated adults) in accordance with state law.

Auditors examined 65 of the 88 guardianship estates for wards that required bonds and the filing of an annual inventory of the ward's assets. For 18 (28%) of the guardianship estates examined, the Clerk failed to compel an inventory filing or failed to assess and collect sufficient bonds. Specifically:

- For 13 (20%) of the guardianship estates, annual inventories were not filed and the Clerk failed to issue written requests requiring the inventory filings.
- For five (8%) of the guardianship estates, annual inventories were filed, however, the bonds assessed and collected were insufficient as of the current inventory filing. Assets in these estates totaled \$408,121 and required \$471,564 in bonds. However, the Clerk only assessed and collected \$299,415 in bonds.

Failure to compel the timely filing of inventories prevents the Clerk from assessing and collecting sufficient bonds from guardians and could result in financial loss to the ward if the guardian misuses the assets in the estate. Additionally, the Clerk may be liable³ for the financial loss if bonds are not sufficient.

According to the Clerk, the Clerk's office prioritized other duties over reviewing the inventory reports for filing deadlines due to turnover of staff overseeing the compelling of guardianship estates. Additionally, monitoring procedures were not in place to ensure inventories were compelled and bonds were sufficient for the guardianship estates.

North Carolina General Statutes 35A-1230 and 35A-1231 require the Clerk to assess and collect sufficient bonds before appointing a guardian to the estates of minors and incapacitated adults or permitting guardians from receiving the wards' property. North Carolina General Statutes 35A-1264 and 35A-1265 require the annual filing of an inventory of the ward's personal property. If an annual inventory is not filed, the Clerk must compel the inventory by issuing written requests requiring the guardian to file the inventory.

Recommendation: The Clerk should develop contingency plans to ensure inventory reports are reviewed during periods of staff turnover.

In addition, the Clerk should implement monitoring procedures to ensure guardians are compelled to file inventories when necessary and that the bonds collected remain sufficient.

Clerk's Response: See page 7 for the Clerk's response to this finding.

² North Carolina General Statutes 35A-1230 and 35A-1231 require bonds for estate guardians to equal 125% of the ward's personal property (if less than or equal to \$100,000) or 110% of personal property (if greater than \$100,000). Per the *North Carolina Clerk of Superior Court Procedures Manual*, Chapter 86, bond amounts should be reviewed upon the filing of annual inventories to ensure they remain sufficient.

³ Chapter 35A, Article 7 of the North Carolina General Statutes.



MARK J. KLEINSCHMIDT
EX OFFICIO JUDGE OF PROBATE
CLERK OF SUPERIOR COURT
ORANGE COUNTY
106 E. MARGARET LANE
HILLSBOROUGH, NC 27278

June 29, 2022

The Honorable Beth A. Wood
NC State Auditor
2 S. Salisbury St.
20601 Mail Center Road
Raleigh, NC 27699-0600

Re: 2022 State Audit of the Orange County Clerk of Superior Court's Office

Dear Auditor Wood

I am in receipt of the letter from your office of June 15, 2022, regarding the 2022 audit of the Orange County Clerk of Superior Court's office ("the 2022 audit"). I understand that the Orange County Clerk's Office will have two audit findings as a result of the 2022 audit. Thank you for the opportunity to respond to these findings.

1. FAILURE TO COMPEL ESTATE INVENTORY FILINGS OR FEE COLLECTION

The Clerk's office did not compel the filing of estate inventories or collect estate fees in accordance with state law.

Office of the State Auditor Recommendation

The Clerk should develop contingency plans to ensure estates are compelled to file inventories in the event of personnel shortages. In addition, the Clerk should implement monitoring procedures such as reviewing fee calculations for accuracy and identifying uncollected fees at the time of the final inventory files.

2. FAILURE TO COMPEL ESTATE INVENTORY FILINGS OR ASSESS AND COLLECT SUFFICIENT BONDS FOR ESTATES OF MINORS AND INCAPACITATED ADULTS

The Clerk's office did not compel the filing of guardianship estate inventories or assess and collect sufficient bonds to protect wards (minors or incapacitated adults) in accordance with state law.

Office of the State Auditor Recommendation

The Clerk should develop contingency plans to ensure inventory reports are reviewed during periods of staff turnover. In addition, the Clerk should implement monitoring procedures to ensure guardians are compelled to file inventories when necessary and that the bonds collected remain sufficient.

Clerk's Response

I believe the audit finding to be accurate. As I explained to State Auditor personnel during the audit, our office was forced to prioritize other duties during the audit period due to turnover of staff overseeing the compelling process. During the audit study period the Orange County Clerk's Office had repeated turnover in a position charged with overseeing the process of compelling the filing of inventories in both decedent's estates and guardianships. During the same time, our office was experiencing the highest volume of new estate filings in our county's history. I am confident that a lack of experience in the position and the high volume of new cases led to these issues.

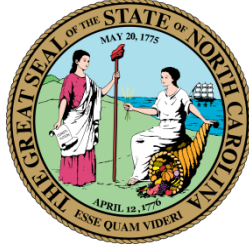
I am proud to say that the Orange County Clerk's Office has already taken measures to implement the State Auditor Recommendations. Authorization was requested and approved for the hiring of a one-year temporary employee to assist with developing and implementing a system for more effectively monitoring filings of inventories and accounts and ensuring that notices to file are timely sent to personal representatives managing decedents' estates and guardians. Also, a new staff member with experience practicing law and with several years of experience in the Orange County Register of Deeds Office joined our Estates Division this month. His experience and work ethic, along with the experience of the other members of this small division, has already allowed us to address a backlog of cases, notices to file, and the creation of dedicated time to review fee calculations for accuracy at the time of filing. With this new position and new talent, Orange County Estates Division is being completely reconfigured with a focus on creating a dedicated position for compelling inventories and accountings and creating a system a review of the calculations of fees and adequacy of bonds at the time of the filing of inventories and accounts.

Finally, please know how proud I am of the staff of the Orange County Clerk of Superior Court's Office. Together we were able to keep access to justice available to the people of our community during what has been one of the most difficulty periods in our state's history as we dealt a with worldwide pandemic. I am confident that the staff additions, training, and system changes I reference above will adequately address the two areas of deficit your staff identified. Please know that the state auditors who visited my office were courteous, professional, and efficient in their work. Thank you for the service you provide to the state.

Sincerely,



Mark Kleinschmidt
Clerk of Superior Court for the County of Orange



APPENDIX

Internal Control Components and Principles Significant to the Audit Objectives

Our general audit objective was to identify improvements needed in internal control over selected financial matters.

Internal control components and underlying principles that were significant to our audit objectives are identified in the table below.

COMPONENTS AND PRINCIPLES	AUDIT OBJECTIVES			
	CASH	ESTATES	ESCHEATS	TRUSTS
CONTROL ENVIRONMENT				
1. The oversight body and management should demonstrate a commitment to integrity and ethical values.	X	X	X	X
2. The oversight body should oversee the entity's internal control system.	X	X	X	X
3. Management should establish an organizational structure, assign responsibility, and delegate authority to achieve the entity's objectives.	X	X	X	X
4. Management should demonstrate a commitment to recruit, develop, and retain competent individuals.				
5. Management should evaluate performance and hold individuals accountable for their internal control responsibilities.				
RISK ASSESSMENT				
6. Management should define objectives clearly to enable the identification of risks and define risk tolerances.				
7. Management should identify, analyze, and respond to risks related to achieving the defined objectives.	X	X	X	X
8. Management should consider the potential for fraud when identifying, analyzing, and responding to risks.				
9. Management should identify, analyze, and respond to significant changes that could impact the internal control system.	X	X	X	X

CONTROL ACTIVITIES				
10. Management should design control activities to achieve objectives and respond to risks.	X	X	X	X
11. Management should design the entity's information system and related control activities to achieve objectives and respond to risks.				
12. Management should implement control activities through policies.	X	X	X	X
INFORMATION AND COMMUNICATION				
13. Management should use quality information to achieve the entity's objectives.	X	X	X	X
14. Management should internally communicate the necessary quality information to achieve the entity's objectives.	X	X	X	X
15. Management should externally communicate the necessary quality information to achieve the entity's objectives.	X	X	X	X
MONITORING ACTIVITIES				
16. Management should establish and operate monitoring activities to monitor the internal control system and evaluate the results.	X	X	X	X
17. Management should remediate identified internal control deficiencies on a timely basis.	X	X	X	X

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North Carolina Office of the State Auditor at:

919-807-7666



This audit required 235 hours at an approximate cost of \$24,910.