



State of North Carolina Office of the State Controller

Michael F. Easley, Governor

Robert L. Powell, State Controller

September 9, 2004

Memorandum No. OSC-ADMIN-0003

TO: Agency Department Heads
University Chancellors
Community College Presidents

FROM: Robert L. Powell, State Controller

SUBJECT: Internal Control Compliance Reviews

As you know, the Office of the State Controller (OSC) is statutorily responsible for establishing internal control standards that define the minimum level of quality acceptable for internal control systems. North Carolina General Statute (NCGS) §143B-426.39 establishes the State Controller's statutory responsibility for internal control standards. Over the past several months, we have informed you that OSC is planning to launch a new statewide initiative to proactively monitor compliance with prescribed internal control policies. The purpose of this memorandum is to inform you that we will commence these reviews beginning in early October 2004.

It is important to note that these reviews are not audits and should not be considered as a duplication or substitution of the audit work performed by the Office of the State Auditor. OSC has worked closely with the Office of the State Auditor to ensure that our efforts "dove-tail" with their work.

These reviews are intended to proactively assist management with assessing their risk tolerance through the identification of existing or potential internal control weaknesses within their operations. They are also intended to provide an educational opportunity for raising awareness across state government of the vital importance of appropriate internal controls and to educate entity personnel on internal control best practices. These reviews will not monitor or assess all internal control cycles; they will spot check various internal control cycles. The goal of these reviews is to improve the fiscal management of our state agencies, institutions and entities. OSC will identify both the functional areas and the state entities at greatest potential risk for internal control failure.

In order to achieve optimal efficiency and maximum value from its available resources, OSC will select a representative sample of several state entities to be reviewed. The primary factors to be considered when making these selections are:

- 1) risk and materiality;
- 2) personnel changes in senior management and other key fiscal positions;
- 3) recurring deficiencies cited in reports issued by the State Auditor; and,
- 4) any other issues identified by OSC staff, as well as other external bodies.

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Our reviews will generally begin with the Self-Assessment of Internal Control Questionnaire (ICQ) that each state entity is required to complete or update annually, and will document agency compliance with OSC policies and procedures. During the internal control compliance reviews, various internal control cycles, as defined in the ICQ, will be selected for detailed follow-up – to be performed by executing a series of pre-defined procedures, referred to as a compliance review work program. This compliance review work program will be used at each state entity being reviewed and will provide a consistent step-by-step approach for validating assertions relative to the entity's internal control systems.

State entities selected for review will receive a notification letter at least two weeks prior to the commencement of our on-site compliance review. We anticipate, depending on the size of the agency, that these reviews will generally be short term – usually lasting three weeks or less in duration. Upon completion of the review, findings and recommendations will be discussed with management. OSC may perform periodic follow-up to ensure that corrective actions have been taken.

We remain excited about the challenges and opportunities resulting from this initiative and will continue to keep you posted on any new developments. If you have any questions regarding these reviews, please contact Ben McLawhorn, Risk Mitigation Services Manager, at (919) 981-5409.

cc: Chief Fiscal Officers
Vice Chancellors
Business Managers