

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

**INTERNAL AUDIT
ACTIVITY REPORT**

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

October 2017



Prepared By:

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

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INTRODUCTION

The North Carolina Internal Audit Act¹ (the Act) was signed into law on August 31, 2007. The Act established the Council of Internal Auditing (Council) and requires all Executive branch agencies² 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 2016 through June 2017 of 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

Council of Internal Auditing Members	
Dr. Linda Combs, Chair	State Controller
Charles Perusse	State Budget Officer
Machelle Sanders	Secretary of Administration
Josh Stein	Attorney General
Ronald Penny	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.

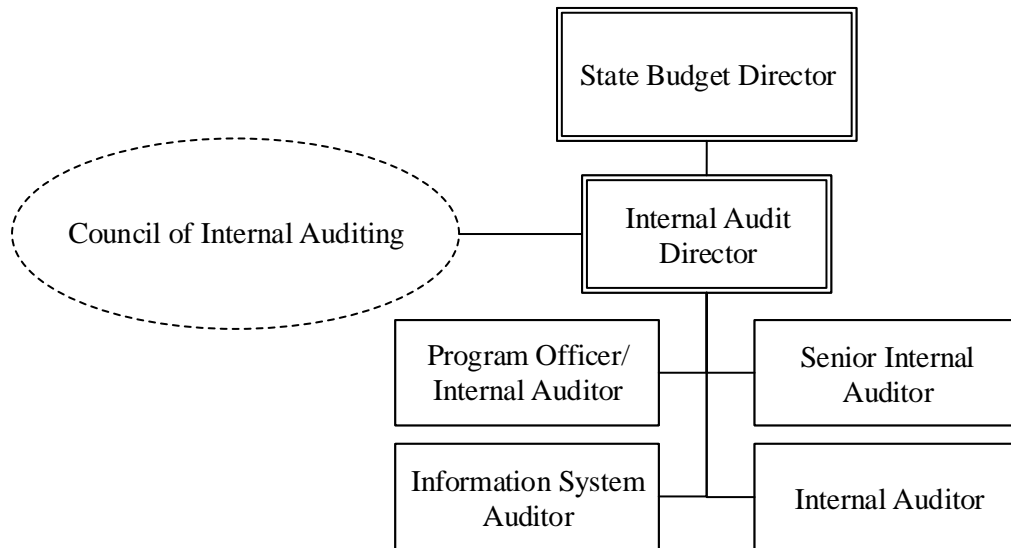
The Office of State Budget and Management (OSBM) supports the Council and established the Office of Internal Audit (OIA) to house the Council staff. The organizational structure of the OIA is shown in Exhibit 1 on the next page. The five staff members hold eight professional credentials as follows:

- Two Certified Internal Auditors;
- Two Certified Fraud Examiner;
- One Certified Government Audit Professional;
- One Certified Public Accountants;
- One Certified Internal Control Auditor; and
- One Certified Government Financial Manager.

¹ Entire Internal Audit Act is in Appendix A.

² Agency means department, office, university, commission, board.

Exhibit 1
Office of Internal Audit as of June 30, 2017



The expenditures for FY2012-13 through FY2016-17 are shown in Table 2. The Office of Internal Audit had a 1% overall increase in expenditures during FY2016-17.

Costs related to contractors were for: 1) obtaining experts; and 2) services to an agency not under the authority of OIA which were charged to those agencies. The increase in travel cost is due to a peer review performed at the State of Rhode Island. Rhode Island reimbursed OSBM for all associated costs. Also, training expenditures continue to decrease due to a small fee being charged to participants attending the training sessions.

Table 2

Office of Internal Audit Five Year Expenditures					
Expenditures	FY2016/17	FY2015/16	FY2014/15	FY2013/14	FY2012/13
Personnel					
<i>Employee</i>	518,220	504,252	413,646	464,540	537,190
<i>Contractor</i>	15,020	29,887	172,678	33,315	21,688
Total Personnel	533,240	534,139	586,324	497,855	558,878
Purchased Services					
<i>Software</i>	5,411	4,267	3,552	4,533	
<i>Training & Development</i>	2,244	4,968	6,355	13,210	8,458
<i>Information Technology Services</i>	6,368	5,760	5,471	6,895	5,628
<i>Travel, Telephone, Miscellaneous</i>	7,820	2,486	2,838	8,489	10,138
Total Purchased Services	21,844	17,481	18,216	33,127	24,224
Supplies	-	50	-	-	100
Property, Plant, & Equipment	2,181	610	-	-	-
Other	1,385	452	1,191	-	-
Total Expenditures	558,650	552,732	605,731	530,982	583,202
<u>BREAKDOWN BY FUND SOURCE</u>					
General Fund	526,422	522,845	382,560	452,695	417,456
ARRA Race to the Top Fund	-	29,887	223,172	78,287	92,555
Early Learning Challenge	-	-	-	-	43,297
Information Technology Services	-	-	-	-	29,894
Other State Agencies	15,020	-	-	-	-
Rhode Island QAR	17,208	-	-	-	-

Efforts and Accomplishments

Over the last ten years the Council complied with all the mandated requirements in the Act. Guidelines and manuals were published in May 2008, communicated to all internal auditors and continue to be updated when necessary. The peer review, internal audit recognition and shared internal audit programs were developed and operationalized. Below are specific accomplishments during FY2016-17.

Training and Professional Development Opportunities

To maintain proficiency, audit standards require internal auditor participation in professional development. During FY2016-17, the Council sponsored three trainings which provided internal auditors the opportunity to earn up to 54 certified professional education (CPE) hours.

A one day training session was held in December 2016, covering leading edge ideas to improve the efficiency and effectiveness of audit functions and audit projects. The training session provided eight hours of certified professional education (CPE) hours at a cost of \$50.00 per participant. Participants were invited from state agencies, universities, community colleges, local education agencies, local governments and IIA members. There were 155 registered participants and the cost of sponsoring the training session was just under \$40 per participant. Based on participant surveys, 96% responded that the overall contract of the sessions provided value.

OIA staff coordinated a four-day Certified Internal Auditor (CIA) review course that corresponded to the three parts of the Certified Internal Auditor examination administered by the *Institute of Internal Auditors* (IIA). The training occurred between February and May 2017. The training sessions provided 32 hours of CPE hours at a cost of \$65.00 per day. There were 67 registered participants and the cost of sponsoring the training was about \$56 per participant per day. Survey responses indicated 17 participants attempted Part 1 and/or Part 2 of the examination; 11 (65%) successfully passed. Based on IIA records, 3 participants (4%) passed all three parts and obtained the CIA designation.

The 2nd Annual Fraud Audit Conference was held in June 2017. This 2-day training session provided 14 CPE hours at a minimal cost of \$40 per day. Participants were invited from state agencies, universities, community colleges, local education agencies, and local governments. There were 150 registered participants and the cost of sponsoring this conference was \$35 per participant per day. Based on participant surveys, there was a 98% very good or excellent program rating.

In addition to the three 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 postings on the OSBM website. Over the past year, 64 professional development opportunities were identified and communicated. There were 243.5 CPE hours identified and 19% of these hours were free of charge.

Peer Review Program

The Peer Review program is a cooperative effort to establish a method to comply with the Institute of Internal Auditors' external quality assurance review requirement. All internal audit functions are required to have an external quality assurance review every five years. This program enables state agencies to obtain their external assessment in a cost-effective method. Over the last five years, 26 agencies used the Peer Review program. The Department of Commerce's Division of Employment Services, Elizabeth City State University and Department of Agriculture and Consumer Services used the Peer Review program in FY2016-17 and all received a generally conforms rating³. See page 15 for more details related to the outcomes of the Peer Review program.

³ Generally Conforms with the *Internal Professional Practice Framework* is the highest rating that can be received for an external quality assurance review.

Internal Audit Recognition Program

The North Carolina Award of Excellence is the Council of Internal Auditing award for outstanding achievement in internal auditing. To express its appreciation for excellence in the field of internal auditing, this award is presented annually to honor a state internal auditor or a group of internal auditors who has made extraordinary contributions that promote excellence in internal auditing. The 2016 Internal Auditor Award of Excellence was presented to Jeani Allen, Internal Audit Director for the Department of Public Instruction.

Shared Internal Audit Program

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

1. Has an annual operating budget exceeding 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.

Currently, 11 agencies qualify to use this program; however, four of these agencies opt to have in-house functions. These agencies are the Department of the Secretary of State, Elizabeth City State University, House Finance Agency and Office of the State Controller.

The program will also provide audit assistance to any internal audit functions upon request. Services are dependent upon resource availability of the program. For accomplishment of this program, see the State Agency Internal Audit Functions section titled Efforts and Accomplishments on page 12.

Report and Audit Plan Repository

Audit reports are submitted to the office throughout the year. Agencies must also submit their audit plans by September 30th of each year. For more details on compliance with requirements and the number and types of reports, see the State Agency Internal Audit Function section titled Efforts and Accomplishments on page 12.

Staffing Analysis

The Council's staffing analysis is a cursory review to identify the minimal number of internal audit positions needed, not the optimal. A more extensive review must be conducted to determine the optimal number of positions need in each internal audit function. The fiscal year 2017 analysis identified 24 agencies under the minimal number of internal auditors needed to address risk within their agencies. Positions needed to get all agencies to the minimal number is 52.50 positions at a cost⁴ just under \$5 million. Details of the specific staffing recommendations can be seen in Appendix B.

Institute of Internal Auditors Government Group Membership

The purpose of the program is to broaden internal audit knowledge by providing a membership reduction rate. Some benefits of a membership include free and discounted continuing education development and professional publications; enhanced networking; and exclusive on-line resource materials. The Council staff has worked with the IIA to establish the North Carolina Government Group membership program that starts October 1 and ends September 30 of each year. Any government employee can join this group and receive a discount on an IIA membership. On October 1, 2016, the program registered 170 individuals and throughout the year, added 30 additional individuals allowing for a 43% reduction of the membership rate.

Proposed Legislation Changes

The Council of Internal Auditing did not sponsor changes related to the Internal Audit Act during the 2016-2017 Legislative Session.

⁴ Annual cost of a position includes: Salary and Benefits – \$91,200; and operating cost of \$3,800.

STATE AGENCY INTERNAL AUDIT FUNCTIONS

Audit Resources

There are 48 agencies subject to the Internal Audit Act. Different models are used to establish an internal audit function from in-house staffing to outsourcing the entire function. Below is information on internal audit positions, contractor use and supplemental staffing via intern or temporary employees.

As shown in Table 3 on the next page, there are 196.25 internal auditor positions, which are spread across 36 state agencies. As of June 30, 2017, 84% of these positions were filled. There was a net gain of 5.75 positions throughout the state over the past year. Significant changes over the last year include:

- The UNC Health Care System gained three positions;
- UNC Chapel Hill gained .75 position; and
- Three “one-person” functions, Department of the Secretary of State, Community College System Office and University of North Carolina General Administration each gained one position.

Agencies under \$70 million in operating funds can use OSBM as their internal audit function. During fiscal year 2017, eight agencies used OSBM services instead of having an in-house internal audit function. The Department of Military and Veterans Affairs is the only agency that is above the required threshold but uses OSBM due to a lack of resources. Agencies serviced by OSBM during FY2016-17 are:

- Commissioner of Banks;
- Department of Labor;
- Department of Military and Veterans Affairs;
- North Carolina Industrial Commission;
- Office of State Budget and Management;
- Office of State Human Resources;
- Office of the Governor; and
- Office of the State Auditor.

The following agencies outsource their internal audit function:

- North Carolina School of the Arts contracts with Winston-Salem State University for audit services;
- North Carolina School of Science and Mathematics contracts with the University of North Carolina General Administration;
- North Carolina State Education Assistance Authority contracts with the University of North Carolina General Administration;
- Fayetteville State University contracts with an individual; and
- Housing Finance Agency contracts with Cherry Bekaert.

Table 3

Statewide Internal Auditor Position Level Comparison FY2013 to FY2017					
	2017	2016	2015	2014	2013
Community College System Office	2	1	1	1	1
Commissioner of Banks ¹	0	0	0	0	0
Department of Administration	1	1	1	1	0
Department of Agriculture & Consumer Services	4	4	3	3	3
Department of Commerce	4	4	4	5	4
Department of Natural and Cultural Resources	2	2	2	1	1
Department of Environmental Quality	2	2	4	3	3
Department of Health & Human Services	41	41	43	39	15
Department of Information Technology	3	3	3	3	2
Department of Insurance	1	1	1	1	1
Department of Justice	1	1	1	1	1
Department of Labor ¹	0	0	0	0	0
Department of Military and Veterans Affairs ¹	0	0	N/A	N/A	N/A
Department of Public Instruction	2	2	2	2	1
Department of Public Safety	20	20	19	20	20
Department of Revenue	3	3	3	3	2
Department of Secretary of State	2	1	2	2	2
Department of State Treasurer	3	3	3	3	4
Department of Transportation	25	25	25	22	22
Housing Finance Agency ²	0	1	1	2	2
North Carolina Education Lottery	3	3	3	2	2
North Carolina Industrial Commission ¹	0	0	0	0	0
Office of State Controller	0.5	0.5	0.5	0.5	0
Office of State Human Resources ¹	0	0	0	0	0
Office of State Budget & Management ¹	5	5	5	4.5	6
Office of the Governor ¹	0	0	0	0	0
Office of the State Auditor ¹	0	0	0	0	0
Wildlife Resources Commission	1	1	1	1	0
Appalachian State University	5	5	5	5	5
East Carolina University	8	8	8	7	7
Elizabeth City State University	1	1	1	1	1
Fayetteville State University ²	0	0	1	0	1
North Carolina Agricultural & Technical State University	4	4	4	4	5
North Carolina Central University	4	4	3	3.5	3
North Carolina School of Science and Mathematics ⁴	0	0	0	0	0
North Carolina School of the Arts ³	0	0	0	0	0
North Carolina State Education Assistance Authority ⁴	0	0	N/A	N/A	N/A
North Carolina State University	7	7	8	7	7
University of North Carolina - Asheville	1	1	1	1	1
University of North Carolina - Chapel Hill	7.75	7	7	7	6
University of North Carolina - Charlotte	5	5	5	5	5
University of North Carolina - General Administration	2	1	1	1	1
University of North Carolina - Greensboro	2	2	2	2	2
University of North Carolina - Health Care System	12	9	10	8	6
University of North Carolina - Pembroke	2	2	1	1	1
University of North Carolina - Wilmington	4	4	4	4	4
Western Carolina University	1	1	1	1	1
Winston-Salem State University	5	5	5	5	3
Total	196.25	190.50	194.50	182.50	151.00
1. Utilizes OSBM Internal Audit program					
2. Uses contract auditors					
3. Contracts with Winston-Salem State University					
4. Contracts with UNC-General Administration					

Agencies continue efforts to supplement staffing levels which include: developing of a State Term internal audit supplemental staffing convenience contract; establishing intern programs; hiring temporary employees and using guest auditors⁵. Over the past year, 19 agencies have utilized these alternative methods to address resource limitations as shown in Table 4.

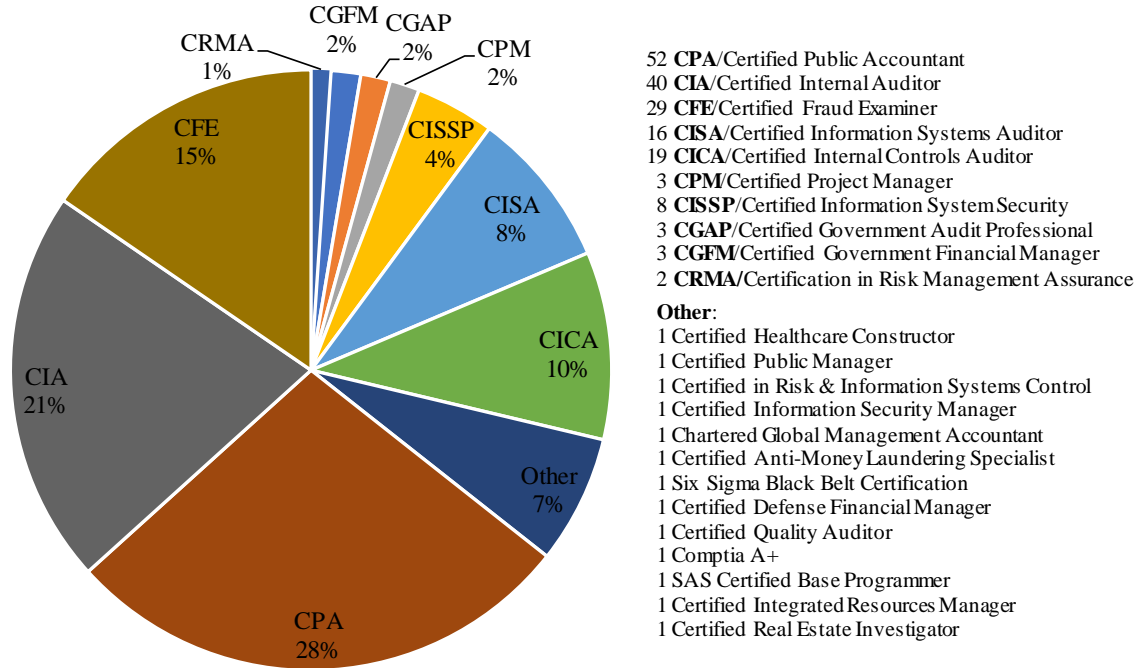
Table 4 Supplemental Staffing Efforts				
Agency	State Term Contract	Interns	Temporary Employees	Guest Auditors
Department of Commerce		✓		
Department of Health & Human Services	✓	✓		
Department of Information Technology		✓		
Department of Public Instruction	✓		✓	
Department of Secretary of State		✓		
Department of Transportation	✓		✓	
Office of State Budget & Management	✓	✓	✓	
East Carolina University		✓		
North Carolina Agricultural & 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 - Health Care System		✓		
University of North Carolina - Pembroke		✓		
University of North Carolina - Wilmington		✓		
Western Carolina University		✓		
Total	4	14	5	1

Personnel Proficiency

Internal auditors can demonstrate proficiency by obtaining professional certifications and advanced degrees. Overall, internal auditors hold 188 professional certifications in 23 different areas; an increase of 13% over last year. Eighty-three percent of the designations held by agency's internal auditors are in five of the 23 areas which are: Certified Public Accountants; Certified Internal Auditors; Certified Information Systems Auditors; Certified Internal Control Auditor; and Certified Fraud Examiners. A breakdown of all designation held by agency's internal auditors is shown in Chart 1, on the next page.

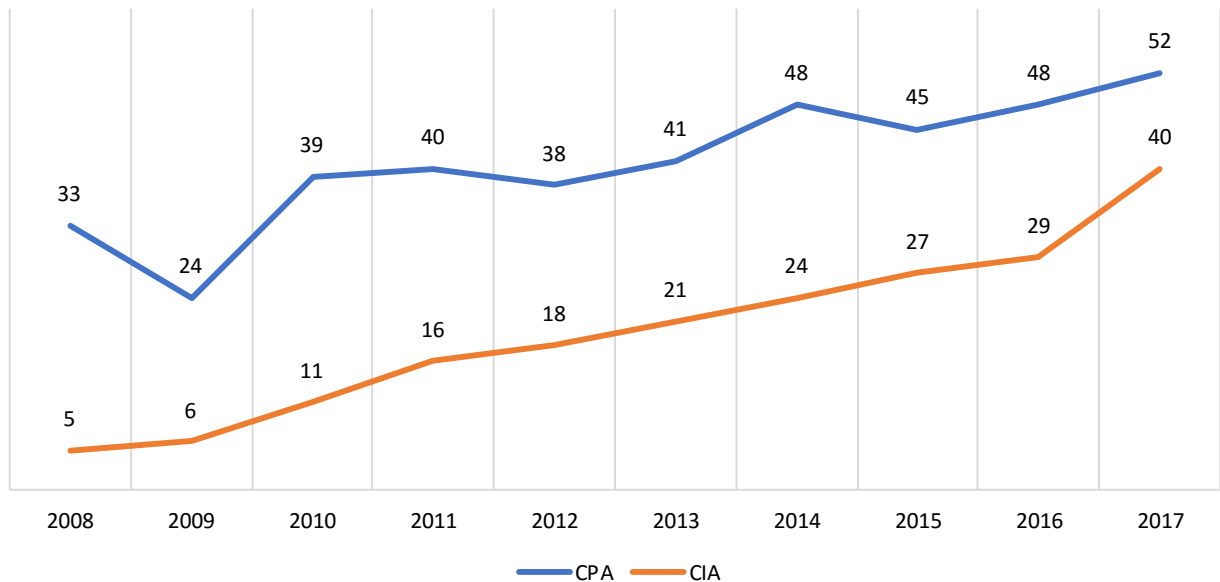
⁵ A guest auditor operates as a subject matter expert providing additional insight on the audit approach and/or interpretation of results.

Chart 1: FY2016-17 Professional Certification



Over the last ten years, professional certifications held by internal auditors increased 224%, from 58 to 188 certifications, while staffing levels increased by 35%. Chart 2 provides a historical view of the top two certifications held by internal auditors. In the last year, the number of internal auditors that hold the CIA designation increased by 38%.

Chart 2: 10-Year Growth Top Two Certifications Held by Internal Auditors



Along with the increases in professional certifications, advanced degrees held by internal auditors had a modest increase of 3% over the last year; however, over a ten-year period there has been a 200% increase, as shown in Chart 3 on the next page.

**Chart 3: Growth from FY2008 to FY2017
Advanced Degrees Held by Internal Auditors**

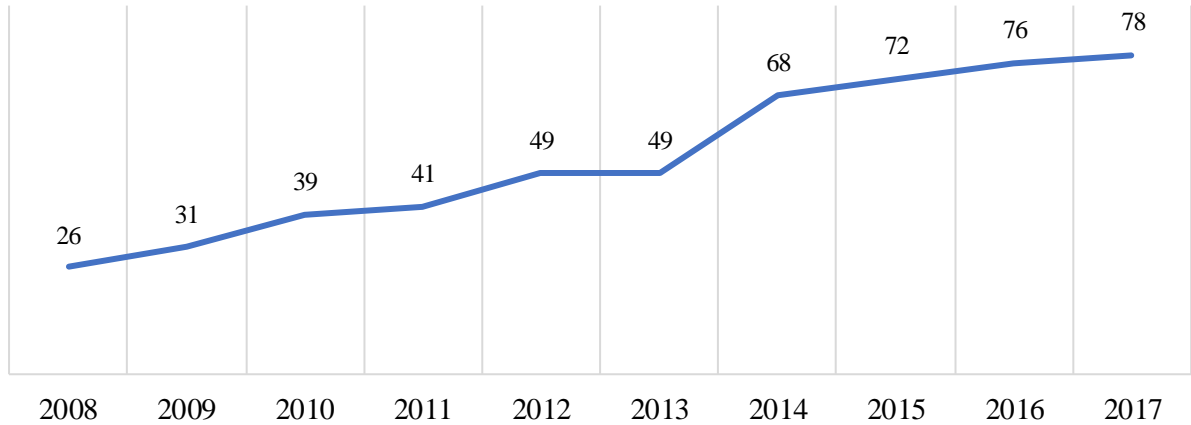
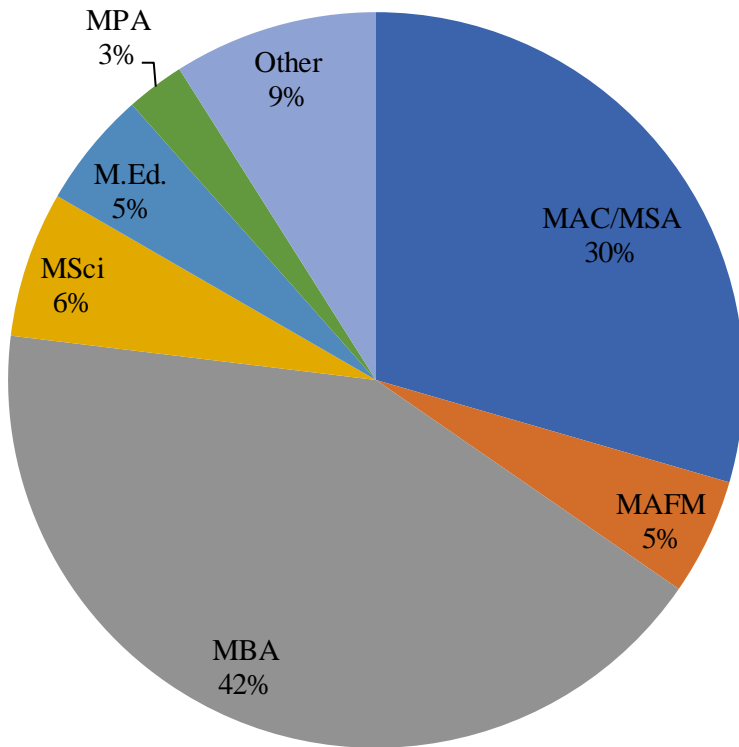


Chart 4, shows the type of advanced degrees held by the agency’s internal auditors during fiscal year 2017. Auditors hold 78 advanced degrees with 77% of these being Masters in Business Administration, Accounting or Accounting and Finance Management.

Chart 4: Advanced Degrees



- 33 **MBA**/Master of Business Administration
- 23 **MAC**/Master of Accounting & **MSA**/Master of Science Accountancy
- 5 **MSc**i./Master of Science
- 4 **MAFM**/Master of Accounting & Financial Management
- 4 **M.Ed.**/Master of Education
- 2 **MPA**/Master of Public Administration
- Other:**
 - 1 Master of Information Systems
 - 1 Juris Doctorate
 - 1 Master of Science Information Assurance
 - 1 Master of Art Organizational Management
 - 1 Master of Science in Management
 - 1 Master of Economic
 - 1 Master of Bible Studies

Computer Assisted Audit Tools

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 spreadsheets, 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, such as Teammate and SharePoint, aid with the administration and management of the audit processes. Generalized audit software tools, such as ACL and IDEA, assist with data extraction, analytics and testing.

Table 5 identifies the types of CAAT products used throughout State government and the number of internal audit functions using these products during fiscal year 2017. East Carolina University; Department of Health and Human Services; and Department of Commerce, Division of Employment Services employ more the one type of generalized audit software.

Department of State Treasurer; Department of Health and Human Services; and Department of Transportation use more than one productivity tools to automate work papers and work flow processes.

Table 5

Computer Assisted Audit Tools			
Generalized Audit Software		Productivity Tool	
Software	Number Agencies Using	Software	Number Agencies Using
ACL	10	SharePoint	10
IDEA	4	Teammate	3
Tableau	4	Auto Audit	3
Active Data	3	Auditor Assistant	1
SAS	1		
Truven	1		
QuickBooks	1		
TLO	1		
EnCase	1		
Total	26	Total	17

A 5-year historic view shows growth in the use of CAATs as shown in Chart 5.

Chart 5: Use of CAAT

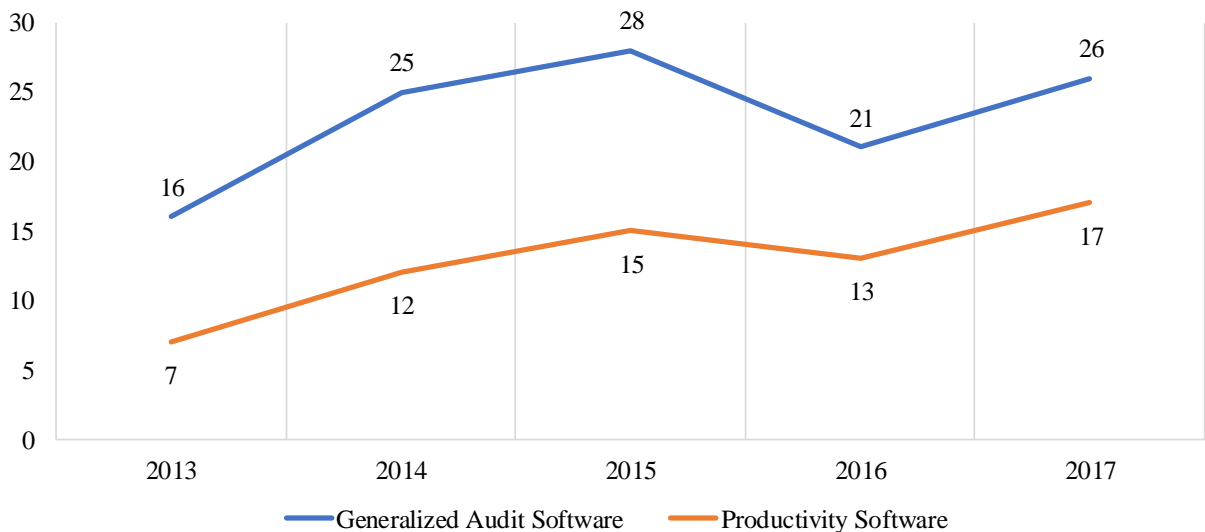


Table 6, on the next page, shows all internal audit functions use Microsoft Office products to enhance productivity through automation and which agencies employ the use of other CAAT products.

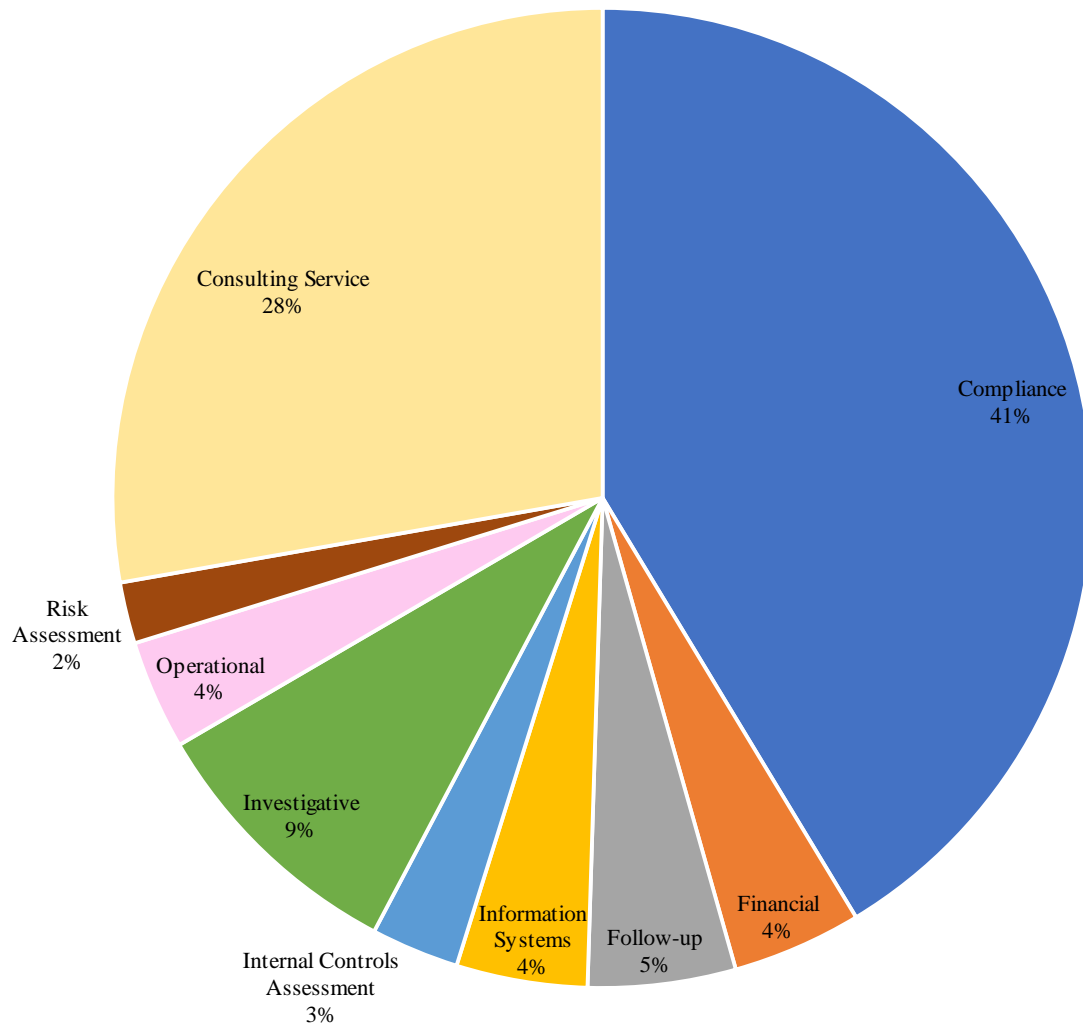
Table 6

Computer Assisted Audit Tool Usage			
State Agency	Microsoft Office Products	Generalized Audit Software¹	Productivity Tool²
Community College Central Office	✓		
Department of Administration	✓		
Department of Agriculture & Consumer Services	✓	✓	✓
Department of Commerce	✓	✓	✓
Department of Natural and Cultural Resources	✓		
Department of Environmental Quality	✓		✓
Department of Health and Human Services	✓	✓	✓
Department of Information Technology	✓	✓	
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	✓	✓	
North Carolina Education Lottery	✓	✓	✓
Office of State Budget & Management	✓	✓	
Office of the State Controller	✓		✓
Wildlife Resource Commission	✓		
Appalachian State University	✓		
East Carolina University	✓	✓	
Elizabeth City State University	✓		
Fayetteville State University	✓		
North Carolina Agricultural & 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 - Hospitals	✓	✓	✓
University of North Carolina - Pembroke	✓		
University of North Carolina - Wilmington	✓	✓	✓
Western Carolina University	✓	✓	
Winston-Salem State University	✓	✓	✓
1. Perform routine audit tasks including data extract, analytics, and testing.			
2. Streamline processes to manage audits through electronic work papers and work flows.			

Efforts and Accomplishments

Internal audit functions conduct various activities designed to add value and improve a state agency's operations. From July 1, 2016 through June 30, 2017, more compliance audits were completed when compared to other internal audit engagements. Chart 6 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, internal auditors provided over 21,600 hours of assistance to their agency's management which did not result in report issuance.

Chart 6: FY2017 Engagements



The audit engagements by state agency are shown in Table 7 on the next two pages. The Table depicts the efforts of each internal audit function. Efforts are directly related to the size of the audit function and the complexity of the engagement. There are many state agencies that have one or two internal auditors which limits the number of audits that can be accomplished throughout the year.

Table 7 (Continued on next page)

Agency Engagements											
Agency	Compliance	Financial	Follow-up	Information Systems	Internal Controls Assessment	Investigative	Operational/Performance	Risk Assessment	Consulting Service	Total Reports	Technical Assistance Hours
Community College System Office					1					1	320
Department of Administration	1				1				1	3	100
Department of Agriculture and Consumer Services	2		2			11	3		3	21	44
Department of Commerce - DES	5	18		2		8	3	3	134	173	67
Department of Natural and Cultural Resources					5	1				6	240
Department of Environmental Quality	2	1	2			2	1	1		9	600
Department of Health and Human Services	68	8	5	23		20	5	1	230	360	240
Department of Information Technology		7		20		5	4			36	1,560
Department of Insurance	1		1			1	3	1	2	9	120
Department of Justice		1	6				1	1		9	38
Department of Public Instruction					1	5		1	2	9	388
Department of Public Safety	30	21	2			10				63	12
Department of Revenue	3		1		2		4			10	800
Department of Secretary of State					1					1	12
Department of State Treasurer					1		5		5	11	250
Department of Transportation	556		2			23		1	76	658	2,000
North Carolina Education Lottery	11			1	3		2	2		19	800
North Carolina Housing Finance Agency				1	1			1		3	40
Office of State Budget and Management	1		8	9	4	9	4	8	13	56	463
Office of the State Controller										0	40
Wildlife Resources Commission					1				5	6	1,000

Table 7 (Continued from previous page)

Agency Engagements (continued from previous page)											
Agency	Compliance	Financial	Follow-up	Information Systems	Internal Controls Assessment	Investigative	Operational Performance	Risk Assessment	Consulting Service	Total Reports	Technical Assistance Hours
Appalachian State University	2	5	8	9	21	5	2	1		53	483
East Carolina University	2		10	2		11	8	1	3	37	3,271
Elizabeth City State University						4	1	1	1	7	284
Fayetteville State University					1	2	1			4	18
North Carolina Agricultural & Technical State University	1	3	2		1	3				10	1,068
North Carolina School of Science and Math			1				1	1		3	176
North Carolina School of the Arts				1		1		1	2	5	276
North Carolina State Education & Assistance Authority								1		1	91
North Carolina Central University	6		5	1	1	5	5		2	25	100
North Carolina State University	1		11		2	11		3	11	39	3,705
UNC Asheville					1			1		2	222
UNC Chapel Hill			2			10		1		13	33
UNC Charlotte	3						8			11	92
UNC General Administration	1		1			4		1		7	135
UNC Greensboro	5	1			1			1		8	40
UNC Health Care	7	12		8		2	2		8	39	60
UNC Pembroke					1	2		1	1	5	912
UNC Wilmington	3	1	6	2	1	4	3	1		21	731
Western Carolina University	44		13		1	1		1		60	55
Winston-Salem State University			1		1	2		1	8	13	807

Compliance

Internal Audit Act and Council Requirements

The Internal Audit Act and the North Carolina Internal Audit Manual require internal audit functions to submit their annual audit plan by September 30 of each year and engagement reports as completed. All Internal Audit Functions conformed with these requirements throughout the year.

External Quality Assurance Review (Peer Review)

To comply with audit standards, external quality assurance reviews (QAR) are required every five years. QARs for six internal audit functions are not due until a future date, as shown in Table 8.

Table 8

Agencies Pending External QAR	
Agency	Due Date
Office of the State Controller	December 2018
Department of Information Technology	February 2019
Housing Finance Agency	April 2019
Department of Administration	May 2019
Wildlife Resource Commission	November 2019
State Education Assistance Authority	September 2022

Of the 35 internal audit functions remaining, all have received a QAR and only one did not receive the generally conforms rating⁶. The Department of the Secretary of State received a partially conforms opinion on their last QAR. The agency hired a new Internal Audit Director in February 2017. The new Internal Audit Director must develop policies and procedures and conduct audit engagements before requesting a QAR. The tentative target date to request a follow up QAR is June 2018.

⁶ Generally Conforms with the *Internal Professional Practice Framework* is the highest rating that can be received for an external quality assurance review.

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APPENDIX A
NORTH CAROLINA INTERNAL AUDIT ACT

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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, the President of the Community College System, the State Controller, and other independent appointed officers with authority over a State agency. The agency head for the Department of Public Instruction shall be the State Board of Education.
 - (2) "State agency" means each department created pursuant to Chapter 143A or 143B of the General Statutes, and includes all institutions, boards, commissions, authorities, by whatever name, that is a unit of the executive branch of State government, including The University of North Carolina, and the Community Colleges System Office. The term does not include a unit of local government.
- (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; 2009-516, s. 2; 2013-406, s. 1.)

§ 143-746. Internal auditing required.

- (a) Requirements. - A State agency shall establish a program of internal auditing that:
 - (1) Promotes an effective system of internal controls that safeguards public funds and assets and minimizes incidences of fraud, waste, and abuse.
 - (2) 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. 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 State employee who performs the internal audit function shall meet the minimum qualifications for internal auditors established by the Office of State Human Resources, in consultation with the Council of Internal Auditing.
- (d) Director of Internal Auditing. - The agency head shall appoint a Director of Internal Auditing who shall report to, as designated by the agency head, (i) the agency 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 to avoid impairments to independence as defined in the auditing standards referenced in subsection (b) of this section.
- (e) If a State agency has insufficient personnel to comply with this section, the Office of State Budget and Management shall provide technical assistance. (2007-424, s. 1; 2013-382, s. 9.1(c); 2013-406, 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 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. (2007-424, s. 1; 2013-406, s. 1.)

§ 143-748. Confidentiality of internal audit work papers.

Internal audit work papers are confidential except as otherwise provided in this section or upon subpoena issued by a duly authorized court. A published internal audit report is a public record as defined in G.S. 132-1 to the extent it does not include information which is confidential under State or federal law or would compromise the security of a State agency. An internal auditor shall maintain for 10 years a complete file of all audit reports and reports of other examinations, investigations, surveys, and reviews conducted under the internal auditor's authority. Audit work papers and other evidence and related supportive material directly pertaining to the work of the internal auditor's office shall be retained in accordance with Chapter 132 of the General Statutes. Unless otherwise prohibited by law and to promote intergovernmental cooperation and avoid unnecessary duplication of audit effort, audit work papers related to released audit reports shall be made available for inspection by duly authorized representatives of the State and federal government in connection with some matter officially before them. (2013-406, s. 1.)

§ 143-749. Obstruction of audit.

It shall be a Class 2 misdemeanor for any officer, employee, or agent of a State agency subject to the provisions of this Article to willfully make or cause to be made to a State agency internal auditor or the internal auditor's designated representatives any false, misleading, or unfounded report for the purpose of interfering with the performance of any audit, special review, or investigation or to hinder or obstruct the State agency internal auditor or the internal auditor's designated representatives in the performance of their duties. (2013-406, s. 1.)

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APPENDIX B
STAFFING RECOMMENDATIONS

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**Internal Audit Staffing Analysis and Recommendation for Minimal Staff Level
As of June 30, 2017**

Agency	Current Positions	Minimal Positions Needed	Recommended New Positions	Estimated Cost of New Positions
Administrative Office of the Courts	4.00	6.00	2.00	190,000
Department of Administration	1.00	3.00	2.00	190,000
Department of Commerce	4.00	11.00	7.00	665,000
Department of Natural and Cultural Resources	2.00	3.00	1.00	95,000
Department of Environment Quality	2.00	3.00	1.00	95,000
Department of Insurance	1.00	2.00	1.00	95,000
Department of Justice	1.00	2.00	1.00	95,000
Department of Military and Veterans Affairs ¹	-	2.00	2.00	190,000
Department of Public Instruction	2.00	8.00	6.00	570,000
Department of State Treasurer	3.00	13.00	10.00	950,000
North Carolina Education Lottery	3.00	6.00	3.00	285,000
North Carolina Housing Finance Agency ^{3, 5}	-	2.00	2.00	190,000
Office of State Budget and Management ¹	5.00	6.00	1.00	95,000
Office of State Controller ⁵	0.50	2.00	1.50	142,500
Wildlife Resources Commission	1.00	2.00	1.00	95,000
Elizabeth City State University ⁵	1.00	2.00	1.00	95,000
Fayetteville State University ³	-	2.00	2.00	190,000
North Carolina State University	7.00	8.00	1.00	95,000
University of North Health Care System	12.00	14.00	2.00	190,000
University of North Carolina-Asheville	1.00	2.00	1.00	95,000
University of North Carolina-Chapel Hill	7.75	9.00	1.00	95,000
University of North Carolina-Greensboro	2.00	3.00	1.00	95,000
University of North Carolina-General Administration ²	2.00	3.00	1.00	95,000
Western Carolina University	1.00	2.00	1.00	95,000
Grand Total			52.50	4,987,500

Agencies at or above Minimum, Using Contractors or Using Shared Pool	
Department of Agriculture and Consumer Services	4.00
Department of Health and Human Services	41.00
Department of Information Technology	3.00
Department of Public Safety	20.00
Department of Revenue	3.00
Department of Secretary of State ⁵	2.00
Department of Transportation	25.00
North Carolina Community College Central Office	2.00
Appalachian State University	5.00
East Carolina University	8.00
North Carolina A&T State University	4.00
North Carolina Central University	4.00
University of North Carolina-Charlotte	5.00
University of North Carolina-Pembroke	2.00
University of North Carolina-Wilmington	4.00
Winston-Salem State University ⁴	5.00
North Carolina School of Science & Math	Contracting
North Carolina School of the Arts	Contracting
North Carolina State Education Assistance Authority	Contracting
Commissioner of Banks	Shared Pool
Department of Labor	Shared Pool
Office of State Auditor	Shared Pool
Office of State Human Resources	Shared Pool
Office of the Governor	Shared Pool
State Board of Elections	Shared Pool

1. Provides internal audit services to agencies under \$70 million expenditures; Shared Pool agencies listed above. Department of Military and Veteran's Affairs receives service; however, they are not included in OSBM calculation.
2. Provides internal audit services to North Carolina School for Science and Mathematics and NC State Education Assistance Authority which was considered in the calculation.
3. Outsourced internal audit services.
4. Provides internal audit services to North Carolina School for the Arts which was considered in the calculation.
5. Agencies under \$70 million operating may use OSBM internal audit services instead established an in-house internal audit function.