

STATE OF NORTH CAROLINA

OFFICE OF THE STATE AUDITOR

BETH A. WOOD, CPA

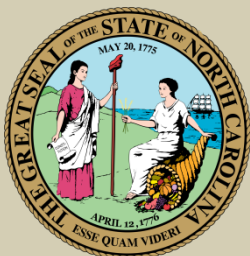


LINCOLN COUNTY CLERK OF SUPERIOR COURT

LINCOLN, NORTH CAROLINA

FINANCIAL RELATED AUDIT

JULY 2019



NCOSA
The Taxpayers' Watchdog

STATE OF NORTH CAROLINA
Office of the State Auditor



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AUDITOR'S TRANSMITTAL

The Honorable Roy Cooper, Governor
The General Assembly of North Carolina
The Honorable Fred R. Hatley, Lincoln County Clerk of Superior Court

This report presents the results of our financial related audit at Lincoln County Clerk of Superior Court. Our work was performed by authority of Article 5A of Chapter 147 of the *North Carolina General Statutes* and was conducted in accordance with the performance audit standards contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

The results of our audit identified deficiencies in internal control and instances of noncompliance that are considered reportable under *Government Auditing Standards*. These items are described in the *Audit Findings and Recommendations* section of this report.

North Carolina General Statutes require the State Auditor to make audit reports available to the public. Copies of audit reports issued by the Office of the State Auditor may be obtained through one of the options listed in the back of this report.

A handwritten signature in cursive script that reads "Beth A. Wood".

Beth A. Wood, CPA
State Auditor



Beth A. Wood, CPA
State Auditor

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Article V, Chapter 147 of the *North Carolina General Statutes*, gives the Auditor broad powers to examine all books, records, files, papers, documents, and financial affairs of every state agency and any organization that receives public funding. The Auditor also has the power to summon people to produce records and to answer questions under oath.

As authorized by Article 5A of Chapter 147 of the *North Carolina General Statutes*, we have conducted a financial related audit at Lincoln County Clerk of Superior Court. There were no special circumstances that caused us to conduct the audit, but rather it was performed as part of our effort to periodically examine and report on the financial practices of state agencies and institutions.

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

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

The general objective of this financial related audit was to identify improvements needed in internal control over selected fiscal matters. Management is responsible for establishing and maintaining effective internal control. Internal control is a process designed to provide reasonable assurance that relevant objectives are achieved. Errors or fraud may nevertheless occur and not be detected because of the inherent limitations of internal control. Also, projections of any evaluation of internal control to future periods are subject to the risk that conditions may change or that compliance with policies and procedures may deteriorate. Our audit does not provide a basis for rendering an opinion on internal control, and consequently, we have not issued such an opinion.

Our audit scope covered the period July 1, 2018 through February 28, 2019. During our audit, we considered internal control related to the following objectives:

Cash – The Clerk’s Office collects various fines, fees, and court costs daily, as well as collections for bonds, judgments, and other matters. We examined internal controls designed to ensure that the Clerk properly safeguards and accounts for cash receipts. We also examined internal controls designed to ensure compliance with laws and regulations related to depositing cash receipts. During the audit period, the Clerk collected \$5,270,257 in cash.

Estates – The Clerk’s Office ensures all estates are charged an application fee plus an assessment based on the value of the estate’s inventory. An estate inventory is to be filed by the representative of the estate. We examined internal controls designed to ensure that the Clerk properly obtains an inventory for each estate in compliance with laws and regulations. We also examined internal controls designed to ensure compliance with laws and regulations related to the appropriate assessment and collection of estate fees. During the audit period, the Clerk collected \$120,206 in estate fees.

The Clerk’s Office ensures that all estate guardians are properly bonded based on the value of the annual estate inventory. An annual estate inventory is to be filed by the estate guardian of a minor or incapacitated adult. We examined internal controls designed to ensure that the Clerk properly obtains an inventory for each guardianship in compliance with laws and regulations. We also examined internal controls designed to ensure that bonds assessed and collected are sufficient and in compliance with laws and regulations. During the audit period, auditors examined \$4,652,463 in estate guardian bonds retained by the Clerk.

Escheats – The Clerk’s Office transfers abandoned property to the State. The transfer results when the person legally entitled to the property fails to make a valid claim on the property within a prescribed period of time. After that time, all abandoned property held by the Clerk is required to be transferred to the North Carolina Department of State Treasurer. We examined internal controls designed to ensure that the Clerk properly identifies escheatable funds. We also examined internal controls designed to ensure compliance with laws and regulations related to escheating unclaimed funds after a prescribed period of time. During the audit period, the Clerk transferred \$115,673 in escheats to the State Treasurer.

Trusts – The Clerk’s Office receives, administers, and disburses trust funds for minors and incapacitated adults. We examined internal controls designed to ensure that disbursements from minor and incapacitated adult trust accounts are proper to ensure compliance with laws and regulations. As of February 28, 2019, the Clerk had \$938,662 in trust accounts.

To accomplish the audit objectives, auditors gained an understanding of the Clerk's internal control over matters described in the *Audit Objectives and Scope* section of this report and evaluated the design of the internal control. Auditors then performed further audit procedures consisting of tests of control effectiveness and/or substantive procedures that provide evidence about our audit objectives. Specifically, auditors interviewed personnel, observed operations, reviewed policies, analyzed accounting records, and examined documentation supporting recorded transactions and balances, as considered necessary in the circumstances. Whenever sampling was used, we applied a nonstatistical approach, but chose sample sizes comparable to those that would have been determined statistically. As a result, we were able to project our results to the population as applicable but not quantify the sampling risk. This approach was determined to adequately support audit conclusions.

As a basis for evaluating internal control, we applied the internal control guidance contained in professional auditing standards. As discussed in the standards, internal control consists of five interrelated components: (1) control environment, (2) risk assessment, (3) control activities, (4) information and communication, and (5) monitoring.

We conducted this audit in accordance with the performance audit standards contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

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

Government Auditing Standards require that we add explanatory comments to the report whenever we disagree with an audit finding response or when planned corrective actions do not adequately address the recommendation. In accordance with this requirement and to ensure that the nature and seriousness of the finding is not minimized or misrepresented, we have provided comments to the Clerk's response when appropriate.

1. IMPROPER SYSTEM ACCESS INCREASED RISK OF UNDETECTED ERRORS AND FRAUD

Staff in the Clerk's Office had the ability to change information in multiple systems, resulting in inadequate segregation of duties. The Clerk's Office handled \$5,270,257 in receipts during the audit period July 2018 to February 2019.

Specifically, one out of 23 (4%) employees had inappropriate access to the Financial Management System (FMS) and the Criminal Court Information System (CCIS). The employee had both cashier rights in FMS and update access in CCIS. As a result, the employee could have potentially misappropriated funds by collecting cash from a criminal payment, bypassing receipt entry into FMS, and updating CCIS to indicate all costs have been paid.

Additionally, a magistrate who is not an employee of the Clerk's Office, had inappropriate access to the Civil Case Processing System (VCAP). This access allowed the magistrate to update civil case information.

Improper segregation of duties increased the risk that errors, unauthorized transactions, and fraud could go undetected. While no fraud was identified during the audit period, an increased risk of undetected fraud existed because access rights and duties were not properly segregated.

According to the Clerk, he was not aware that the cashier had update access in CCIS. Furthermore, the Clerk granted VCAP access to the magistrate for advanced printing of the small claims docket prior to printing by the Clerk's Office.

Adequate segregation of duties is required by the *Clerk of Superior Court Financial Policies and Procedures Manual*. Proper segregation of duties involves assigning duties and access to assets and information systems so that one employee's duties automatically provide a cross-check of the work of other employees.

As a result of our audit, the Clerk revoked the inappropriate access rights for the individuals in question. The access deficiencies were corrected as of April 9, 2019.

Recommendation: The Clerk should monitor all assignments of system access rights to ensure consistency with proper segregation of duties in accordance with the *Clerk of Superior Court Financial Policies and Procedures Manual*. Additionally, the Clerk should ensure assignments are restricted to clerk employees who need access to perform their duties. If it is not practical to segregate all incompatible duties, then effective monitoring procedures should be implemented to reduce the risk of errors or fraud.

Clerk's Response: See page 9 for the Clerk's response to this finding.

2. FAILURE TO PROPERLY CALCULATE OR COLLECT ESTATE INVENTORY FEES

The Clerk's Office did not accurately assess or collect estate inventory fees in accordance with state law. The Clerk's Office collected \$120,206 in estate fees during the audit period July 2018 to February 2019.

Auditors examined 65 of 200 estates in the audit period in which a final inventory was filed. Fees totaling \$360 for 13 (20%) estates were not accurately assessed or collected when the final inventory was filed. Specifically,

- For seven (11%) estates, fees were not accurately assessed, resulting in the Clerk's Office collecting \$127 more than required.
- For six (9%) estates, fees totaling \$233 were not collected when the final inventory was filed. Also, there was no evidence in the file to support fee collection attempts.

As a result, there were delays and potential for loss in the collection of estate costs and fees.

According to the Clerk, the failure to accurately assess and collect the fees resulted from a lack of proper review and audit of the files before finalizing.

North Carolina General Statute 7A-307(a)(2) requires the Clerk to assess and collect the estate fees at the time the final inventory is filed.

Recommendation: The Clerk should implement effective monitoring procedures, such as a secondary review of fee calculations for accuracy. The Clerk should also document efforts to identify, track, and compel the collection of outstanding fees.

Clerk's Response: See page 9 for the Clerk's response to this finding.

3. FAILURE TO IDENTIFY AND TRANSFER UNCLAIMED FUNDS TO THE STATE TREASURER

The Clerk's Office did not identify and transfer unclaimed funds to the North Carolina Department of State Treasurer (Treasurer) in accordance with state law.

Auditors examined the February 2019 aging report¹ for items held over one year and identified 194 unclaimed items totaling \$1,597,538. Fifty-three (27%) items totaling \$52,830 remained on deposit with the Clerk as of the time of our audit that should have been transferred to the Treasurer during the periods 2011-2018.

As a result, the return of unclaimed funds to the rightful owners has been delayed. Additionally, there is a potential loss of earnings on the Unclaimed Property Fund, or Escheats Fund. A loss of Escheats Fund earnings reduces the amount of funds available for transfer to the North Carolina State Education Assistance Authority.²

¹ The monthly aging report reflects all case level account funds being held by the Clerk and the amount of time the funds have remained in the Clerk's office without any activity.

² The State Education Assistance Authority provides loans and grants to worthy and needy North Carolina students attending state-supported colleges and universities.

According to the Clerk, the bookkeeper was new to the position and had minimal training in 2018 when the preparation and submission of escheats to the Treasurer were performed.

*North Carolina General Statutes*³ and the *North Carolina Clerk of Superior Court Escheats Manual*⁴ require the Clerk's Office to:

- Review monthly aging reports to identify funds that should be disbursed to the rightful owners or escheated.
- Determine that unclaimed funds are eligible for delivery to the Treasurer and transfer those funds at the appropriate time.

Recommendation: The Clerk should ensure responsible employees receive proper training. The Clerk should also implement effective monitoring procedures over the escheat process, such as a periodic review of aging reports.

Clerk's Response: See page 9 for the Clerk's response to this finding.

³ NCGS 116B-53(c) and 116B-60(d)

⁴ Sections C1 and C2

STATE AUDITOR'S RESPONSE

The Office of the State Auditor (OSA) is required to provide additional explanation when an agency's response could potentially cloud an issue, **mislead the reader**, or inappropriately minimize the importance of auditor findings.

Generally Accepted Government Auditing Standards state,

"When the audited entity's comments are inconsistent or in conflict with the findings, conclusions, or recommendations in the draft report, or when planned corrective actions do not adequately address the auditor's recommendations, the auditors should evaluate the validity of the audited entity's comments. If the auditors disagree with the comments, they should explain in the report their reasons for disagreement."

Therefore, OSA offers the following clarifications for finding number 2:

FAILURE TO PROPERLY CALCULATE OR COLLECT ESTATE INVENTORY FEES

The Clerk's response misleads the reader about the cause of the finding and does not provide for sufficient corrective action. The Clerk states:

"This change in collecting Inventory Fees was not noticed in any of my E-mails. I will be more attentive when changes occur."

The Clerk's response is misleading because it implies the cause of the errors were only due to changes in the estate fee amounts. However, as stated in the finding, the cause of the finding was the lack of proper review and audit of the files before finalizing. A proper review and audit of the files prior to finalizing would have caught the fee changes, as well as calculation errors.

In addition, the corrective action stated by the Clerk does not address the auditor's recommendation. Effective monitoring procedures should be implemented by the Clerk to ensure that estate inventory fees are accurately assessed and collected, including any outstanding fees.



FRED HATLEY
CLERK OF SUPERIOR COURT
EX OFFICIO JUDGE OF PROBATE

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IMPROPER SYSTEM ACCESS INCREASED RISK OF UNDETECTED ERRORS AND FRAUD

Recommendation: The Clerk should monitor all assignments of system access rights to ensure consistency with proper segregation of duties in accordance with the *Clerk of Superior Court Financial Policies and Procedures Manual*. Additionally, the Clerk should ensure assignments are restricted to clerk employees who need access to perform their duties. If it is not practical to segregate all incompatible duties, then effective monitoring procedures should be implemented to reduce the risk of errors or fraud.

Response: This was corrected as soon as it was brought to my attention. I will be more aware of the notices I receive from Security.

FAILURE TO PROPERLY CALCULATE OR COLLECT ESTATE INVENTORY FEES

Recommendation: The Clerk should implement effective monitoring procedures, such as a secondary review of fee calculations for accuracy. The Clerk should also document efforts to identify, track, and compel the collection of outstanding fees.

Response: This change in collecting Inventory Fees was not noticed in any of my E-mails. I will be more attentive when changes occur.

FAILURE TO IDENTIFY AND TRANSFER UNCLAIMED FUNDS TO THE STATE TREASURER

Recommendation: The Clerk should ensure responsible employees receive proper training. The Clerk should also implement effective monitoring procedures over the escheat process, such as a periodic review of aging reports.

Response: This happened when our Bookkeeper was near retirement and her replacement was learning the Escheat process. Our new Bookkeeper is well aware of this problem and it will not happen again.



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This audit was conducted in 208 hours at an approximate cost of \$21,437.