

**STATE OF NORTH CAROLINA  
COUNCIL OF INTERNAL AUDITING**

**INTERNAL AUDIT  
ACTIVITY REPORT**

**As Required by G.S. 143-747(c)(12)**

**October 2012**



*Prepared By:*

***Office of Internal Audit  
Office of State Budget and Management***

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# INTRODUCTION

The North Carolina Internal Audit Act<sup>1</sup> (the Act) was signed into law on August 31, 2007. The Act established the Council of Internal Auditing (Council) and required State agencies and universities (agencies) to establish a program of internal auditing. The Council of Internal Auditing is mandated to report on service efforts and accomplishments of these programs and propose legislation for consideration by the Governor and General Assembly. This report documents the service efforts and accomplishments from July 2011 through June 2012, of State agencies and the Council of Internal Auditing in fulfilling the mandates of the legislation.

## COUNCIL OF INTERNAL AUDITING

### *Membership, Programs and Staff*

The Council membership is set by statute as shown in Table 1. The Council meets quarterly to provide guidance, set policies, and assess progress of internal auditing efforts within State government.

**Table 1**

<b>Council of Internal Auditing Members</b>	
David T. McCoy, Chair	State Controller
Andy Willis	State Budget Director
Moses Carey Jr.	Secretary of Administration
Roy Cooper	Attorney General
David Hoyle	Secretary of Revenue
Beth Wood	State Auditor (nonvoting)

The Council is mandated to administer programs and activities which:

- Promulgate guidelines, develop technical manuals and suggest best practices;
- Conduct statewide internal audit staffing analysis;
- Provide training and professional development opportunities;
- Report on statewide internal audit service efforts and accomplishments;
- Develop and administer a peer review program;
- Develop and administer an internal audit recognition program;
- Develop and administer a shared internal audit program; and
- Maintain a report and audit plan repository.

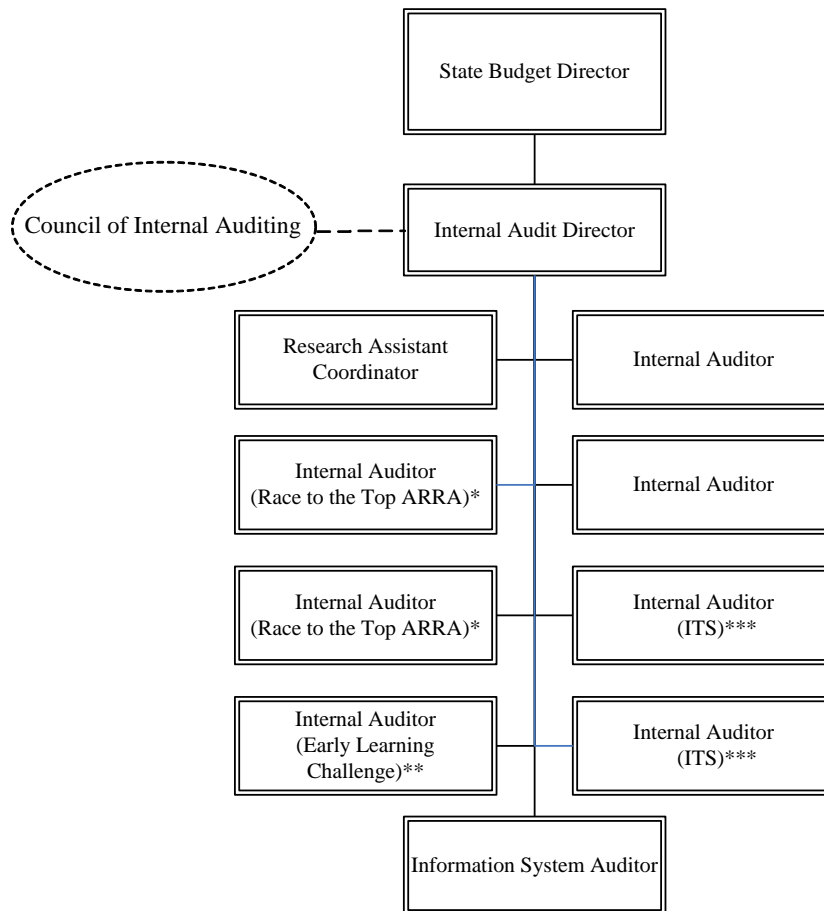
The Office of State Budget and Management (OSBM) support the Council and established the Office of Internal Audit (OIA) to house the staff to the Council. The organizational structure of the OIA is shown in Exhibit 1 on page 2. There are five permanent positions and five time-limited positions. The time-limited positions focus their efforts on the programs/agency that funds the position. The professional credentials held by the internal audit staff include:

- Three Certified Public Accountants;
- Three Certified Internal Auditors;
- Two Certified Internal Control Auditors;
- Two Certified Fraud Examiners;
- One Certified Government Auditing Professionals; and
- One Certified Government Financial Manager.

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<sup>1</sup> Entire Internal Audit Act is located in Appendix A.

**Exhibit 1  
Office of Internal Audit  
Organizational Structure  
June 30, 2012**



- \* Time-limited positions term August 31, 2014
- \*\* Time-limited position term December 31, 2015
- \*\*\* Receipt supported through MOU with ITS

The Office of Internal Audit had a 15% reduction in expenditures during FY2011-12 compared to the prior year. The decrease is related to the loss of State Fiscal Stabilization Funds which terminated September 30, 2011. The federal funds were used to hire six internal auditors whose primary purpose was to audit and provide technical assistance to agencies receiving ARRA funds. In addition, two different federal grants fund three auditor positions which are: two Race to the Top (RttT) and one Early Learning Challenge (ELC) auditors. These positions are strictly for auditing RttT and ELC funds. Finally, two auditor positions are funded through a memorandum of understanding (MOU) to provide audit services to Information Technology Services (ITS). The combined general and federal funds expenditures for FY2007-08 through FY2011-12 are shown in Table 2 on the next page.

As the economic downturn prolonged, the Office diligently continued to reduce spending. The Office of Internal Audit general fund reduction was 31% between FY2008/09 and FY2011/12. The effect of the reduction was elimination of the program administrator position, delays in filling vacant positions, reduction in training, postponement of audits requiring travel and delays in purchasing professional materials and software.

**Table 2**

<b>Office of Internal Audit Expenditures</b>					
	<b>FY2011/12</b>	<b>FY2010/11</b>	<b>FY2009/10</b>	<b>FY 2008/09</b>	<b>FY 2007/08</b>
<b>Expenditures</b>					
<b>Personal Services</b>	<b>718,992</b>	<b>\$ 867,475</b>	<b>\$ 562,759</b>	<b>\$ 466,451</b>	<b>\$ 161,526</b>
<b>Purchased Services</b>					
<i>Central Database Dev. &amp; Maintenance</i>		-	-	96,215	-
<i>Training &amp; Development</i>	14,460	7,662	3,760	11,205	24,500
<i>Information Technology Services</i>	13,272	10,720	1,415	40,545	6,000
<i>Travel, Telephone, Miscellaneous</i>	12,743	8,327	923	996	543
<b>Total Purchased Services</b>	<b>40,475</b>	<b>26,709</b>	<b>6,098</b>	<b>148,961</b>	<b>31,043</b>
<b>Supplies</b>	<b>100</b>	<b>710</b>	<b>1,232</b>	<b>129</b>	<b>2,425</b>
<b>Property, Plant, &amp; Equipment</b>	<b>550</b>	<b>580</b>	<b>872</b>	<b>516</b>	<b>10,042</b>
<b>Other</b>	-	-	60	110	358
<b>Total Expenditures</b>	<b>760,117</b>	<b>895,474</b>	<b>571,021</b>	<b>616,167</b>	<b>205,394</b>
<b>Carry Forward</b>	-	-	-	-	200,985
<b>Grand Total Expenditures</b>	<b>760,117</b>	<b>895,474</b>	<b>571,021</b>	<b>616,167</b>	<b>406,379</b>
<b><u>BREAKDOWN BY FUND SOURCE</u></b>					
<b>General Fund</b>	<b>425,146</b>	<b>429,948</b>	<b>469,126</b>	<b>616,176</b>	<b>406,379</b>
<b>ARRA State Fiscal Stabilization Fund</b>	<b>116,832</b>	<b>443,483</b>	<b>101,895</b>		
<b>ARRA Race to the Top Fund</b>	<b>150,079</b>	<b>22,042</b>			
<b>Early Learning Challenge</b>	<b>8,479</b>				
<b>Information Technology Services</b>	<b>59,583</b>				

***Efforts and Accomplishments***

Over the last five years the Council complied with all the mandated requirements in the Act. Guidelines and manuals were published in May 2008 and communicated to all internal auditors. The peer review, internal audit recognition, and shared internal audit programs are developed and operating. The staffing analysis is conducted every three years (See Appendix B for details) and annual activity report is published every year. Below is specific accomplishment during FY2011-12.

***Training and Professional Development Opportunities***

To maintain proficiency, audit standards require internal auditor participate in professional development. During May 2012, two training sessions were conducted. The, one day, Quality Assurance Review training session educated 26 internal auditors on how to conduct a quality assurance review. These internal auditors agreed to participate in the peer review program. The Performance Measures in Government training session was opened to employees in State government, licensing boards, and local government. There were 215 attending this one day training session.

In addition to the two training sessions, throughout the year, other free or low cost training is identified and communicated to all internal auditors. Communication takes place via email and

posting on OSBM website. Over the past year, approximately 50 professional development opportunities were identified and communicated.

#### *Peer Review Program*

The Peer Review program is a cooperative effort to establish a method to comply with the Institute of Internal Auditor's external quality assurance requirement. All internal audit functions are required to have an external quality assurance review every five years. This program enables agencies and universities to obtain their external assessment in a cost-effective method. North Carolina State University requested a peer review during FY2012. The process started in late June 2012 and is estimated to be completed by October 2012.

#### *Internal Audit Recognition Program*

The recognition program consists of two activities. First, in the quarterly newsletter an internal auditor or audit group is profiled. Second, the Award of Excellence is bestowed upon an internal auditor or group of internal auditors that goes above and beyond normal expectations of their job requirements to improve or promote internal auditing. The first award was presented to James Bruce Dillard Department of Transportation, Inspector General, Retired.

#### *Shared Internal Audit Program*

The internal audit program provides audit services to small State agencies. The guideline for State agencies to use the internal audit program for compliance with the Act is:

1. Has an annual operating budget exceeds ten million dollars but is less than seventy million dollars; or
2. Has less than 100 full-time equivalent employees; or
3. Receives and processes more than ten million dollars but less than seventy million dollars in cash in a fiscal year; or
4. Is deemed appropriate by the Council of Internal Auditing.

In addition, the program will provide audit assistance to small<sup>2</sup> internal audit functions upon request. Services are dependent upon resource availability of the program.

For accomplishment of this program see the State Agency Internal section titled Efforts and Accomplishments on page 10.

#### *Report and Audit Plan Repository*

Audit reports are submitted to the office throughout the year. Also, by September 30<sup>th</sup> of each year, agencies must submit their audit plans. For more details on compliance with requirements and the number and types of reports see the State Agency Internal section titled Efforts and Accomplishments on page 10.

#### *Proposed Legislation Changes*

The Council has approved four separate amendments to the Internal Audit Act. The most recent amendment relates to the obstruction of an audit. The other three amendments have been provided to the Governor and General Assembly in prior years. Amendments include:

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<sup>2</sup> Small internal audit functions is define as one or two auditor positions.



1. Technical Correction. Major changes included: adding a University System representative to the Council; expanding the reporting requirement of the internal audit director; and allowing the Office of State Personnel to develop auditor qualification.
2. Confidential Work Papers. Provides consistency within the General Statute regarding audit work papers. The Offices of the State Auditor and Controller, and the Department of Health and Human Service Internal Audit function has full confidential work paper law. The University system law provides work paper confidentially on a time-limited basis. All other internal audit functions have no confidential laws.
3. Subject to the Act. Provides consistency by requiring all Executive Branch and Council of State agencies to comply with the requirements in the Act. There are five agencies not subject to the Act.
4. Obstruction of Audit. Stipulates the penalty for willfully attempting to hinder, interfere or obstruct an audit.

Amendments can be seen in their entirety in Appendix C.

## **STATE AGENCY INTERNAL AUDIT FUNCTIONS**

### ***Audit Resources***

#### *Personnel Resources*

As shown in Table 3, on page 7, there are 139.25 internal auditor positions, which are spread across 34 State agencies. There was a net loss of one position throughout the State over the past year. Significant changes over the last year included:

- Department of Transportation gained five positions but still has taken a 29% reduction in positions over five years;
- Department of Public Safety has three less positions compared to the Departments of Correction, Crime Control and Public Safety, and Juvenile Justice and Delinquency Prevention combined positions before consolidation;
- OSBM lost six SFSF<sup>3</sup> time-limited positions and gained one ELC<sup>4</sup> and two positions funded by the Office of Information Technology Services.

There are twelve agencies with no internal auditor positions. Four of these agencies use the OSBM's Office of Internal Audit as their internal audit program and five agencies are not subject to the Internal Audit Act. Three university contract for audit service as follows:

- North Carolina School of the Arts contracts with Winston-Salem State University for audit services;
- North Carolina School of Science and Math contracts with the University of North Carolina General Administration; and
- Fayetteville State University utilizes contracted auditors.

The information in Table 3, on page 7, provides data on positions regardless of filled or vacant status.

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<sup>3</sup> Federal State Fiscal Stabilization Fund grant supported these positions.

<sup>4</sup> Federal Early Learning Challenge grant funds this position and terminates December 31, 2015.

Internal auditors can demonstrate proficiency by obtaining professional certification and advanced degrees. Overall, internal auditors hold 111 professional certifications in 15 different audit areas; 78% of these being either Certified Public Accountants, Certified Internal Auditors, Certified Information Systems Auditors or Certified Fraud Examiners. The number and type of professional certifications held by the agency's internal auditors are shown in Chart 1 on page 8.

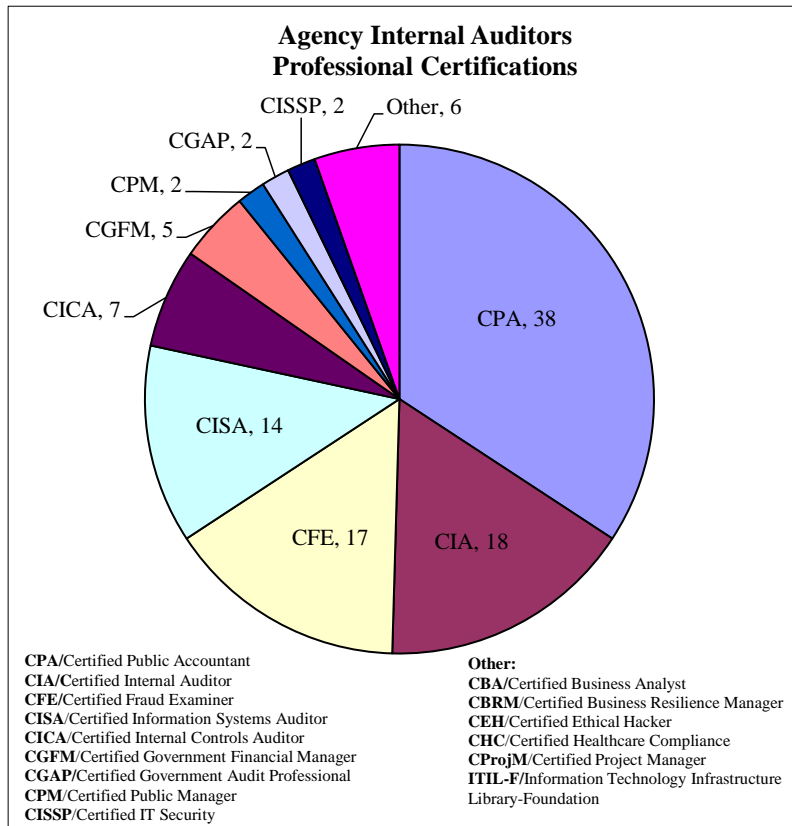
In addition, Chart 2, on page 8, shows advanced degrees held by the agency's internal auditors. Combined, the auditors hold 49 advanced degrees with 73% of these being Masters in Business Administration, Accounting or Accounting and Finance Management.

Table 3

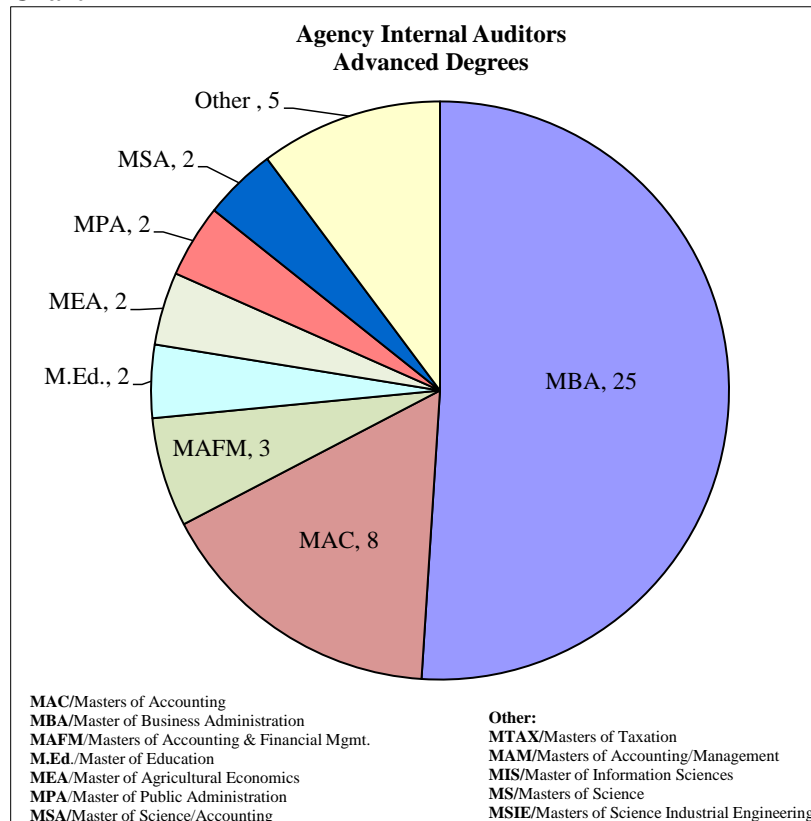
Statewide Internal Auditor Position Level Comparison											
Agency	Positions					Agency	Positions				
	2012	2011	2010	2009	2008		2012	2011	2010	2009	2008
Administrative Office of the Courts <sup>4</sup>	3	3	3	3	3	Office of Administrative Hearings <sup>4</sup>	0	0	0	0	0
Community College System Office	1	1	1	0	0	Office of Lieutenant Governor <sup>4</sup>	0	0	0	0	0
Department of Administration <sup>1</sup>	0	0	0	0	0	Office of State Controller <sup>4</sup>	0	0	0	1	1
Department of Agriculture & Consumer Services	1	1	1	1	1	Office of the Governor/Office State Budget and Management <sup>1,3</sup>	8	11	10	4	0
Department of Commerce <sup>2</sup>	3	0	0	0	2	Office of the State Auditor <sup>1</sup>	0	0	0	0	0
Department of Commerce, Employment Security Division <sup>2</sup>	N/A	2	2	1	0	State Board of Elections <sup>4</sup>	0	0	1	4	4
Department of Cultural Resources	1	1	1	1	1	Wildlife Resources Commission <sup>1</sup>	0	0	0	0	0
Department of Environment and Natural Resources	2	2	2	2	1	Appalachian State University	4	5	4	5	5
Department of Health and Human Services	8	8	8	8	8	East Carolina University	7	7	7	6	6
Department of Insurance	1	1	1	1	0	Elizabeth City State University	2	2	2	2	2
Department of Justice	1	1	1	1	0	Fayetteville State University <sup>5</sup>	0	2	2	2	2
Department of Labor <sup>1</sup>	0	0	0	0	0	North Carolina Agriculture and Technical State University	5	4	4	4	4
Department of Public Instruction	1	2	1	1	1	North Carolina Central University	3	3	3	3	4
Department of Public Safety <sup>9</sup>	19	N/A	N/A	N/A	N/A	North Carolina School of Science and Math <sup>7</sup>	0	1	1	1	1
Department of Correction <sup>9</sup>	N/A	18	18	18	19	North Carolina School of the Arts <sup>6</sup>	0	0	1	1	1
Department of Crime Control and Public Safety <sup>9</sup>	N/A	1	1	1	1	North Carolina State University	6.25	4.25	6	7	7
Department of Juvenile Justice and Delinquency Prevention <sup>9</sup>	N/A	3	3	3	4	University of North Carolina Hospitals	5	4	5	5	5
Department of Revenue	2	2	2	2	2	University of North Carolina - Asheville	1	1	1	1	1
Department of Secretary of State	1	1	1	1	1	University of North Carolina - Chapel Hill	6	6	6	6	6
Department of State Treasurer	3	2	2	1	1	University of North Carolina - Charlotte	4	4	4	4	4
State Health Plan <sup>8</sup>	N/A	0	0	0	0	University North Carolina - General Administration	1	1	1	1	1
Department of Transportation	22	17	25	31	31	University of North Carolina - Greensboro	2	2	2	3	2
Housing Finance Agency <sup>4</sup>	0	0	0	0	0	University of North Carolina - Pembroke	1	1	1	1	1
Indigent Defense Services <sup>4</sup>	1	1	1	1	1	University of North Carolina - Wilmington	4	4.5	4	4	4
Information Technology Services <sup>4</sup>	2	3	2	2	1	Western Carolina University	2	2	2	2	2
North Carolina Education Lottery <sup>4</sup>	2	2	2	2	2	Winston-Salem State University	4	4	3	3	3
						<b>Total</b>	<b>139.25</b>	<b>140.75</b>	<b>148.00</b>	<b>151.00</b>	<b>146.00</b>

1. Utilizes the Interagency Internal Audit program
2. The Employment Security Commission merged with Department of Commerce in FY2012, Division of Employment Service has federal funded internal audit position and the remaining Department of Commerce is utilizes the Interagency Internal Audit program
3. Council of Internal Auditing Interagency Internal Audit Program, housed in the Office of State Budget and Management
4. Agency is not subject to the Internal Audit Act
5. Uses contract auditors
6. Contracts with Winston-Salem State University
7. Contracts with UNC-General Administration
8. State Health Plan merged with Department of State Treasurer in FY2012
9. Departments of Correction, Crime Control and Public Safety, and Juvenile Justice and Delinquency Prevention consolidated as of January 1, 2012

**Chart 1**



**Chart 2**



*Computer Assisted Audit Tools*

In addition to personnel, internal audit functions use computer assisted audit tools (CAATs) to improve the efficiency and effectiveness of administrative and audit tasks. Automated tools range from basic office productivity software such as spreadsheet, word processors and text editing programs to more advanced software packages involving the use of statistical analysis and business intelligence tools.

The advanced software products are typically productivity tools or generalized audit software. Productivity tools aid with the administrative and management of the audit processes such as Teammate and SharePoint. Generalized audit software tools assist with data extract and analyze such as ACL, IDEA and SAS.

Table 4 shows all internal audit functions use the Microsoft Office products to enhance productivity through automation. In addition, fifteen agencies use generalized audit software tools for data extraction and analysis; and six agencies use productivity tools to automate work papers and work flow processes.

**Table 4**

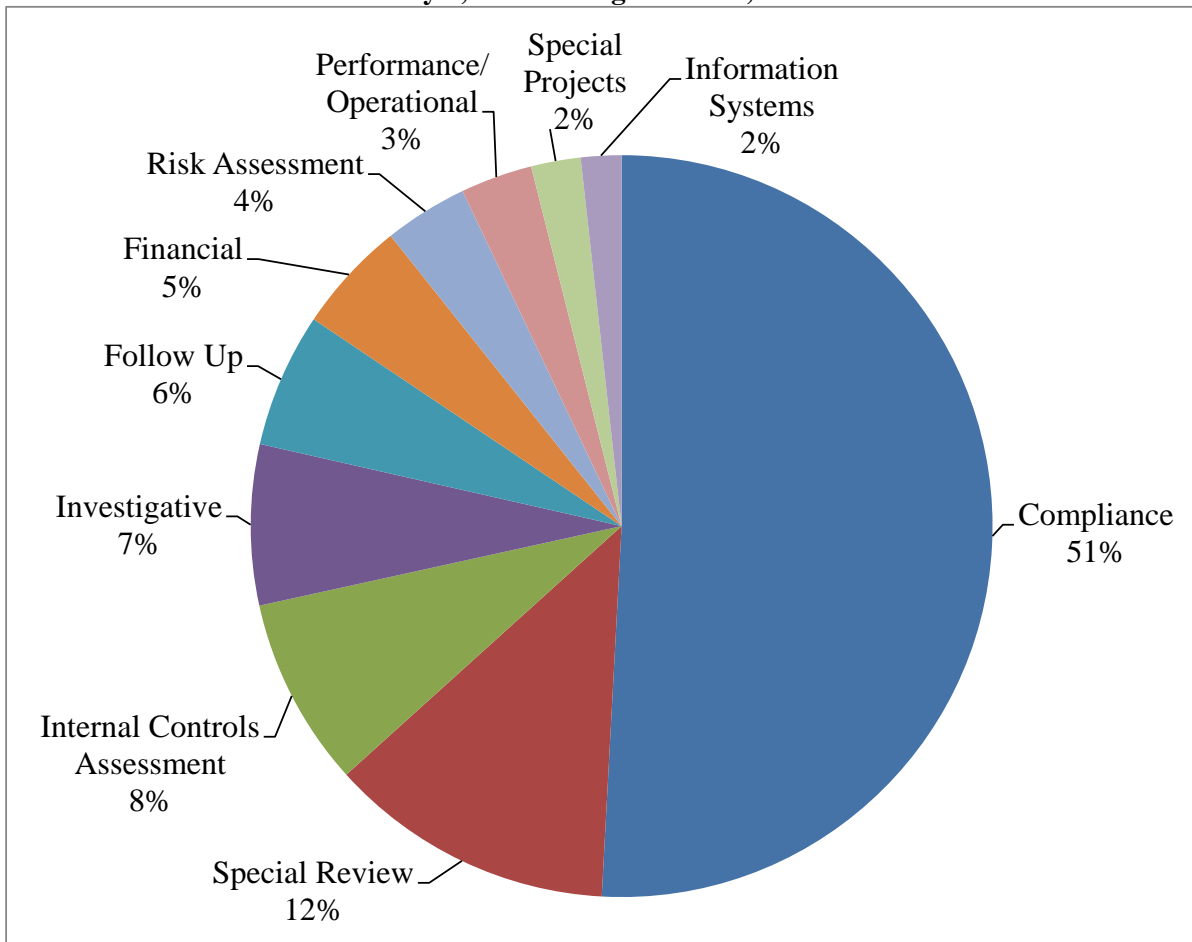
<b>Computer Assisted Audit Tools Usage</b>			
<b>State Agency</b>	<b>Spreadsheet or Word Documents<sup>1</sup></b>	<b>Generalized Audit Software<sup>2</sup></b>	<b>Productivity Tools<sup>3</sup></b>
Community College Central Office	✓		
Department of Agriculture and Consumer Services	✓		
Department of Commerce-Division of Employment Services	✓	✓	✓
Department of Cultural Resources	✓		
Department of Environment and Natural Resources	✓	✓	
Department of Health and Human Services	✓	✓	
Department of Insurance	✓		
Department of Justice	✓		
Department of Public Instruction	✓	✓	
Department of Public Safety	✓		
Department of Revenue	✓		
Department of Secretary of State	✓	✓	
Department of State Treasurer	✓		✓
Department of Transportation	✓		
Office of the Governor/Office of State Budget and Management	✓	✓	
Appalachian State University	✓		
East Carolina University	✓	✓	
Elizabeth City State University	✓		
North Carolina Agriculture and Technical State University	✓	✓	
North Carolina Central University	✓		
North Carolina State University	✓	✓	✓
University of North Carolina - Asheville	✓	✓	
University of North Carolina - Chapel Hill	✓	✓	
University of North Carolina - Charlotte	✓	✓	
University of North Carolina - General Administration	✓		
University of North Carolina - Greensboro	✓		
University of North Carolina - Pembroke	✓		
University of North Carolina - Wilmington	✓	✓	✓
University of North Carolina Hospitals	✓	✓	✓
Western Carolina University	✓		
Winston-Salem State University	✓	✓	✓

1. Microsoft Office products.  
2. Perform routine task for data extract and analysis. Some products are ACL, IDEA, and EZ-R Stats.  
3. Streamline process to managing audits through electronic work papers and work flows. Some products are Teammate and SharePoint.

### ***Efforts and Accomplishments***

Internal audit functions conduct various activities designed to add value and improve a State agency's operations. For the period July 1, 2011 through June 30, 2012, the majority of activities conducted by the internal auditors were compliance audits. Chart 3 shows the percentage of internal audit reports prepared by type. In addition to the audit work shown here, most internal audit functions provide technical assistance throughout the year. During the same time period, internal auditors provided assistance to their agency's management on 578 different activities which did not result in report issuance.

**Chart 3**  
**Agency Engagements**  
**July 1, 2011 through June 30, 2012**



The audit projects by State agency are shown in Table 5 on the next page. The Table depicts the efforts of each internal audit function. Efforts are directly related to the size of the audit function. There are many State agencies that have one internal auditor which limits the number of audits that can be accomplished throughout the year.

**Table 5**

**Agency Engagements  
July 1, 2011-June 30, 2012**

Agency	Financial	Performance/ Operational	Investigative	Compliance	Internal Controls Assessment	Information Systems	Risk Assessment	Follow Up	Special Review	Special Projects
Community College Central Office		1								3
Department of Agriculture & Consumer Services	8	2	8						2	
Department of Commerce-Division of Employment Security	3				41		1	1	32	
Department of Cultural Resources									4	
Department of Environment & Natural Resources	5		3	3	2				1	
Department of Health & Human Services		1	2	35	3			1		
Department of Insurance	1	2					1	2	1	
Department of Justice	1			1			1		1	
Department of Public Instruction					1		1			1
Department of Public Safety <sup>2</sup>	3	2	10	53	12		38	24	74	4
Department of Revenue				6	12	1			49	
Department of Secretary of State					1				6	
Department of State Treasurer		2		2	3		1	9		
Department of Transportation	33		37	740	1				3	
OIA's Interagency Internal Audit Program <sup>1</sup>		2	2	14	5	4	8		5	12
Appalachian State University	6	5	3	4	37	12	1	2	4	
East Carolina State University		5	20	2		2	2	14	4	
Elizabeth City State University								1	2	1
Fayetteville State University	1	3		1	1	1		1		1
North Carolina Agriculture & Technical State University	5	1	3	3	1			1	1	
North Carolina Central University	2	2	2	2	4		1	1	5	
North Carolina School of Science & Math					2			4	9	
North Carolina School of the Arts			1		1		1		1	
North Carolina State University			10	1		1		9		
University North Carolina - Asheville			1	1	1	1	1	1	5	1
University of North Carolina - Chapel Hill	1	3	2							4
University of North Carolina - Charlotte	4	2	1	4	1	2	1	3		
University of North Carolina - General Administration		1					1			1
University of North Carolina - Greensboro	2			4	4		1		2	
University of North Carolina - Pembroke	2		1				1	2	4	
University of North Carolina - Wilmington	1	3	4	3	3	1		7		4
University of North Carolina Hospitals	2	17	4	14	6	6	1	5	2	2
Western Carolina University	4	1	4	1	1		1	15		1
Winston-Salem State University	2		5		2		1		2	3
<b>Totals</b>	<b>86</b>	<b>55</b>	<b>123</b>	<b>894</b>	<b>145</b>	<b>31</b>	<b>64</b>	<b>103</b>	<b>219</b>	<b>38</b>

1. Using OIA Interagency Internal Audit Program: Department of Administration, Department of Commerce, Department of Labor, Department of State Auditor, Wildlife Resource Commission, Office of the Governor, and OSBM

2. Departments of Correction, Crime Control and Public Safety, and Juvenile Justice and Delinquency Prevention consolidated as of January 1, 2012

## Compliance

### Internal Audit Act and Council Requirements

The Internal Audit Act and the North Carolina Internal Audit Manual require internal audit functions to submit the following documents and reports to the Office of Internal Audit: internal audit charter, organizational chart, audit plan and engagement reports. Table 6 shows compliance with document submission and overall compliance rates for all 35 internal audit functions.

**Table 6**

<b>Compliance with Internal Audit Act and Statewide Internal Audit Manual</b>				
<b>Agency</b>	<b>Charter</b>	<b>Org Chart</b>	<b>Annual Plan</b>	<b>Reports</b>
Community College System Office	✓	✓	✓	
Department of Agriculture & Consumer Services	✓	✓	✓	✓
Department of Correction	✓	✓		✓
Department of Crime Control and Public Safety	✓	✓	✓	✓
Department of Juvenile Justice and Delinquency Prevention	✓	✓	✓	✓
Department of Public Safety <sup>1</sup>	✓	✓	N/A	✓
Department of Cultural Resources	✓	✓	✓	✓
Department of Environment and Natural Resources	✓	✓	✓	✓
Department of Health and Human Services <sup>2</sup>		✓	✓	✓
Department of Insurance	✓	✓	✓	✓
Department of Justice	✓	✓	✓	✓
Department of Public Instruction <sup>3</sup>	✓	✓		✓
Department of Revenue	✓	✓	✓	✓
Department of Secretary of State <sup>3</sup>	✓	✓		
Department of State Treasurer <sup>3</sup>	✓	✓		✓
Department of Transportation	✓	✓		✓
OIA's Interagency Internal Audit Program <sup>4</sup>	✓	✓	✓	✓
Appalachian State University <sup>3</sup>	✓	✓		✓
East Carolina University	✓	✓	✓	✓
Elizabeth City State University	✓	✓	✓	
Fayetteville State University	✓	✓	✓	✓
North Carolina A&T State University	✓	✓	✓	✓
North Carolina Central University	✓	✓	✓	✓
North Carolina School of the Arts	✓	✓	✓	
North Carolina School of Science and Math	✓	✓	✓	✓
North Carolina State University	✓	✓	✓	✓
University of North Carolina - Asheville	✓	✓	✓	✓
University of North Carolina - Chapel Hill	✓	✓	✓	✓
University of North Carolina - Charlotte	✓	✓	✓	✓
University of North Carolina - General Administration	✓	✓	✓	✓
University of North Carolina - Greensboro	✓	✓	✓	✓
University of North Carolina - Pembroke	✓	✓	✓	✓
University of North Carolina - Wilmington	✓	✓	✓	✓
University of North Carolina Hospitals	✓	✓		
Western Carolina University	✓	✓	✓	✓
Winston-Salem State University	✓	✓	✓	
<b>TOTAL</b>	<b>35</b>	<b>36</b>	<b>29</b>	<b>30</b>
<b>Compliance rate</b>	<b>97%</b>	<b>100%</b>	<b>81%</b>	<b>83%</b>

1. The Departments of Correction, Crime Control and Public Safety and Juvenile Justice and Delinquency Prevention consolidated on January 1, 2012.  
2. Follows Government Auditing Standards which does not require an audit charter.  
3. Internal audit position was vacant.  
4. Using OIA Interagency Internal Audit Program: Department of Administration, Department of Commerce, Department of Labor, Office of State Auditor, Wildlife Resources Commission, Office of the Governor, and Office of State Budget and Management.



*Internal Audit Director*

The Internal Audit Act requires State agencies to appoint a Director of Internal Audit (Director) who must report to the head of the agency. The Act defines head as Governor, Council of State member, Cabinet Secretary, the President of the University System or the Superintendent of Public Instruction. Table 7 shows all State agencies have appointed a director but only 39% of the director's report to the head of the State agency as defined in the Act. The low reporting compliance rate is most likely due to the strict definition of 'agency head' which has lead to one of the proposed legislative changes located on page 27.

**Table 7**

<b>Compliance with Internal Audit Director Appointment and Reporting</b>		
<b>Agency</b>	<b>Director Appointed</b>	<b>Meets Reporting Requirement</b>
Community College Central Office	✓	Yes
Department of Administration	✓	Yes
Department of Agriculture and Consumer Services	✓	Yes
Department of Commerce	✓	No
Department of Cultural Resources	✓	Yes
Department of Environment and Natural Resources	✓	Yes
Department of Health and Human Services	✓	Yes
Department of Insurance	✓	Yes
Department of Justice	✓	Yes
Department of Labor	✓	No
Department of Public Instruction	✓	Yes
Department of Public Safety	✓	No
Department of Revenue	✓	Yes
Department of State Treasurer	✓	Yes
Department of the Secretary of State	✓	Yes
Department of Transportation	✓	Yes
Office of the Governor/Office of State Budget and Management	✓	Yes
Office of the State Auditor	✓	Yes
Wildlife Resources Commission	✓	No
Appalachian State University	✓	No
East Carolina University	✓	No
Elizabeth City State University	✓	No
Fayetteville State University	✓	No
North Carolina Agriculture and Technical State University	✓	No
North Carolina Central University	✓	No
North Carolina School of Science and Math	✓	No
North Carolina School of the Arts	✓	No
North Carolina State University	✓	No
University of North Carolina - Asheville	✓	No
University of North Carolina - Chapel Hill	✓	No
University of North Carolina - Charlotte	✓	No
University of North Carolina - General Administration	✓	No
University of North Carolina - Greensboro	✓	No
University of North Carolina - Pembroke	✓	No
University of North Carolina - Wilmington	✓	No
University of North Carolina Hospitals	✓	No
Western Carolina University	✓	No
Winston-Salem State University	✓	No
<b>Compliance rate</b>	<b>100%</b>	<b>39%</b>

*External Quality Assurance Review (Peer Review)*

Quality assurance reviews are required either every three or five years, depending on which audit standard is followed. Thirteen internal audit functions are currently being developed and are not required to have a review. Of the 23 internal audit functions established, only two have received external quality assurance reviews within the required time period as shown in Table 8. It can take 6 months to prepare for an external quality assurance review. North Carolina State University's peer review began June 2012 and should be completed in October 2012. Fayetteville State University completed the self-assessment and requested a peer review. This review is expected to begin in November 2012.

**Table 8**

<b>Agency Establishment Date and Compliance with Quality Assurance Review (QAR) Requirement</b>			
<b>Agency/University</b>	<b>Agency Establishment Date</b>	<b>Date of Last QAR</b>	<b>Deadline For First Required QAR</b>
<b><u>Compliant</u></b>			
University of North Carolina - Wilmington	1983	June 2011	
East Carolina University		May 2011	
<b><u>Non-Compliant</u></b>			
Department of Agriculture & Consumer Services	1969	None	
Department of Health and Human Services	1994	March 2004	
Department of Transportation		December 2002	
Appalachian State University	1965	None	
Elizabeth City State University	1994	None	
Fayetteville State University	1998	None	
North Carolina A&T State University	1969	July 1997	
North Carolina Central University	1997	None	
North Carolina School of the Arts	2004	None	
North Carolina State University	1963	None	
University of North Carolina - Asheville	2001	None	
University of North Carolina - Chapel Hill	1963	None	
University of North Carolina - Charlotte	1973	None	
University of North Carolina - Greensboro	1984	None	
University of North Carolina - Pembroke	1984	None	
University of North Carolina Hospitals	1988	None	
Western Carolina University	1975	None	
Winston-Salem State University	1992	None	
<b><u>Not Required</u></b>			
North Carolina School of Science and Math	November 2007	None	November 2012
Department of Public Safety <sup>1</sup>		None	December 2012
Department of Cultural Resources	January 2008	None	January 2013
Department of Insurance	June 2008	None	June 2013
Department of Secretary of State	July 2008	None	July 2013
OIA Internal Audit Interagency program <sup>2</sup>	September 2008	None	September 2013
Department of Environment and Natural Resources	October 2008	None	October 2013
Department of Revenue	October 2008	None	October 2013
Department of Justice	February 2009	None	February 2014
Department of State Treasurer	April 2009	None	April 2014
Department of Public Instruction	June 2009	None	June 2014
Community College System Office	September 2009	None	September 2014
University of North Carolina - General Administration	August 2010	None	August 2015

1. Departments of Correction, Crime Control and Public Safety, and Juvenile Justice and Delinquency Prevention consolidated on January 1, 2012. Council allowed the new Department until the end of the year to comply with this requirement.

2. Using OIA Interagency Internal Audit Program: Department of Administration, Department of Commerce, Department of Labor, Office of State Auditor, Wildlife Resources Commission, Office of the Governor, and Office of State Budget and Management.

**APPENDIX A**  
**NORTH CAROLINA INTERNAL AUDIT ACT**

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## **Appendix A Internal Audit Act**

### Article 79.

#### Internal Auditing.

#### **§ 143-745. Definitions; intent; applicability.**

- (a) For the purposes of this section:
  - (1) "Agency head" means the Governor, a Council of State member, a cabinet secretary, the Chief Justice of the Supreme Court, the President of The University of North Carolina, and the Superintendent of Public Instruction.
  - (2) "State agency" means each department created pursuant to Chapter 143A or 143B of the General Statutes, the Judicial Branch, The University of North Carolina, and the Department of Public Instruction.
- (b) This Article applies only to a State agency that:
  - (1) Has an annual operating budget that exceeds ten million dollars (\$10,000,000);
  - (2) Has more than 100 full-time equivalent employees; or
  - (3) Receives and processes more than ten million dollars (\$10,000,000) in cash in a fiscal year. (2007-424, s. 1.)

#### **§ 143-746. Internal auditing required.**

- (a) Requirements. – A State agency shall establish a program of internal auditing that:
  - (1) Implements an effective system of internal controls that safeguards public funds and assets and minimizes incidences of fraud, waste, and abuse.
  - (2) Ensures programs and business operations are administered in compliance with federal and state laws, regulations, and other requirements.
  - (3) Reviews the effectiveness and efficiency of agency and program operations and service delivery.
  - (4) Periodically audits the agency's major systems and controls, including:
    - a. Accounting systems and controls.
    - b. Administrative systems and controls.
    - c. Electronic data processing systems and controls.
- (b) Internal Audit Standards. – Internal audits shall comply with current Standards for the Professional Practice of Internal Auditing issued by the Institute for Internal Auditors or, if appropriate, Government Auditing Standards issued by the Comptroller General of the United States.
- (c) Appointment and Qualifications of Internal Auditors. – Any internal auditor employed by a State agency shall at a minimum have a bachelor's degree from an accredited college or university and:
  - (1) Certification or licensure as a certified public accountant, certified internal auditor, certified fraud examiner, certified information systems auditor, professional engineer, or attorney; or
  - (2) A minimum of five years' experience in internal or external auditing, management consulting, program evaluation, management analysis, economic analysis, industrial engineering, or operations research.
- (d) Director of Internal Auditing. – The agency head shall appoint a Director of Internal Auditing who shall report to the agency head and shall not report to any employee subordinate to the agency head. (2007-424, s. 1.)

**§ 143-747. Council of Internal Auditing.**

- (a) The Council of Internal Auditing is created, consisting of the following members:
  - (1) The State Controller who shall serve as Chair.
  - (2) The State Budget Officer.
  - (3) The Secretary of Administration.
  - (4) The Attorney General.
  - (5) The Secretary of Revenue.
  - (6) The State Auditor who shall serve as a nonvoting member. The State Auditor may appoint a designee.
- (b) The Council shall be supported by the Office of State Budget and Management.
- (c) The Council shall:
  - (1) Hold its first meeting before November 1, 2007, and thereafter at the call of the Chair or upon written request to the Chair by two members of the Council.
  - (2) Keep minutes of all proceedings.
  - (3) Promulgate guidelines for the uniformity and quality of State agency internal audit activities.
  - (4) Recommend the number of internal audit employees required by each State agency.
  - (5) Develop internal audit guides, technical manuals, and suggested best internal audit practices.
  - (6) Administer an independent peer review system for each State agency internal audit activity; specify the frequency of such reviews consistent with applicable national standards; and assist agencies with selection of independent peer reviewers from other State agencies.
  - (7) Provide central training sessions, professional development opportunities, and recognition programs for internal auditors.
  - (8) Administer a program for sharing internal auditors among State agencies needing temporary assistance and assembly of interagency teams of internal auditors to conduct internal audits beyond the capacity of a single agency.
  - (9) Maintain a central database of all annual internal audit plans; topics for review proposed by internal audit plans; internal audit reports issued and individual findings and recommendations from those reports.
  - (10) Require reports in writing from any State agency relative to any internal audit matter.
  - (11) If determined necessary by a majority vote of the council:
    - a. Conduct hearings relative to any attempts to interfere with, compromise, or intimidate an internal auditor.
    - b. Inquire as to the effectiveness of any internal audit unit.
    - c. Authorize the Chair to issue subpoenas for the appearance of any person or internal audit working papers, report drafts, and any other pertinent document or record regardless of physical form needed for the hearing.
  - (12) Issue an annual report including, but not limited to, service efforts and accomplishments of State agency internal auditors and to propose legislation for consideration by the Governor and General Assembly. (2007-424, s. 1.)

**APPENDIX B**  
**Staffing Recommendation**

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## Appendix B Staffing Recommendation

Council of Internal Auditing State Agency Internal Audit Staffing Level Recommendation October 2010				
Agency	Total Internal Audit Positions Needed	Current Internal Audit Positions	Recommended Number of New Positions	Estimated Cost of New Internal Audit Positions
Department of Administration	3	0	3	279,000
Department of Agriculture and Consumer Services	3	1	2	186,000
Department of Commerce	5	0	5	465,000
Department of Correction	18	18	-	-
Department of Crime Control & Public Safety	5	1	4	372,000
Department of Cultural Resources	2	1	1	93,000
Department of Environment and Natural Resources	8	2	6	558,000
Department of Health and Human Services	19	8	11	1,023,000
Department of Insurance	2	1	1	93,000
Department of Justice	3	1	2	186,000
Department of Juvenile Justice and Delinquency Prevention	3	3	-	-
Department of Labor	Shared Pool	0	-	-
Department of Public Instruction	3	1	2	186,000
Department of Revenue	2	2	-	-
Department of State Treasurer	2	2	-	-
Department of the Secretary of State	Shared Pool	1	-	-
Department of Transportation	31	25	6	558,000
Office of Administrative Hearings	n/a	0	-	-
Office of Lieutenant Governor	n/a	0	-	-
Office of the Governor /Office of State Budget and Management	Shared Pool	4	-	-
Office of the State Auditor	Shared Pool	0	-	-
Wildlife Resource Commission	Shared Pool	0	-	-
North Carolina Community College Central Office	3	1	2	186,000
Appalachian State University	4	4	-	-
East Carolina University	7	7	-	-
Elizabeth City State University	2	2	-	-
Fayetteville State University	2	2	-	-
North Carolina A&T State University	4	4	-	-
North Carolina Central University	3	3	-	-
North Carolina School of Science & Math	1	1	-	-
North Carolina School of the Arts	1	1	-	-
North Carolina State University	7	6	1	93,000
University of North Carolina Hospitals	7	5	2	186,000
University of North Carolina-Asheville	1	1	-	-
University of North Carolina-Chapel Hill	8	6	2	186,000
University of North Carolina-Charlotte	4	4	-	-
University of North Carolina-General Administration	3	1	2	186,000
University of North Carolina-Greensboro	3	2	1	93,000
University of North Carolina-Pembroke	1	1	-	-
University of North Carolina-Wilmington	4	4	-	-
Western Carolina University	2	2	-	-
Winston-Salem State University	3	3	-	-
<b>Subtotal</b>	<b>179</b>	<b>131</b>	<b>53</b>	<b>4,929,000</b>
<b>Agencies Not Subject to Legislation</b>				
Administrative Office of the Courts	6	3	-	-
Employment Security Commission	10	2	-	-
Housing Finance Agency	Shared Pool	0	-	-
Information Technology Services	3	2	-	-
North Carolina Education Lottery	6	2	-	-
Office of State Controllor	Shared Pool	0	-	-
State Board of Elections	Shared Pool	1	-	-
State Health Plan	18	0	-	-
<b>Subtotal</b>	<b>43</b>	<b>10</b>	<b>0</b>	<b>0</b>
<b>Grand Total</b>	<b>222</b>	<b>141</b>	<b>53</b>	<b>4,929,000</b>
1 - Agencies with an established internal audit function with one position may utilize the shared pool for support.				
2 - Six time-limited positions within the Office of Budget and Management are not included. The positions terminate September 30, 2011 and are only used to audit American Recovery and Reinvestment Act funds through State government.				

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**APPENDIX C**  
**Proposed Legislation**

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**Appendix B  
Proposed Legislation**

The Council of Internal Auditing voted to propose four amendments to the Internal Audit Act, one being a revision and the other an addition to the Act.

***AMENDMENT 1: Revisions to the Internal Audit Act***

The Council of Internal Auditing successfully introduced House Bill 393 (see below) during the 2011-2012 General Assembly Session. House Bill 393 passed the House of Representatives and the Senate sent the Bill to the Program Evaluation Committee receiving a favorable vote, then to the Committee on Finance where no action was taken.

**GENERAL ASSEMBLY OF NORTH CAROLINA  
SESSION 2011  
HOUSE BILL 393**

Short Title:	Modify Internal Auditing Statutes.	(Public)
Sponsors:	Representatives Hastings and McGee (Primary Sponsors). For a complete list of Sponsors, see Bill Information on the NCGA Web Site.	
Referred to:	Government.	

March 17, 2011

A BILL TO BE ENTITLED  
AN ACT TO MODIFY THE INTERNAL AUDITING STATUTES APPLICABLE TO LARGE  
STATE DEPARTMENTS AND THE UNIVERSITY SYSTEM.

The General Assembly of North Carolina enacts:

**SECTION 1.** Article 79 of Chapter 143 of the General Statutes reads as rewritten:

"Article 79.

"Internal Auditing.

**"§ 143-745. Definitions; intent; applicability.**

- (a) For the purposes of this section:
  - (1) "Agency head" means the Governor, a Council of State member, a cabinet secretary, the President of The University of North Carolina, and the Superintendent of Public Instruction.
  - (2) "State agency" means each department created pursuant to Chapter 143A or 143B of the General Statutes, The University of North Carolina, and the Department of Public Instruction.
- (b) This Article applies only to a State agency that:
  - (1) Has an annual operating budget that exceeds ten million dollars (\$10,000,000);
  - (2) Has more than 100 full-time equivalent employees; or

- (3) Receives and processes more than ten million dollars (\$10,000,000) in cash in a fiscal year.

**"§ 143-746. Internal auditing required.**

- (a) Requirements. – A State agency shall establish a program of internal auditing that:
  - (1) ~~Implements~~ Promotes an effective system of internal controls that safeguards public funds and assets and minimizes incidences of fraud, waste, and abuse.
  - (2) ~~Ensures~~ Determines if programs and business operations are administered in compliance with federal and state laws, regulations, and other requirements.
  - (3) Reviews the effectiveness and efficiency of agency and program operations and service delivery.
  - (4) Periodically audits the agency's major systems and controls, including:
    - a. Accounting systems and controls.
    - b. Administrative systems and controls.
    - c. ~~Electronic data processing~~ Information technology systems and controls.

(b) Internal Audit Standards. – Internal audits shall comply with current Standards for the Professional Practice of Internal Auditing issued by the Institute for Internal Auditors or, if appropriate, Government Auditing Standards issued by the Comptroller General of the United States.

(c) Appointment and Qualifications of Internal Auditors. – ~~Any internal auditor employed by a State agency shall at a minimum have a bachelor's degree from an accredited college or university and:~~ Any state employee who performs the internal audit function shall meet the minimum qualifications for internal auditors established by the Office of State Personnel.

- (1) ~~Certification or licensure as a certified public accountant, certified internal auditor, certified fraud examiner, certified information systems auditor, professional engineer, or attorney; or~~
- (2) ~~A minimum of five years' experience in internal or external auditing, management consulting, program evaluation, management analysis, economic analysis, industrial engineering, or operations research.~~

(d) Director of Internal Auditing. – The agency head shall appoint a Director of Internal Auditing who shall report to (i) the agency head and shall not report to any employee subordinate to the agency head; head, (ii) the chief deputy or chief administrative assistant, or (iii) the agency governing board, or subcommittee thereof, if such a governing board exists. The Director of Internal Auditing shall be organizationally situated in a manner that avoids impairments to independence as defined in the auditing standards referenced in subsection (b) of this section.

**"§ 143-747. Council of Internal Auditing.**

- (a) The Council of Internal Auditing is created, consisting of the following members:
  - (1) The State ~~Controller~~ Controller, who shall serve as Chair.
  - (2) The State Budget Officer.
  - (3) The Secretary of Administration.
  - (4) The Attorney General.
  - (5) The Secretary of Revenue.
  - (6) The President of The University of North Carolina, who may appoint a designee.
  - (7) The State ~~Auditor~~ Auditor, who shall serve as a nonvoting member. The State Auditor may appoint a designee.
- (b) The Council shall be supported by the Office of State Budget and Management.
- (c) The Council shall:
  - (1) ~~Hold its first meeting before November 1, 2007, and thereafter~~ meetings at the call of the Chair or upon written request to the Chair by two members of the Council.

- (2) Keep minutes of all proceedings.
- (3) Promulgate guidelines for the uniformity and quality of State agency internal audit activities.
- (4) Recommend the number of internal audit employees required by each State agency.
- (5) Develop internal audit guides, technical manuals, and suggested best internal audit practices.
- (6) Administer an independent peer review system for each State agency internal audit activity; specify the frequency of such reviews consistent with applicable national standards; and assist agencies with selection of independent peer reviewers from other State agencies.
- (7) Provide central training sessions, professional development opportunities, and recognition programs for internal auditors.
- (8) Administer a program for sharing internal auditors among State agencies needing temporary assistance and assembly of interagency teams of internal auditors to conduct internal audits beyond the capacity of a single agency.
- (9) Maintain a central database of all annual internal audit plans; topics for review proposed by internal audit plans; internal audit reports issued and individual findings and recommendations from those reports.
- (10) Require reports in writing from any State agency relative to any internal audit matter.
- (11) If determined necessary by a majority vote of the council:
  - a. Conduct hearings relative to any attempts to interfere with, compromise, or intimidate an internal auditor.
  - b. Inquire as to the effectiveness of any internal audit unit.
  - c. Authorize the Chair to issue subpoenas for the appearance of any person or internal audit working papers, report drafts, and any other pertinent document or record regardless of physical form needed for the hearing.
- (12) Issue an annual report including, but not limited to, service efforts and accomplishments of State agency internal auditors and to propose legislation for consideration by the Governor and General Assembly."

**SECTION 2.** This act is effective when it becomes law.

### ***AMENDMENT 2: Confidential Work Papers***

The Council approved the following amendment to the Internal Audit Act.

#### **N.C. Gen Stat. § 143-748**

An internal auditor shall maintain, for 10 years, a complete file of all audit reports and reports of other examinations, investigations, surveys, and reviews issued under the internal auditor's authority. Audit work papers and other evidence and related supportive material directly pertaining to the work of that internal auditor's office shall be retained in accordance with Chapter 132 of the General Statutes. To promote intergovernmental cooperation and avoid unnecessary duplication of audit effort, audit work papers related to issued audit reports shall be, unless otherwise prohibited by law, made available for inspection by duly authorized representatives of the State and federal government in connection with some matter officially before them. Except as provided above, or upon subpoena issued by a duly authorized court or court official, audit work papers shall be kept confidential. Audit reports shall be public records

to the extent they do not include information which, under State laws, is confidential and exempt from Chapter 132 of the General Statutes or would compromise the security of a State agency.

***AMENDMENT 3: Not Subject to the Act***

There are five State agencies not subject to the Internal Audit Act. The Council approved the following amendment of the Internal Audit Act.

Article 79.

Internal Auditing.

**§ 143-745. Definitions; intent; applicability.**

(a) For the purposes of this section:

- (1) "Agency head" means the Governor, a Council of State member, a cabinet secretary, commissioner, director, executive director, the President of The University of North Carolina, the State Controller, the Chief Information Officer, Executive Administrator and the Department of Public Instruction.
- (2) "State agency" means each department or entity created pursuant to Chapter 143A, or 143B of the General Statutes, The University of North Carolina, the North Carolina State Board of Election, the State Health Plan for Teachers and State Employees, the Office of Information Technology Services, Employment Security Commission of North Carolina, North Carolina Housing Finance Agency, North Carolina Education Lottery, and the Department of Public Instruction.

***AMENDMENT 4 OBSTRUCTION***

*To be inserted*